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I. INTRODUCTION

Nearly every community in the United States is now within reasonable proximity to an airport which provides commercial air transportation services. Since the 1950s the Nation has grown to rely more and more on this system of airports to conduct important business, social, governmental, and educational activities. And, vital to many regions and the Nation is the contribution airports and aviation activity make to the economy.
A recent study suggested the economic activity associated with civil aviation in the United States exceeds $500 billion annually.

But, this national system of interconnecting, economically-beneficial airports is controlled almost exclusively by very independent units of local government. While many of these governments receive adequate to very handsome rewards for their participation in the national aviation system, they encounter intergovernmental, land use, and budgetary forces which detract from a vigorous promotion of airport services. For almost three decades now this locally-controlled, national system has been criticized by air travelers, business leaders, airlines, airport neighbors, and elected officials, as inefficient and unfair.

The purpose of this research was to review this locally-owned, national system of commercial airports and determine:
- whether there was public and private sector accountability commensurate with the importance of airports to the Nation; and
- if there was an adequate level of planning, meaning the development of goals, policies, and procedures, to meet the long term requirements of the Nation's air transport segment.

Such a review is timely since the Bush Administration has now adopted a "national transportation policy," including the announced intention to improve airport capacity within the Nation. Many were surprised, however, that the Administration's policy seemed to back even further away from a strong federal role in solving the Nation's complex transportation infrastructure problems. Unfortunately, the Administration's position is fairly consistent with previous federal neglect of the airport system in the United States. Because of past and present neglect, the federal government has come under increasing pressure from the aviation industry to accept more responsibility and ensure better planning for the Nation's airports. Others have criticized commercial air carriers for failing to become more involved in solving the many airport problems. The conflicts and differences of opinion over airport policy in the United States seem to have grown more pronounced.

DEREGULATION AND ITS AFTERMATH

In 1978 the United States Congress passed legislation leading to the demise of the Civil Aeronautics Board, and eliminating federal regulatory controls over air carrier routes and air fares. During the next decade the competitive practices of the deregulated aviation industry, along with a strong national economy, combined to double commercial air passenger activity. The result was congestion and delays, especially during peak-hour travel times, at many limited-capacity, urban airports.

Of concern to many during this period has been the absence of increased cooperation among the airport operators, the airlines, the local
governments, and the federal government, each having control over different solutions to the capacity problem. Such cooperation, of course, is necessary not only to keep traffic flowing at particular airports, but to assure that costly congestion and delay at one airport does not have a ripple effect at other airports within the national system. Some argue this latter fact calls for special federal intervention.

The Federal Aviation Administration, which was left with the primary federal responsibility for air commerce after deregulation, responded to this system capacity crisis by targeting improvements in its air traffic control operation. But the long range solutions to national system capacity problems require additional actions, such as real estate acquisition, land use and environmental planning, economic incentives, and regulatory controls. The Federal Aviation Administration, however, has played a very minor role in these and other non-air traffic control alternatives.

THE AIRPORT PROPRIETOR’S WEB

PRESSURE FROM NOISE IMPACTED HOMEOWNERS

The surge in air traffic became troublesome for airport proprietors who have found themselves standing alone to answer homeowners worried about increases in noise levels and reduced property values. Some airports have responded by adopting “curfews” or other restrictions on airport use to appease their neighbors. But, such restrictions can limit an airport’s capacity, compounding the problem of satisfying the growing demands within the national system. The air carriers, in particular, have complained about airport use restrictions, and called on the federal government to curb them.

AIRPORTS AS SOLELY LIABLE FOR NOISE INJURIES SUFFERED BY NEIGHBORS

One reason behind the airports’ ability to unilaterally restrict the use of airport facilities arises from the legal remedy available to noise-impacted landowners. That remedy makes airport proprietors solely liable for any injury caused by aircraft noise. But, this rule of law is inconsistent with the realities of diverse public and private sector decision making which combine to impact airport neighbors. Nevertheless, these other decision makers, including air carriers, local governments, and the federal government, have been content to avoid liability by: acknowledging the preeminent role of airport proprietors; and avoiding actions which might be interpreted as a sharing or preempting of the airports’ authority.
VERY DIVERSE PUBLIC AND PRIVATE SECTOR OBJECTIVES CAUSE PROBLEMS FOR LONG RANGE AIRPORT DECISION MAKING

Notwithstanding this reluctance to become legally accountable for airport noise, these other actors have competing interests causing them to complain about or subtly undercut some airport proprietor decisions. Air carriers, for example, are concerned about corporate profits and have used their economic power to influence airport facility construction and noise-related use restriction actions which are inconsistent with company planning. Also, local governments which benefit from the tax revenues of new development often ignore airport-requested prohibitions against residential construction in high noise exposure zones. Or, local governments may operate their own airports and use political leverage to oppose the expansion of another government's airport which might compete for revenues.

SPLIT OR NON-EXISTENT POLITICAL ACCOUNTABILITY FOR AIRPORT-RELATED DECISIONS

Of course, part of the problem is that political responsibility for decisions affecting airports is fragmented. While the states or the federal government could step in and orchestrate cooperation and compromise, they have been reluctant to do so. Among the reasons for such hesitation are: the intent to avoid legal liability; concepts of federalism or state prerogatives; and the perception that airport matters are "land use" decisions which historically are locally-made.

AIRPORT PROPRIETORS AS POOR LONG RANGE PLANNERS AND RESOLVERS OF "LAND USE" CONFLICTS

But if airports are both legally and politically accountable for important long range airport decisions, and for resolving local "land use" conflicts, studies indicate many are poor planners and community conflict negotiators. Ideally airports which are part of the national air transportation system should dedicate significant funding and personnel resources to the following functions:

• understanding and tracking community land use and transportation planning and decisions;
• credible data collection and forecasting of airport activity in support of airport-related construction and noise compatibility plans;
• effective communication with, and education of, the public and elected officials at all levels of government; and
• establishing close working relationship between airport and community fiscal, legal, and real estate professionals.

Of course, any failure of airports to commit local resources to such functions is partly understandable. If budgets are constrained airport decision
makers may prioritize funds to satisfy needs which are more immediate and local. And, even if an airport has an exceptional vision of its long term, national status, it may conclude that the power of its opponents is sufficient to undermine most airport plans.

**COMPETING FAA INTERESTS**

While federal statutes give the Federal Aviation Administration some responsibilities for airports planning, and land use/community conflict resolution, the same laws state the Agency may not interfere with airport "proprietary powers and rights." Additionally, airport matters must compete for FAA resources with the agency’s aircraft safety and air traffic control missions. These and the obligations to commercial air carriers, the Office of Management and Budget, and the Defense Department, frequently restrict the FAA’s interest in airport problems.

**AIRCRAFT NOISE REDUCTION**

For two decades the FAA has had the statutory responsibility to prescribe standards and regulations to control and abate aircraft noise. Given the Agency’s experience with aircraft certification, the FAA has published regulations requiring air carriers to use aircraft engines which are quieter than those used twenty years ago. While these regulations have been an important step in reducing noise levels around airports, many complain that the FAA should adopt a stricter, more comprehensive noise control program. The Agency’s failure to adopt such measures underscores the competing forces which influence FAA decision making. Reasons for the Agency’s failure to take more aggressive action include: economic impacts on air carriers; intrusions into perceived local government prerogatives; erosion of air traffic controller’s discretionary authority over flight operations near airports; and impacts on the federal budget.

**AIRPORT VICINITY LAND USE PLANNING**

Beginning in the early 1960s studies of federal airport policy recommended a greater FAA role in promoting compatible land uses in the vicinity of airports. Unfortunately, the Agency was only marginally involved in local land use planning until 1979, when Congress directed the FAA to establish a program to measure airport noise exposure levels and to assist airports in developing noise compatibility initiatives. Since that date the Agency has published federal guidelines for airport noise control and land use compatibility planning, and has administered federal grants to encourage such efforts. But, many have criticized the FAA for setting up a good program on paper, but then not training or participating with airports in the development of plans. Also, the FAA has not made clear the national interests requiring consideration during such planning. The ab-
sence of federal representation during planning, and the lack of defined federal standards, leads to controversy when the FAA later exercises its authority to disapprove some or all of the locally-negotiated actions. The FAA's failure to provide resources for training and agency participation in planning is linked: to federal concerns about disrupting local "proprietary" functions; to federal deficit reduction measures; and to the perceived priority needs of air traffic control.

 MANAGEMENT OF AIRSPACE NEAR AIRPORTS

As flight corridors to and from airports have become congested in the last decade, the FAA has sought to increase the number of such routes to enhance system capacity. But, such changes create noise over previously quiet neighborhoods. In many cases the residents of these areas become politically active in fighting the intrusion. Because of diverse governmental accountability, and fragmented responsibility for community issues within the FAA, the early identification and resolution of these concerns have been poor. Because of congressional pressure the Agency is now taking a hard look at its planning and management structure to improve communications with local governments. But, such improvements are difficult to accomplish because of: budget constraints; air traffic controllers' prerogatives; and local "proprietary" rights.

 PLANNING FOR A NATIONAL SYSTEM OF AIRPORTS

Since 1946 Congress has directed the regular publication of a plan for a national system of airports. Conceptually, such a plan should: be based on credible airport activity forecasts; clearly define federal interests in airports; and prioritized actions to assure airport services for the Nation. But, the biannual plan published by the FAA has been heavily criticized for accomplishing none of these. While the Agency's document lists airport projects desired by individual airports and some state agencies, there is little analytical work accompanying the cataloguing. While numerous pressures influence FAA's plan, two of the most important are: the Office of Management and Budget's opposition to any plan which could be used to demand increases in federal expenditures; and the potential for opposition from congressmen whose districts might lose federal grant funds due to a reordering of national priorities.

 LAND ASSEMBLY TO MEET FUTURE AIRPORT REQUIREMENTS

In a 1977 report to Congress the FAA stated that the acquisition of significant real property interests was vital to ensure future airport system capacity. Fortunately, some land has been made available through the closure of obsolete military bases, or through the joint military/civil use of existing bases. Also, a few communities have had the foresight to
purchase or hang onto additional property for future airport needs. But, these events have occurred, and continue to occur, without much FAA leadership. Today the need for more airport land continues to grow much faster than the ad hoc response to the problem. Nevertheless, the FAA has relative few employees responsible for assisting airports acquire land, nor does the Agency have specific goals for land assembly needed for the national system. Again, the FAA's failure to dedicate resources to this purpose can be traced back to the deference for "proprietary" rights, and to emphasis from other forces within the Agency.

These conditions cause many citizens to perceive the nation's air transportation system as a craft without a pilot: an ad hoc, leaderless association of governments, planes, land, and runways. Most previous efforts to attack the problems associated with the Nation's airports have narrowly focused on specific economic, legal, social, or governmental issues without taking a comprehensive view of the whole. The first two chapters here attempt such a panoramic view, though in almost outline form.

But, any changes in the status quo are not likely to occur until all private and public sector airport-related interests agree on certain root problems. Naturally, the selection of such roots runs the risk, once again, of ignoring the diversity and complexity of the puzzle. Nevertheless, this paper concludes that the root issues are all closely associated with problems of accountability and planning.

Given the decades of division over how to approach airport issues, it is assumed that such root problems must be paired up with bold leadership in order to change the status quo. Anticipating the needs of such leadership, this paper concludes with proposed airport policy principles for public debate, and recommended actions to improve accountability and planning.

AIRPORT POLICY PRINCIPLES

POLICY PRINCIPLE ONE: \textbf{SINCE AIRPORT PROBLEMS CANNOT BE SOLVED BY A SINGLE INSTITUTION OR GOVERNMENT AUTHORITY, ALL AFFECTED GROUPS MUST ACTIVELY COOPERATE IN FORMULATING AND SUPPORTING ACTIONS TO INCREASE FAIRNESS, EFFICIENCY, AND ACCOUNTABILITY.}

POLICY PRINCIPLE TWO: \textbf{SINCE AIRPORTS IN THE UNITED STATES OPERATE UNDER A CITIZEN FRANCHISE REQUIRING PUBLIC CONFIDENCE, ALL AIRPORT DECISION MAKERS MUST ACTIVELY ACCOUNT FOR PUBLIC CONCERNS IN PLANNING AND IMPLEMENTATION.}

POLICY PRINCIPLE THREE: \textbf{AVIATION INDUSTRY GROUPS AND VARIOUS LEVELS OF GOVERNMENT ARE ALL RESPONSIBLE FOR RESOLVING DIS-}
PUTES OVER AIRPORT NOISE, INCLUDING PROVIDING “JUST COMPENSATION” TO PROPERTY OWNERS AND BALANCING THE MANY GENERAL WELFARE NEEDS TIED TO AIRPORTS.

POLICY PRINCIPLE FOUR: THERE ARE CERTAIN AIRPORT-RELATED ISSUES OF NATIONAL CONCERN WHICH MUST BE CLEARLY DEFINED AND ACCEPTED.

POLICY PRINCIPLE FIVE: ASSUMING THAT THE FAILURE TO CONTROL INCOMPATIBLE LAND USES ON AND IN THE VICINITY OF AIRPORTS HARM BOTH PUBLIC AND PRIVATE INTERESTS, SUBSTANTIVE AND PROCEDURAL STANDARDS FOR AIRPORT AREA LAND USE PLANNING CAN REDUCE INCONSISTENCY, INEQUITY, AND INEFFICIENCY.

POLICY PRINCIPLE SIX: PUBLIC ACQUISITION AND EFFECTIVE MANAGEMENT OF AIRPORT REAL PROPERTY INTERESTS ARE ESSENTIAL FOR THE LONG RANGE NEEDS OF AVIATION IN THE UNITED STATES.

POLICY PRINCIPLE SEVEN: IF LIABILITY FOR INJURY CAUSED BY AIRCRAFT NOISE WAS SHARED BY THOSE PRIVATE AND PUBLIC INTERESTS INVOLVED IN AVIATION ACTIVITY AND AIRPORT VICINITY LAND USE CONTROL, SOME OF THE BARRIERS TO COOPERATIVE AIRPORT DECISION MAKING COULD BE REMOVED.

POLICY PRINCIPLE EIGHT: IMPORTANT ACHIEVEMENTS IN AIRPORT DECISION MAKING WILL NOT OCCUR WITHOUT TALENTED AND COMMITTED LEADERS FROM THE PUBLIC AND PRIVATE SECTOR.

CONGRESS RECOMMENDATIONS

CONGRESS RECOMMENDATION ONE: AMEND FEDERAL AVIATION LAW TO MORE CLEARLY DEFINE AIRPORT “PROPRIETARY POWERS AND RIGHTS” TO PREVENT THE FEDERAL AVIATION ADMINISTRATION FROM GIVING UNDUE DEFERENCE TO AIRPORT PROPRIETORS WHEN INTERSTATE AIR COMMERCE INTERESTS ARE AT STAKE.

CONGRESS RECOMMENDATION TWO: TAKE ACTION TO SPREAD THE LEGAL LIABILITY FOR AIRCRAFT NOISE INJURIES AMONG BOTH PUBLIC AND PRIVATE SECTOR INTERESTS WHICH ARE RESPONSIBLE FOR THE CONTROL OF AIRCRAFT NOISE OR OF THE PHYSICAL ENVIRONMENT THROUGH WHICH THE NOISE EMANATES.

CONGRESS RECOMMENDATION THREE: ACT TO INCREASE THE PARTICIPATION AND ACCOUNTABILITY OF AIRCRAFT OPERATORS, AND LOCAL GOVERNMENTS HAVING JURISDICTION OVER AIRPORT VICINITY LAND USE CONTROL IN NOISE COMPATIBILITY AND NATIONAL AIR TRANSPORTATION SYSTEM PLANNING.
DEPARTMENT OF TRANSPORTATION RECOMMENDATIONS

DOT Recommendation One: In close consultation with the diverse airport interest groups, develop procedures and the format for a national airport system plan which will serve as the primary airport policy and long range planning document for the nation.

DOT Recommendation Two: Establish a national airport real property acquisition program with specific goals including: the identification and prioritization of long range national airport system real property requirements; the training of airport proprietors in the planning and acquisition of real property interests for aircraft noise abatement and future aeronautical purposes; and the increased use of available federal property for national air transportation system purposes.

DOT Recommendation Three: After studying federal and state land use control initiatives (such as floodplains, coastal zones, and so forth), adopt appropriate federal procedures, standards, and incentives to reduce incompatible development in the vicinity of nation system airports.

DOT Recommendation Four: Ensure that the FAA airport services manpower is adequate to regularly participate with airport proprietors in negotiating individual noise compatibility and capacity enhancement agreements.

DOT Recommendation Five: Evaluate the need for more community relations, real estate, and urban planning professionals within the national air transportation system; and adopt appropriate budget initiatives to integrate such skills into federal aviation administration and airport proprietor education, planning, and decision making.

II. AIRPORTS IN THEIR INSTITUTIONAL SETTING

A. Aviation Activity and Airports are Important to United States Economic, Social, and International Policy

1. Rapid Air Transport of People and Goods Affects the Economic Well-Being, Health, and Welfare of the Nation

The United States has about 6,000 public-use airports serving nearly all cities and small communities in the nation. Connecting these

1. There are 2.3 million acres in the United States dedicated to airport use. H. Frey & R.
airports is a network of air routes, defined by navigational aids, which channel the flow of approximately 3,600 commercial and 220,000 general aviation aircraft. Flights along these routes, as well as operations in the vicinity of airports, are monitored and controlled by a system of ground-based surveillance equipment and communication links.2

For the past three decades this system has experienced an exponential growth in commercial transportation activity.3 Daily enplanements of passengers at U.S. airports have increased from 50,000 passengers each day in 1950 to over one million passenger enplanements daily today.4 In 1987, among public modes of long distance transport, aviation accounted for more passenger miles than all other modes combined.5 The increased reliance on air transportation is also illustrated by the fact that seventy-three percent (or 130 million) of the adult U.S. population have flown at some time in their life on an airplane, up from forty-nine percent in 1971.6

Matching this growth is the significant impact of aviation and related economic activity on the United States. In 1987, economic activity associated with aviation totalled $522 billion7 and employed 8 million people or 7.3% of the workforce.8

In addition to such economic impact, air transportation has caused changes in American institutional and personal conduct. During the last two decades, American business, governmental, scientific, technological,
and educational institutions have come to rely on rapid travel, face-to-face meetings, and direct supervision in the execution of their responsibilities. Goods of all kinds—mail, bank checks, medical supplies, farm produce, machine parts—often travel by air.⁹

Air transportation can promote economies of scale, increase efficiency, and further specialization. It has increased competition among producers by expanding the area in which a product can be economically distributed. Such competition leads to lower prices and a wider choice of products for consumers.

Air transportation has also changed personal choice, offering alternative selections of medical care, schooling, places of recreation, and cultural enrichment.

Of course, these benefits are offset with the economic and social "costs" of air transport. Aviation activity produces accidents which result in loss of life and property. Also, aircraft annoy with noise, consume sizeable parcels of land, and use large amounts of fuel. In addition, legal and political disputes can clog courts and legislative chambers.

Such factors as the increasing reliance on air transportation, and the economic and social impacts of aviation, arguably demand national-level attention. In fact, considerable national debate and federal resources are committed to aviation-related matters, particularly aircraft safety. However, important questions continue to be raised whether the federal government has fully shouldered its national leadership responsibilities. This is especially true when the discussion turns to the federal government's accountability for and planning of a national air transportation system.

2. **AIRPORTS HAVE BECOME INDISPENSIBLE PARTS OF CITIES THROUGHOUT THE UNITED STATES**

Of the 6,000 U.S. airports, about 4,200 are owned by local governments including cities, towns, counties, port authorities, airport authorities, and special districts.¹⁰ This local ownership and responsibility for airports has been welcomed by communities because of the significant

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⁹ For a typical manufacturing firm, transportation expenses rank third in dollar outlays, behind direct materials and direct labor. For a large company this can mean hundreds of millions of dollars annually. Naturally, with such sums at stake, integrating transportation planning with other company activities and understanding transportation options is very important. In selecting a transportation mode a shipper will consider rate differences, and differences in service, routings, speed, reliability, packaging requirements, and the likelihood of loss or damage. R. Lieb, Transportation: The Shipper's Perspective 17-30 (1985).

¹⁰ Of the 980 airports in 1918 many were privately-owned golf courses, racetracks, or farms. M. Greif, The Airport Book: From Landing Field to Modern Terminal 25-26 (1979). Local governments moved in large numbers into airport ownership after World War II when surplus military airfields became available and the federal government made grants available for
economic benefits\textsuperscript{11} associated with airport activity.\textsuperscript{12} Also, for many communities an efficient\textsuperscript{13} airport can promote civic pride\textsuperscript{14} and consti-

airport land acquisition, and the construction of runways, taxiways, and aprons. FAA, THE AIR-


Nearly every state has an airport enabling act which authorizes subdivisions of the state to
acquire, improve, maintain and operate airports for public use. In the sponsorship of these air-
ports local governments may use both the state's eminent domain and police power. In the opera-
tion of airports, local governments are recognized as being engaged in a proprietary activ-
ity, with the responsibility to operate it as efficiently as a private proprietor would. In their respon-
sibility for airports a unit of local government typically establishes rules/regulations in the
following areas: tenant agreements and obligations; aircraft operating rules; environmental re-
lated requirements; compatible land use development; parking; public conduct; emergencies;
and safety and security. C. RHYNE, AIRPORTS AND THE LAW 1-8 (1979); H. WOLFE & D.
NEWMYER, AVIATION INDUSTRY REGULATION 79 (1985).

11. An airport's economic impact on a community is determined by adding airline and air-
port employee payroll, local purchases of supplies and services, capital expenditures, payments
to government, expenditures for flight crew room rentals, and aviation visitor expenditures. Stud-
ies have shown thatvisitors who arrive in a community through an airport will spend considerably
more money in the community than the visitor who arrives by other transportation. GENERAL
AVIATION MANUFACTURER ASS'N, HOW TO LAND AND EXPAND AN AIRPORT IN YOUR COMMUNITY 2
(1976). \textit{See also}, S. BUTLER & KIERNAN, MEASURING THE REGIONAL ECONOMIC SIGNIFICANCE OF
AIRPORTS (FAA Report No. DOT/FAA/PP/87-1 (1986)); AIRPORTS AND AIRWAYS, supra note 4 at
111-12; PUBLIC WORKS HISTORICAL SOC'Y, supra note 5, at 38. Typically, such studies do not
measure net economic impacts, which would include the cost of lost land value and similar
losses due to environmental conditions. AIRPORT OPERATORS COUNCIL INT'L, MARKETING HANDBOOK
18-19 (1989); H. MERTINS, NATIONAL TRANSPORTATION POLICY IN TRANSITION 119-21
(1972).

A prime example of airport economic impact is the Atlanta Hartsfield Airport. With over
33,000 employees, the airport is the largest single employer in the state with a $1 billion annual
payroll and $3.5 billion annually in local purchases. In 1985, 85\% of the Fortune Magazine 500
companies had offices in the area. Carter, A Commissioner Looks at "His" Airport, AIRPORT
FORUM, June 1985, at 38. Other airports reporting significant economic impacts are: Tulsa's $1
billion, Curtis, Local Aviation Officials See Blue Skies Ahead, TULSA BUS. CHRONICLE, July 5,
1988, at 7; Chicago's $9 billion, AIR TRANSPORT ASS'N, CHICAGO AND THE AIRLINES (Apr. 1987);
St. Louis $2 billion, AIR TRANSPORT ASS'N, LAMBERT ST. LOUIS INTERNATIONAL AIRPORT (Oct.
1986); Nashville's $500 million, Harris, New Airport a White Jewel, ADVANTAGE, July 1987, at 26;
Beatrice (Nebraska)'s $119 million, Worthington, Pilot "Roll Book" Reveals Airport's Monetary
Impact, AIRPORT SERVICES, Sept. 1986, at 12; Tucson's $863 million, Economic Impact, AIRPORT
HIGHLIGHTS, Nov. 28, 1988, at 8. For an excellent article on the impact of aviation in the State of
Alaska see Fried, Air Biggest Transport Segment, ALA. J. COM., July 18, 1988, at 8 (discusses
impact of deregulation, international air traffic, relations with the Soviet Union, changes in fleet
size, air cargo).

Recently, some communities have become concerned that their long-term economic well-
being may be impaired if they cannot provide increased airport services. Stewart, Logan Air-
port's Grim Date with 2010, Boston Globe, May 9, 1989, Economy sec. at 29; Thompson, The
Triad's Fight for Flight, BUS. NORTH CAROLINA, Mar. 1989, § 1, at 52.

12. Like ports and harbors, the federal government has recognized the local government
responsibility for airports. But, just as the federal government provided safe, navigable chan-
nels, the federal government has taken responsibility for the maintenance of safe airways.

13. The need for quality community infrastructure, including transportation public works, is
well recognized. Kaplan, \textit{Infrastructure Policy: Repetitive Studies, Uneven Response, Next}
Steps, 25 URB. AFF. Q. 371 (1990); Rosenberg & Rood, \textit{The Realities of Our Infrastructure Prob-
tute a "geographical anchor" for necessary aviation transportation. Because of their size and related activity, airports have a very important impact on land use within communities. The reasons for this influence are several:

- The use by the airport of large tracts of buildable acreage in urban settings where land is at a premium.
- An airport spawns numerous off-site activities which consume and control additional property.
- Airports typically influence development patterns in the vicinity of the airport.
- An airport's impact on the physical environment can be significant.
- An airport is usually served by extensive roadway systems and other public utility infrastructure.

Also, airports can provide important government services, such as support for natural disasters, law enforcement, life saving and rescue, forest fire fighting, and air national guard/armed services training.

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1. Fried, supra note 11, at 8.
2. Fried, supra note 11, at 13.
3. Fried, supra note 11, at 5.
4. Fried, supra note 11, at 6.
5. Fried, supra note 11, at 17.
7. Fried, supra note 11, at 8.
10. Fried, supra note 11, at 25.
11. Fried, supra note 11, at 8.
13. Fried, supra note 11, at 5.
14. Fried, supra note 11, at 8.
15. Fried, supra note 11, at 8.
16. Fried, supra note 11, at 8.
17. Fried, supra note 11, at 8.
The significance and diversity of aviation activity impacts within a community mean that extraordinary attention must be given by local elected officials, business leaders, and residents to the airport and its operation. It is not enough merely to turn all aviation-related matters over to an able airport manager. Those communities which, in the short term, fail to integrate such issues into local planning and decision making, can expect increased costs later on in retaining adequate airport services.

Also, there are questions about the role of the local leadership in the national air transportation system. Do they have any responsibility to safeguard the federal government’s substantial capital investment in airport land and infrastructure? To what extent are local government officers accountable for the expansion of airport capacity to meet future demand, when such actions are unwanted by airport neighbors?

3. United States Aviation Activity is Important for the Nation’s Status Within the International Community

Beyond their local and national importance, airports play a role in international commercial activity. Today, the United States enjoys a significant advantage in international air transport, giving the domestic market strong access to the world-wide market. Unlike most nations which have only one “gateway” airport, the United States has many. Through the exchange of landing rights between United States and foreign airports, the U.S. has obtained a favored position in foreign markets. Also, the U.S. decision to deregulate its airline industry in 1978 gave a competitive edge over foreign regulated airlines.

The nature and complexity of the United States’ role in international aviation goes beyond the scope of this discussion. But, the same themes of accountability, planning, and leadership are assumed to apply in evaluating the nation’s success or failure in the increasingly competitive world community.

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18. International trade is an important consideration in deciding the amount of public works services required by a nation. Since World War II, the U.S. economy has become increasingly more integrated into, and dependent on, the world market. Contributing to this U.S. dependence has been the substantial reduction in import tariffs in all the major trading nations and the increasing multinational character of business. A recent U.S. Dep’t of Commerce study forecasts a major surge in international activity in the mid-1990’s, to the benefit of those countries which can transport goods and services rapidly at reasonable costs. OFFICE OF ECONOMIC AFFAIRS, U.S. DEP’T OF COMMERCE, EFFECTS OF STRUCTURAL CHANGE ON THE U.S. ECONOMY ON THE USE OF PUBLIC WORKS SERVICES, ch. 2 (Project No. PW 7-625, July 30, 1987).


B. CONDITIONS ARISING SINCE THE DEREGULATION OF U.S. AIRLINES
AGGRAVATED EXISTING PHYSICAL CAPACITY AND INSTITUTIONAL
ACCOUNTABILITY WEAKNESSES IN THE NATIONAL AIR
TRANSPORTATION SYSTEM

1. A SURGE IN AIR TRAFFIC DURING THE LAST DECADE, ALONG WITH
HUBBING AND SCHEDULING PRACTICES OF COMMERCIAL
AIRLINES, HAS INCREASED DEMAND ON THE AVIATION
INFRASTRUCTURE

Prior to the deregulation of the U.S. airline industry in 1978,21 the
Civil Aeronautics Board (CAB) assigned routes to commercial aircraft,
thereby controlling the demand on the air transportation infrastructure.22
The CAB also regulated the pricing of air transport services. Once these
controls were abolished, the airlines adopted practices in an effort to in­
crease their respective market share. Among the most important industry
changes were hubbing, competitive scheduling of flights, and reduced air
fares.

The idea of concentrating operations in a few hub airports was prac­
ticed before deregulation, but became much more common in the height­
ened competitive environment.23 The prime purpose for hubbing is to
allow an airline to increase the frequency24 of operation. The economics
of commercial aviation have shown that an airline which can increase its
frequency of service can boost its proportional market share. Airlines can
improve their frequency by routing passengers through fewer routes, us­
ing hub airports.25 The conversion to a more intense hubbing system,
however, has placed a great burden on the infrastructure of these major

21. R. DE NEUFVILLE, DEREGULATION OF AIR TRANSPORT—LESSONS FROM NORTH AMERICA
   (1986).
22. Before deregulation communities often got involved in promoting ticket sales to retain
   needed routes into their cities and towns. A 1960 publication of the National Association of State
   Aviation Officials suggested forty ways to promote community use of the airport. R. REDDING,
   COMMUNITY PLANNING FOR AIR TRANSPORTATION (1960).
23. R. DE NEUFVILLE, supra note 21; A. GHOBRIAL, ANALYSIS OF THE AIR NETWORK STRUC­
   TURE: THE HUBBING PHENOMENON (1983); Morrison & Winston, InterCity Transportation Route
   Structures under Deregulation: Some Assessments Motivated by the Airline Experience, AM.
   ECON. REV., May 1985, at 57.
24. A. GHOBRIAL, supra note 23, at 17-20 (1983). Of course, an airline is constrained from
   engaging in excessive frequency competition by the need to maintain profitable load factors.
   Load factors within the 60 to 65 percent range seem to be the breakeven range. Id. at 39.
25. There are about 30 large hubs in the United States. Fawcett & Fawcett, Congestion at
   Capacity-Constrained Airports: A Question of Economics and Realism, TRAN. J., Summer 1988,
   manuscript available from the Forecast Branch, Headquarters, FAA). Additional communities
   continue to plan and market their airports to attract hub business. Benmour & Kamuf, Airport
   Plan May Help Lure Hub, BUS. FIRST—LOUISVILLE, June 27, 1988, § 1, at 1. But, the creation of
   new hubs may have peaked. Kyle, Hoping to be a Hub, GOVERNING, Apr. 1988, at 48; Proctor,
Air carriers also recognized that their market share would depend on the ability to satisfy passenger preferences for travel times. Consequently, airlines tightly scheduled their flights into specific time windows to assure the best competitive situation. As a result many airports experience "peak hour" pressures when many planes and passengers converge on the terminals.

Along with hubbing and scheduling practices, the airlines lowered capacity constraints will influence fleet composition through 2010, Aviation Week & Space Tech., Nov. 21, 1988, at 87.


A disadvantage of hubbing and congestion at a few airports is the ability of the dominant carriers to take strategic actions that undercut smaller rivals. Such an oligopoly situation or competitive barriers have led some to label the major airports "fortress hubs." Airlines defend their hubbing practices by arguing that it allows them to use planes more efficiently and therefore give passengers better fares and service. See Borenstein, Airline Merger, Airport Dominance, and Market Power, 80 Am. Econ. Rev. 400 (1990); Feldman, Path to Additional Airport Capacity has Many Potholes, Air Transport World, Nov. 1988, at 18; Phillips, Structural Change in the Airline Industry: Carrier Concentration at Large Hub Airports, Transp. J., Winter 1985, at 18; Street, Kind of Public Utility Commission Proposed to Oversee U.S. Airports, Airport F., Feb. 1989, at 31; AOCI Testifies on Airline Concentration at U.S. Hubs, Airport Highlights, Sept. 26, 1988, at 2;Senate Aviation Leaders Concerned about Hub Concentration, Airport Report, May 1, 1989, at 2.


27. Passengers select an airline for travel based on frequency of service, travel time, fare, aircraft type, and flight schedule. A. Ghobrial, supra note 23, at 14.

28. During the summer of 1987, airlines scheduled 33 flights to arrive at Chicago O'Hare at exactly 9:15 on weekdays. Similarly, at Atlanta's Hartsfield Airport, airlines scheduled between 41 and 73 operations during various peak 15-minute intervals despite the airport's ability to handle only 37 flight operations in those periods. Fawcett & Fawcett, supra note 26, at 42, 44.

On the issue of scheduling, the view point of the airport manager typically differs from the air carriers. Rather than enhancing airline market share, the airport is more concerned with the safe and orderly movement of aircraft and ground transportation, and limiting environmental impacts of the airport. But, the airport manager seldom participates in the scheduling of aircraft which use the facility. N. Ashford, H. Stanton, & C. Moore, Airport Operations 26-51 (1984). See also Mayer, The Late, Late Show: How a Priority Flight System Can Reduce the Cost of Air Traffic Delays, Transp. Res. Rec. No. 1161, at 14 (1988).
fares to attract more travelers. These lowered fares occurred just as the Nation was entering a strong economic recovery. These factors combined for a near doubling in air passenger activity in just a few years.  

While these events have led to costly congestion and delays at some airports, the airlines are likely to adhere to them because of the significant offsetting economic benefits. Also, the regulatory mechanism which could require air carriers to be accountable for such costs as congestion and delay has been partly dismantled.

2. An Airport's Capacity to Accommodate Surges in Air Traffic is Frequently Finite; and is Hindered by Fragmented Governmental Responsibility

Given the size, technology mix, and multiple-simultaneous activities associated with an airport, the planning for future adequate capacity is often troublesome. One method of analyzing airport capacity is to break it down into "airside" and "landside" capacity. "Airside" capacity is the number of aircraft movements that the airport and the supporting air traffic control system can accommodate in a unit of time, such as an hour. Among several factors which determine airside capacity are:

- the length of a runway needed for safe aircraft operations;
- the number and location of runways/taxiways to handle multiple aircraft movement;
- the separation required between approaching aircraft necessary to limit problems associated with wake vortices;
- the types of navigational aids in use for proper surveillance and control of aircraft;
- the number of gates to accommodate aircraft; and
- the need for noise abatement operating procedures to limit environmental impacts.


33. Wake vortices are eddies and turbulence generated by the flow of air over the wings and fuselage. They trail behind an aircraft and can upset the stability of following aircraft. The heavier the lead plane, the stronger the vortex which follows it. Light planes following heavy planes can experience considerable difficulty with wake vortices.
Add to these certain "landside" considerations; such as size of the terminal and the bag handling facilities, adequacy of ground access, and capacity of parking areas.

As traffic activity increases these and many other factors become important in handling aircraft, passengers, and goods. Usually, more than one unit of government is responsible for the various capacity factors, complicating the overall management of capacity. In the first decade after deregulation, as traffic grew at an accelerated rate, there was not a commensurate increase in coordination among the local governments and the federal government. Consequently, physical capacity solutions needed to handle the growth were slow in coming.34

3. THE SURGE IN AVIATION ACTIVITY, ALONG WITH THE FINITE CAPACITY OF AVIATION INFRASTRUCTURE, AGGRAVATED THE CAUSES OF DELAY IN THE NATIONAL SYSTEM OF AIRPORTS AND CALLED FOR AN INCREASED FEDERAL GOVERNMENT ROLE

With the surge in commercial aviation activity during the 1980's, including the airlines' tight scheduling and hubbing practices, many have argued that additional, unacceptable35 delays may be created because of

34. Within the last couple of years the Federal Aviation Administration and airport operators at several major airports have created airport capacity task forces to identify and implement solutions to the congestion and delay problems. But, such efforts are not widespread throughout the national system.


The airlines' losses also approximate $2 billion annually. Airline Group Reports ATC Delays, AVIATION WEEK & SPACE TECH., May 30, 1988, at 124 (average cost of operating a transport in flight is $2,174 per hour; ground holds cost airlines $600 per hour). In 1987 planes waiting to takeoff or circling for a landing used about 500 billion gallons of jet fuel, or 3.6% of 1987's total jet fuel consumption. Koepp, Gridlock! Congestion on America's Highways and Runways Takes a Grinding Toll, TIME, Sept. 12, 1988, at 52. That same year delays caused U.S. airlines to lose the equivalent of 100 days in aircraft operating time every day. Based on typical 10 hours per day for each aircraft, the losses implied that airlines had to add 235 aircraft to their fleets to
limited aviation infrastructure capacity.36 Others point out, however, that solving delay problems should not focus exclusively on infrastructure limitations.

Of course, congestion and delay are inherent in a system as complex as the national system of air transportation. Also, there are intense interactions between many components of the system.37 Disruptions in one part of the system can have a profound affect on the other parts. Thus, a bottleneck on a freeway leading to the airport, or lack of terminal parking, or long lines at terminal check-in, or congestion on a taxiway, can each cause a ripple effect38 elsewhere in the system. Naturally, the strength of these interactions has intensified with the increased use of airline hubs with their closely timed arrivals and departures.

While figures showing congestion and delay39 began to increase during the early years after deregulation, delays have declined somewhat in the past two years.40 Much of the improvement can be attributed to changes in the FAA’s control of the traffic. Some claim, however, that without more investments in improved ATC equipment and airport infrastructure, the system will experience dramatic delay increases in the future.41

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37. See AIRPORTS AND AIRWAYS, supra note 4, at 10.
38. A hiccup caused by an initial 15-minute delay may not work itself out of the system for several hours. Poritzky, Airports, Airports—Where’s the Capacity?, AEROSPACE AM., Jan. 1985, at 27.
39. Delay is difficult to measure and there is no industry-wide agreement on an appropriate definition of delay. The FAA maintains two systems for continuously monitoring delay: The National Airspace Performance Reporting System (NAPRS), consisting of reports from air traffic control facilities of serious delay conditions and causes of delay; and the standardized delay reporting system (SDRS), which are reports on the length of delay on four phases of flight (gatehold, taxi-out, airborne, taxi-in) submitted by selected air carriers. Based on the data collected, the FAA rated 18 U.S. airports as “seriously congested” in 1987, meaning each airport experienced more than 20,000 hours of aircraft delays. DOT/FAA, AIRPORT CAPACITY ENHANCEMENT PLAN, ch. 1 at 7 (DOT/FAA/DP/88-4 (1988)); McArtor Calls for Blueprint to Increase Airport Capacity, AVIATION WEEK & SPACE TECH., Jan. 18, 1988, at 61.
40. In the first years after deregulation an average of 1600 flights per day experienced delays of more than 15 minutes. The averages for the last three years have fallen: 1986 (1,144 flights per day); 1987 (1076); 1988 (1022). 1988 Flight Delays Hit Three-Year Low, FAA NEWS RELEASE, Feb. 17, 1989. See also DOT/FAA, AIRPORT CAPACITY ENHANCEMENT PLAN (DOT/FAA/CP/88-4 (1988)).
41. Severe shortages in airport capacity have been claimed for twenty years. Butwin, The Great Airport Dilemma, SATURDAY REV., Jan. 6, 1966, at 49; Hotz, Choking on Prosperity, AVIATION WEEK, Aug. 21, 1967, at 11; Jones, Airports Face the Great Passenger Flood, AM. AVIA-
Ultimately, the determination of how much delay is acceptable, and what changes must be made to reduce delay, are policy matters. While some delay may be avoided by constructing more airports or purchasing system-wide advanced microwave landing systems, the costs may exceed the potential benefit. If costs for such additional infrastructure remain high, policy makers may have to turn to other less costly alternatives.

Of course, the concern is who will make such policy choices. To date, the federal government has accepted only limited responsibility, primarily in the area of air traffic control improvements. There has been little national planning and consideration of the long-term benefits of airport real estate acquisition, mitigation of environmental impacts, private-sector economic incentives, and regulatory measures to enhance the Nation's aviation system capacity.

4. AMONG THE MORE CONTROVERSIAL CONSTRAINTS ON THE NATIONAL SYSTEM OF AIRPORTS HAS BEEN THE INCREASE IN AIRPORT USE RESTRICTIONS IN RESPONSE TO LOCAL NOISE COMPLAINTS

One byproduct of the increase in aviation activity has been the difficulty that the airport managers have in dealing with airport neighbors concerned about noise. Many neighborhoods seeking reductions or elimination of aircraft noise have mobilized. For an increasing number of airports, the more politically expedient, cost-effective means of meeting neighbors' demands has been to adopt restrictions on the use of the air-

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42. OFFICE OF TECHNOLOGY ASSESSMENT, AIRPORT SYSTEM DEVELOPMENT: SUMMARY 8-9 (OTA-STI-232 (1984)).
In some cases airports have limited the types of aircraft which may use the airport or the hours of operation.

Given the intense component integration in the aviation system nationally, many of these use restrictions have a ripple effect elsewhere. Such effects have led the airlines to challenge these use restrictions as detrimental to national interests. As will be discussed hereafter, some of the blame should fall on the federal government. The complexity of solving such problems as airport noise and airport capacity call for a comprehensive, cross-governmental response under the leadership of the FAA.

C. AFTER DECADES OF EXPERIENCE, AIRPORT NEIGHBORS HAVE GAINED CONSIDERABLE LEVERAGE IN INFLUENCING AIRPORT DECISION MAKING

Even prior to the jet age, some homeowners near airports claimed that aircraft were a nuisance and sought to influence airport activities. With the introduction of jet aircraft and the surge in air traffic in the United States, the conflicts between airports and their neighbors seem to
have intensified.\(^{47}\)

While a significant portion of those living near an airport tolerate aviation activity,\(^{48}\) there is always a strong core of individuals who are vocal, if not downright rowdy, when given an opportunity to express their thoughts about airport expansion plans. When considered in a less emotional setting, many of the concerns of airport neighbors are worthy or recognition.\(^{49}\) Common comments from airport neighbors\(^ {50}\) are:

- Can we expect the noise to increase in the future?
- I believe the value of my home is less because of the noise exposure.
- Does the airport have a long range plan to meet both aviation and community needs?
- My real estate agent told me I will have a hard time selling my home.
- I am more worried about single aircraft overflights, than the "average noise" measures you airport folks use.
- I can live with the daytime noise, but the nighttime flights are too much.
- How come the military aircraft are so much noisier?
- Isn't there someone I can call if the noise becomes too bothersome?
- I have attended several of these community meetings and nothing ever seems to happen.
- Does the airport have any money to pay for the noise damage? When can I expect to be compensated?
- Are hazardous chemicals or materials being flown over my house?
- Do the airlines have de-icing equipment? Is it used?
- I feel like I'm being manipulated.
- How come you don't want to know about our neighborhood, our schools, our lives?
- I think the vibration of my walls and windows is worse than the noise.
- Will the noise cause hearing loss?

These and other comments from airport neighbors show a need for better education of local residents about aviation matters and increased

\(^{47}\) Around a busy airport the envelope of moderate noise levels can cover 40 to 50 square miles. Severe noise impacts for the same airport can occur in areas up to 20 square miles. DOT/FAA, ESTABLISHMENT OF NEW MAJOR PUBLIC AIRPORTS IN THE UNITED STATES, ch. 5 at 3 (1977).


\(^{49}\) Far from being irrational, many anti-noise groups consistently act effectively to serve their interests as they perceive them. Of course, such rational conduct may also be accompanied by considerable "passion." The combination of both passion and rational conduct in dealing with public decisionmaking can be potent. For an excellent study of this issue see F. BAILEY, THE TACTICAL USES OF PASSION: AN ESSAY ON POWER, REASON, AND REALITY (1983).

airport and aviation industry involvement in community affairs.\footnote{51} Of course, neighbors who fail to get the attention of those responsible for aviation activity may seek restrictions on use of the airport through legal action or political pressure.\footnote{52}

\footnote{51. Notwithstanding the diversity of modern day life, research indicates that most people possess a high degree of pride and satisfaction in their neighborhoods. A. DOWNS, NEIGHBORHOODS AND URBAN DEVELOPMENT (1981); Fried, The Neighborhood in Metropolitan Life: Its Psychosocial Significance, in URBAN NEIGHBORHOODS 331 (R. Taylor ed. 1986). Because of close associations within neighborhoods, families are reluctant to leave even if the area is highly impacted by noise. Campbell, Airport Noise: Aggravation or Acclimation, PSYCHOLOGY TODAY, Dec. 1975, at 118 (nor do those living near noisy airports appear to avoid outdoor activities because of the noise); Greene, Santa Ana Heights has a Problem in the Skies, L.A. Times, Mar. 2, 1989, § 9, at 2, col. 1; Kelley, Under the Wings, They Say a Prayer, L.A. Times Jun. 22, 1986, § 9, at 1, col. 5 ("This is probably the second or third nicest neighborhood in Long Beach. We get along well with our neighbors, our kids' friends are here, my wife and I coach soccer and all the kids play. So we're tied up here." George Schiff, who lives at the end of the Long Beach Airport runway.).

Frankly, those who favor airport development are probably only a narrow segment of a community population, similar to project opponents who are also in the minority. The defenders of airport development may be no more legitimate spokesmen for the public interest than are opponents. Since there are seldom guidelines to resolve conflicts between these interests, it might be better if both factions begin discussions by mutually agreeing that neither minorities' claim is the more deserving. See Feldman, Air Transportation Infrastructures as a Problem of Public Policy, in CURRENT ISSUES IN TRANSPORTATION POLICY 17 (A. Altshuler ed. 1979).


Some anti-noise groups become perpetual motion machines, refusing to back off even after winning several battles over noise. Stein, One Field a Pain, L.A. Times, Dec. 21, 1986, § 9, at 1, col. 4 (discussing persistance of homeowners near the Torrance Airport); Monorail Idea Must Survive Civic Myopia, L.A. Times, Jan. 29, 1989, § 2, at 8, col. 1 (charging Newport Beach residents go too far in trying to stop a privately funded monorail).

Of course, the strategy of an anti-noise group can backfire. In 1985, Donald Trump bought an estate near the Palm Beach International Airport. In 1987, Trump formed a anti-noise political action group to back leading candidates for the County Commission, which owned the airport.
Some in the aviation community now recognize the importance of reducing the conflict between airports and neighbors. A few airports have public relations, community land use planning, or noise abatement offices to help bring local concerns into airport decision making. However, such efforts are not universal. Many airport authorities still fail to dedicate sufficient resources to work out conflicts with local property owners.\(^\text{53}\)

Part of the problem here is that the airport operator does not have direct control over the many factors which are essential in resolving the difference between the airport and its neighbors. Local governments which regulate land use near airports and the federal government which controls airspace play indispensable roles in the resolution of such conflicts. When support and cooperation from these actors is missing, an airport sponsor may feel the likelihood of success is beyond its reach.

**D. Existing Legal Remedies Do Not Encourage Air Carriers or the Federal Government to Actively Participate in Resolving Airport Noise Conflicts**

Among the more troubling aspects of aviation-related noise has been the failure of the legal system to promote a resolution of conflicts among those involved with the problem. An important cause of this failure has been the limited ability of common law causes of action and remedies to address the technological, socioeconomic, and institutional complexities associated with aircraft noise. Some of these shortcomings could be overcome if legislatures would craft new causes of action and remedies.\(^\text{54}\) However, the competition among public and private interests

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But, Trump's endorsement became the kiss of death. Trump became the issue, and his candidates, who were initially leading in the polls, lost the election. Opposing candidates used the slogan, “Can a Billionaire Always Have His Way?” Homeowners Threaten to Sue Over Noise, 1 AIRPORT NOISE REP. 25 (1989).

53. Politicians who support airport development have made some incredibly insensitive statements about airport neighbors. At the opening of the Palmdale Airport facility, Los Angeles Mayor Sam Yorty said “I must warn the environmentalists that unless reason prevails and harassment ceases, the entire economy of this nation will grind to a halt. I do not feel that the silent majority of this country wants to forego a paycheck or to pay exorbitant taxes to further some of the ‘far out’ environmental proposals.” Miles, Yorty Dedicates Palmdale Terminal, L.A. Times, Jun. 30, 1971, § 2, at 1, col. 3. Or, consider Congressman Gene Snyder (R-Ky) at a congressional hearing on airport noise: “The vast majority of these people that have noise pollution—that they asked for it. They bought that property close to an airport. . . . A lot of other people have other problems besides noise problems. People have marital problems. They asked for those, too. They entered into a marriage contract.” Airport and Aircraft Noise Reduction: Hearings Before the Subcomm. on Aviation of the House Comm. on Public Works and Transportation, 95th Cong., 1st Sess. 260 (1977).

which might be furthered or harmed by such legislation has thwarted the likelihood of a change in the status quo.

Generally, under existing rules of law, neighbors of airports may seek damages for noise injury under two causes of action: nuisance or inverse condemnation. Both of these causes of action place a heavy burden of evidentiary proof on the impacted landowner. Additionally, statutes of limitation have barred recovery for the vast majority of those living adjacent to airports. Consequently, many claim the aviation industry has received a windfall because it has not had to pay an important social cost of its activity.

Even if the landowner could prevail in court, the amount of the likely damage award is usually far less than the cost of litigation. Consequently, lawsuits have become used more often by homeowner groups or affluent communities with a "war chest" as political leverage to flight aviation activity. Such use of the legal system can frustrate judges, who recognize

55. Only property owners may seek recovery for noise-related injury. This leaves those who rent without a legal remedy. In Philadelphia one community leader complained that landlords were generally reluctant to insulate apartments against airport noise, even though the apartments were within a high noise zone. EPA/FAA, EFFECTS OF AIRPORT NOISE ON A NEIGHBORING STATE, app. E, at 3 (1980) (Letter from Barbara Farley, Eastwick Project Area Committee).


In 1970 over one hundred homeowners living near the St. Paul-Minneapolis Airport sued to recover for loss of property value caused by aircraft noise. As the litigation continued from year to year without resolution, the number of plaintiffs began to decrease due to moves or death. The case was finally decided on February 1, 1989, with three homeowners remaining. A jury found that noise had not caused a reduction in property value, thus the airport was not liable. Jury Finds Airport Noise Did Not Reduce Home Values, 1 AIRPORT NOISE REP. 28 (1989).

57. Plaintiffs in law suits frequently have difficulty accepting the dismissal of their claims because of a statute of limitations bar. When a judge barred her suit against the Burbank Airport because of a statute of limitations, homeowner Yolanda McGinnis complained, "It's really a crock. It's really unfair. I don't know what my options are or what the lawyers are going to do. But big business talks. Who really gives a damn about the people?" Braxton, Angry Plaintiffs Fume over Ban on Airport Noise Damage Suits, L.A. Times, Sep. 16, 1988, § 2, at 8, col. 1. For the philosophical and practical reasons for statutes of limitations see Epstein, The Temporal Dimension in Tort Law, 53 U. CHI. L. REV. 1175 (1986).


59. Coulson, Nearly 700 Claims Filed; Homeowners Plan to Sue Port over Airport Noise, L.A. Times, July 1, 1986, § 2, at 1, col. 1; Murphy, Airport Noise Foes Display Clout with Pact Limiting Jets, L.A. Times, Nov. 11, 1985, § 1, at 3, col. 4; Szymczak, O'Hare Suburbs Under Fire, Chicago Tribune, June 18, 1989, news, at 1; Airport Noise Spurs Suit by Loma Portal Residents, L.A. Times, July 31, 1986, § 2, at 2, col. 4; Keeping Quiet at HPN; Noise Reduction at Westchester County Airport; BUS. & COM. AVIATION, June 1988, at 48; Austin Group Preparing Test Lawsuit Over Noise, 1 AIRPORT NOISE REP. 76 (1989).
the real battleground is within the legislative arena.\textsuperscript{60}

Additionally, the United States Supreme Court held that only the airport proprietor will be liable for noise-related injury.\textsuperscript{61} Two authors have made the following astute observation about this situation:

The liability for aviation noise has been partially disconnected from the responsibility for aviation noise abatement. This is a result of decisions in which various courts have held that the liability for aviation noise damages rests solely on the hundreds of individual airport proprietors, while responsibility for aviation noise abatement resides collectively among federal, state and local governments, air carrier and airport proprietors. This "single liability/shared responsibility" situation promotes, rather than discourages, confusion. The result is unwarranted agony for all the parties.\textsuperscript{62}

Beyond these problems are some conditions or characteristics of noise litigation which limit a fair resolution of controversies.\textsuperscript{63} Included among these are the following:

- differences between judges, some of whom focus on the nature of the aviation activity, while others look at the consequences to the property owner;
- the problem of finding the airport authority liable in cases where the airport is in compliance with all regulatory requirements;
- uncertainty about the nature of the "property interest"\textsuperscript{64} damaged by the aviation activity;

\textsuperscript{60} See comments of judge in Ft. Lauderdale International Airport: Judge Denies Request for Injunctive Relief, 1 AIRPORT NOISE REP. 93 (1989). But see Judge Gives City 20 Days to Enact Strict Noise Rules, 1 AIRPORT NOISE REP. 159 (1989) (where judge took matter out of the hands of local elected officials who were attempting to negotiate a compromise).

\textsuperscript{61} Griggs v. Allegheny County, 369 U.S. 84 (1962).

\textsuperscript{62} Werlich & Krinsky, The Aviation Noise Abatement Controversy: Magnificent Laws, Noisy Machines, and the Legal Liability Shuffle, 15 LOY. L.A.L. REV. 69 (1981). The Environmental Protection Agency concluded that the sole liability rule "induced strains among institutions which must cooperate if the aircraft/airport noise problem is to be adequately addressed.

\textsuperscript{63} Legal and Institutional Analysis of Aircraft and Airport Noise and Apportionment of Authority Between Federal, State, and Local Governments, ch. 5, at 30 (1973).

\textsuperscript{64} Property is a complicated legal concept. It is not an object that can be owned or possessed, but rather the rights a person has with respect to material objects. Such rights may be several and are represented as a "bundle of rights." In having such property rights, however, the law recognizes the state can reserve certain rights to itself. R. Barlowe, Land Resource Economics: The Economics of Real Estate 328-61 (4th ed. 1986). The disagreement occurs when landowner and state adopt different perceptions about their rights in property. For the landowner, property rights likely include the need for "individual distance," the security in the use and possession of property, and the ability to associate with others on the property. T. Benditt, Rights (1982). Many Americans now believe they have a right to declare their neighborhoods off-limits to unwanted economic and social change. H. Boyte, The Back-Yard...
• efforts to set the amount of compensation\textsuperscript{65} raises questions about the appropriate date and basis for valuation;
• airports have strong economic and political reasons to fight claims of noise injury, no matter how meritorious;
• the common law liability system creates incentives for victims to exaggerate the claim of injury;
• litigation benefits lawyers to a degree disproportionate to their contribution to solving the problem; and
• there is no guarantee that the compensation awarded will be used by the landowner to help ameliorate the problem.

Clearly, present conditions impair rather than enhance the ability to finally resolve disputes between an airport and its neighbors. Perhaps of equal concern is the fact that the law may discourage airport proprietors from carrying out thoughtful planning and coordination for the growth of the airport. Given the risk of sole liability, many airport managers closely guard any information about future airport operations. This has a chilling effect on public discussion and undermines appropriate government accountability.

Additionally, the fact the airport proprietor is solely liable for noise-related injuries limits the concern demonstrated by the airlines, other local governments, the states, and the federal government. Typically, the airport is left alone in seeking ways to mitigate noise impacts, negotiate with or educate local landowners, or pay for the increased costs associated with the spillover effects of aviation activity.

E. COMPETING COMMUNITY CONCERNS AND LACK OF EXPERIENCE IN LAND USE PLANNING CREATE SERIOUS PROBLEMS FOR AIRPORT INFRASTRUCTURE MANAGEMENT

1. LOCALLY OWNED AND OPERATED AIRPORTS IN THE UNITED STATES ARE IMMERSED IN COMMUNITY AND REGIONAL COMPLEXITIES AND RIVALRIES

Airport operation, planning, and development suffer from competing priorities and fragmentation of government authority in urban and rural\textsuperscript{66}


\textsuperscript{66} Expansion of airports into rural areas must confront dwindling resources and changing priorities. Many watch with concern the loss of prime agricultural land and loss of forest, wetlands and wildlife conservation areas. Also, the introduction of a transportation activity into a rural community can significantly affect the community cohesiveness and structure. Alig & Healy,
America. While most airports are owned by one unit of local government, aviation impacts are almost universally felt across several local jurisdictional boundaries. Since these boundaries represent historic differences between neighborhoods and communities, it is not surprising that units of local government will disagree about the use of an airport.

Decision making within local governments is heavily influenced by special local concerns. Such specific interests are able to control local government decisions for at least two reasons: units of local government typically lack the electoral diversity which exists in large populations or extensive land areas; and they often lack the checks and balances, such as bicameral legislatures and separation of powers, found at the state and national level.

Added to this backdrop is the condition that control of land use continues to be the prerogative of local governments. In fact, in an era when cities, towns, counties, and so forth have experienced an erosion of many


A prominent legislative leader in aviation issues stated: "I am not sure we are going to force all the noisy planes into rural America, because they are not going to stand for it, either." Government Policies on Aircraft Noise, Hearings Before the Subcomm. on Aviation of the House Comm. on Public Works and Transportation, 99th Cong., 2d Sess. 50 (1986) (Congressman Glenn M. Anderson).


69. Pressures by interest groups are seldom proportional to the total benefits each group would gain from alternative social choices. Thus, the distribution of political power among interest groups may differ from the distribution of total costs.

One of the more influential interest groups can be the center-city business community who prefer close-in infrastructure support. S. PLOTKIN, KEEP OUT: THE STRUGGLE FOR LAND USE CONTROL 36 (1987).
other governmental powers, the right of local land use control is more jealously guarded than ever before.

A serious consequence of this situation has been the construction of incompatible residential development within close proximity to airports. Weekly, if not daily, landowners desirous of building homes near an airport seek the necessary land use approvals from a local government. If that government does not own the airport or have a strong commitment to the long-range needs of aviation, the developer's proposal will likely be approved. Reasons why incompatible development might be approved include the following:

- the parcel may not be suitably sized to allow for more compatible commercial or industrial development;
- the property may be in an already well-developed residential area having little commercial/industrial potential;
- the general perception that the airport, as a proprietary activity, ought to compensate land owners for restrictions on uses of property;
- failure to approve the project could mean the loss of tax revenue; and
- failure to construct homes might aggravate a community housing shortage.

As a result many airports in the United States have become "bulls eye" facilities, with little or no buffer between the airport and residential communities.

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70. Local governments complain of lost local control because of:
- disharmony among state and federal agencies and branches of government;
- increased resources needed to continually battle cross-jurisdictional issues;
- increased concern over vulnerability to litigation; and
- external policy decisions which have a significant effect on local economics and financing.

Walker, Intergovernmental Relations and the Well-Governed City: Cooperation, Confrontation, Clarification, 75 Nat'l Civic Rev. 65, 85-86 (1986) (claiming that local governments are responding either with apathy or hostility to such matters).


72. This phrase was used by Long Beach City Councilman Tom Clark to describe Long Beach Airport. Long Beach Airport, L.A. Times, Jan. 31, 1989, Editorial, § 2, at 6, col. 6.

73. Encroachment around an airport typically occurs gradually, one decision at a time. Some have called similar policy choices a "tyranny of small decisions." Cf. Kahn, The Tyranny
Another consequence of fragmented local decision making is the opposition by one or more local governments to the airport development plans of another. The opposing government may have its own airport, which it desires to shield from competition, or it may want to curb the spillover effects which accompany increased aviation activity. This competitive atmosphere has become so fierce that the construction of new airports or airport expansion projects are a rarity in the United States.

74. During the 1960s New York and New Jersey were actively considering building a fourth airport in the New York City area. When the State of Connecticut offered to build an airport to compete with the New York area airports, the Port Authority of New York and New Jersey orchestrated opposition to eliminate the Connecticut proposal. Berger, Nobody Loves an Airport, 43 S. CAL. L. REV. 631, 694-96 (1970).

75. A good example of local conflict over airport operations involves the Burbank Airport, owned and operated by the cities of Burbank, Glendale, and Pasadena. These three cities are east of the airport, while the City of Los Angeles lies to the west. For years all planes leaving Burbank Airport have flown departure routes placing them over residential areas in the City of Los Angeles. Los Angeles politicians routinely complain and take every opportunity to challenge the flight path. The City of Los Angeles has urged a “fair share” plan, where planes would fly an equal number of flights to the east and to the west. The three cities respond they are powerless to make a change. Flights to the east require sharp banking maneuvers to avoid the Verdugo Mountains. The three cities claim the issue is one of safety and the FAA has exclusive authority over flight corridors. The airport authority also points out that 55% of the airport employment goes to Los Angeles residents, with only 23.5% to residents of the three cities. Finally, they claim that implementing a fair share plan would simply increase the number of people within noise impacted areas, and increase rather than eliminate public protest. As a counter, the City of Los Angeles Council voted unanimously to zone a small portion of the airport which lies within the City of Los Angeles so the airport could not build a proposed new terminal. McGarry, Burbank Airport Rejects Demand to Share Noise, L.A. Times, Mar. 10, 1988, § 9, at 1, col. 1; Simon, L.A. Council Uses Zoning in Noise War with Airport, L.A. Times, Jan. 14, 1988, § 2, at 8, col. 4.

One way to control an airport is for the local government opposed to further development to purchase the airport. Bailey, Desire to Control Growth, Noise Sparks Move, Carlsbad Weighs Plan to Buy Palomar Airport, L.A. Times, Dec. 23, 1987, § 2, at 1, col. 1.

Of course, some communities may be able to capitalize on airport growth by promoting compatible development and increasing their tax base. MacDougall, Manor Readies for Airport and Betting by Devising Plan to Deal with Growth, AUSTIN BUS. J., May 22, 1989, § 1, at 9; Whitmore, Suburban Mayors at Odds on Noise, Expansion Issues, CRAIN’S CHICAGO BUS., July 11, 1988, at T6.

76. An example of a snarled airport project was the St. Louis proposal. A site was selected for a new airport across the Mississippi River in Illinois. Initially, the Illinois State Government, the City of St. Louis, and the FAA agreed. Opposing the project were residents of the county where the new airport would be located (noise), the State of Missouri (didn’t want airport in Illinois), and business interests in St. Louis (which didn’t want to lose the close-in location of Lambert Field). Finally, a change in the St. Louis city government caused the demise of the project. OFFICE OF TECHNOLOGY ASSESSMENT, AIRPORT AND AIR TRAFFIC CONTROL SYSTEM 115 (1982).

The last major airport built in the United States, the Dallas-Fort Worth Airport, occurred after 30 years of local bickering. The construction of the airport was fought by both Dallas and Fort Worth. The following factors kept the two cities apart: each city had a different congressman who supported federal funding for an airport owned by one city; refusal of the Civil Aeronautics
What is needed is the intervention of a higher level of government to orchestrate a successful resolution of these local interjurisdictional conflicts. But the states and federal government have refused to assume such a role because the problem is perceived as "land use," which is an almost sacrosanct local prerogative.

2. **Lack of Experience in Airport Planning and Community Land Use Control Impairs an Airport’s Ability to Meet Long Range Needs**

Airports themselves must take some of the responsibility for the intergovernmental friction caused by aviation activity. Airports differ widely in the staff size, experience, and training needed to tackle complex land use planning and community conflict issues. More often than not, airport administrators are unaware of community planning and zoning actions which can affect airport operations. Even if airport officials learn of potentially conflicting local government actions, the response is not always timely or well orchestrated to influence community decision making.

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77. Only about 700 airports in the United States require the services of a full-time airport manager. J. WILEY, supra note 31, at 23. For some airports, mismanagement is a major problem, limiting airport services and capacity. Bremer, Airports’ Troubles Raise Questions of Mismanagement, AIRPORT SERVICES, Oct. 1988, at 23. After deregulation smaller airports found it difficult to compete. Among the reasons for small airport troubles: absence of community support; lack of effective airport manager and staff; and absence of a long-range plan for airport development consistent with community goals and objectives. Bienvenu, Staying Alive: How Small Airports Can Meet the Challenge, AIRPORT SERVICES, May 1985, at 42.

78. In 1987 developer Donald Epler petitioned for property rezoning with the Columbus Development Commission. Epler wanted to build a 300-home subdivision on 180 acres of land within the airport high noise area. A month before the scheduled hearing, airport coordinator Bernie Meleski sent a memorandum to the city planning office suggesting disapproval of the petition, or conditional approval requiring sound-proofing of structures and dedication of aviation easements. On the date of the hearing, no airport representative was present, nor was the memo noted or discussed. By a six-to-one vote the rezoning was approved with no restrictions. Subsequently, when the airport complained of the action, the Commission replied:

- the Epler tract was on the "fringe" of the noise area;
Similar shortcomings have a profound influence on an airport's ability to prepare and promote airport master plans and land use compatibility proposals, which are necessary for long term efficiency. Among the common weaknesses in airport planning, which frustrate local residents and community leaders, are the following:

- the focus is on commercial aviation interests, often ignoring broader community priorities and concerns;
- citizens are not involved during all phases of planning, causing important local issues to be overlooked, or understated;
- planning often emphasizes physical solutions, without addressing possible changes in operations or institutional relationships;
- airports have been "secretive" in conducting planning, because of the perceived need to avoid private land speculation, limit the potential for litigation, and "maintain operational flexibility;"
- planners often disclaim any serious environmental or socioeconomic im-

79. The issues to be addressed in airport planning have not changed much in twenty years. They include: resolution of airspace conflicts, how to reduce noise to acceptable levels, location of airport infrastructure, role of reliever airports, resolution of ground access problems, how to accommodate military training/facilities, services for air cargo, the appropriate government entity to sponsor development, and financing options to fund development. R. SHINN, REGIONAL AIRPORT PLANNING: A SYSTEMATIC MODEL 79-80 (1969).


Airport infrastructure strategies can be dominated by four professions, each having a narrow view of the issues: engineers (people will obviously accept this professional, complete, fair analysis and cooperate with the project); planners (the way to deal with opposition is by increasing public participation so that government agencies know how local residents feel about things); lawyers (the way to deal with opponents is to beat them in court, or prove that you can); and economists (if people are upset about the impacts, just offer them enough money and they will be satisfied).

81. The literature in support of airport administration is rich in design and construction information. Comparatively little is available on airport economic, political, environmental, and community relations problems. J. WILEY, AIRPORT ADMINISTRATIONS AND MANAGEMENT 1 (1986).

82. FAA, Record of Decision, Anchorage International Airport Noise Compatibility Program 3-5 (Oct. 10, 1988) (difficult for City of Anchorage to implement airport recommendations requiring city action when the city was not consulted during the planning process); E. FELDMAN & J. MILCH, THE POLITICS OF CANADIAN AIRPORT DEVELOPMENT: LESSONS in FEDERALISM 50-53 (1983); Pavlicek, O'Hare International Airport: Impervious to Proposed State Efforts to Limit Airport Noise, 47 J. AIR L. & COM. 413, 443-44 (1982); Searles, Engle on Teterboro Airport, BUS. & COM. AVIATION, Feb. 1986, at 90.

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Pacts, even though they claim dramatic increases in future aviation activity;83
• often there is lack of leadership in the preparation of a plan, and in the
plan’s advocacy;84 and
• forecasts of future aviation activity are often exaggerated, undermining
subsequent community confidence in a plan.85

Such planning flaws can be further magnified by external forces
which may derail the success of even well-prepared airport objectives.
Two of the most important external factors are:
• the failure of the budget process to fund planning initiatives, thus eroding
the comprehensive nature of a plan;86 and
• the tendency of different local governments or government agencies to
publish conflicting plans affecting the same area of influence.87

Airports can expect that those with interests which conflict with the
airport will use these weaknesses to curtail airport development. Specifi-
cally, landowners with sizeable economic interests at stake will challenge
a plan’s supporting data and conclusions,88 and seek relief through the

83. Local communities were stunned when the Port Authority of New York and New Jersey
published its $2.7 million expansion plan (Project 2000) for Kennedy Airport. The study found no
increase in aircraft noise inspite of a forecasted 50% increase in traffic. Monahan, Airport Study
Raises Fears, N.Y. Times, Nov. 15, 1987, 11L1, at 8, col. 4.
84. Among the common leadership failings is the notorious mishandling of the news media.
85. Because forecasting relies a lot on judgment, there is the risk that political influence may
affect the results. One study found that local airport master plan forecasts were greatly exagger-
ated forty percent of the time. Also, when airport forecasts were totaled the sum of aviation
activity was 2.5 to 3 times higher than the state aviation forecast. J. Rodwell, The States
Aviation Forecasting Needs 27-28 (FAA-AVP-79-7 (1979)).
86. See Walters, Airports: An Economic Survey, 12 J. TRANSPORT ECON. & POL’Y 125-26
(1978) (good bibliography of references on airport topics prior to 1977). A continuing problem at
the local level is the compartmentalization of land use planning and fiscal responsibilities. Closer
ties need to be developed. Chapman, Land Use Planning and the Local Budget: A Model of
Their Interrelationships, 48 PUB. ADMIN. REV. 800 (1988).
87. The history of Southern California airport planning is the almost annual publication of a
“new” airport study sponsored by a different government entity. And, this has been going on for
decades. E.g., R. Shinn, REGIONAL AIRPORT PLANNING: A SYSTEMATIC MODEL 49-63 (1969);
Philmus, Los Angeles Hatches Big Area Airport Plan, AIR TRANSPORT WORLD, Aug. 1965, at 23.
An example of successive, conflicting plans for the same airport occurred between 1983
and 1987 at the Rickenbacker Airport (Columbus, Ohio). In 1983 the local government sponsor
of the civil operations at the airport prepared a “noise reduction plan.” In 1985, the Air Force
prepared a noise study and “community agreement” to reduce noise, as part of the transfer of
property to the local government. Within 18 months the FAA funded a FAR part 150 Noise-
Compatibility Study. There was no continuity among those preparing the three studies. As a
result there were multiple inconsistencies. RICKENBACKER AIRPORT AUTHORITY, AIRPORT MASTER
88. Depending on the economic stakes involved, land developers may do separate noise
political process. Another common response is for elected officials, wanting to avoid the consequences of choosing between competing interests, to require "further study" of the problem and alternatives.89

Pointing out the pitfalls of airport and community planning does not mean that airport projects are doomed from the start. A few airports have succeeded in preparing credible plans and coordinating aviation activities with community initiatives.90 Such successes, however, require considerable commitment, leadership, and resources by the airport and its local government sponsor.91

F. AIRPORTS ARE NOT ALWAYS SUPPORTED BY AIR CARRIERS IN EFFORTS TO SOLVE CAPACITY AND LAND USE COMPATIBILITY PROBLEMS

An airport's success is determined not only by its relationship with neighbors and local governments, but also with air carriers and others who provide important airport revenue. But the conditions under which airports and air carriers have historically conducted business are changing. Prior to deregulation the relationship between the two was relatively stable. In that era, airports and airplanes signed long-term lease agreements reflecting the regulated environment. Since deregulation the air carriers have greater latitude in selecting airports and routes to serve, and in otherwise enhancing corporate profits. Many airports, still bound by contracts negotiated prior to deregulation, are not gaining the support of the airlines in making similar adjustments to the changes.

89. This strategy backfired for politicians in Sacramento. In 1987 the airport noise issue became controversial when flights departing the Metropolitan Airport were rerouted to fly over the Central City. They had previously flown over the suburb of Natomab. The County Supervisors delayed making a decision and formed a 27-member citizen task group, expecting the group would retain the route over the city. When the committee recommended a routing over the suburbs, the committee was immediately disbanded and its recommendations rejected. County Supervisors Disband 27-Member Noise Task Force, 1 AIRPORT NOISE REP. 66 (1989).

90. One of the best airport community relations programs is run by the Port of Seattle for the Seattle-Tacoma International Airport (Sea-Tac). Hallmarks of that program include: a monthly newsletter to 35,000 citizens; an open-to-the-public policy on all meetings and work sessions; an environmental mediation program involving the FAA, air carriers, airline pilots, airport users, and the community; an aggressive public education program using local newspapers, primary/secondary school programs, small group meetings, and airport tours; and a full-time professional real estate staff. See SEA-TAC FORUM: SOUND INFORMATION (serial publications of the Port of Seattle 1988 & 1989).

Among the matters, since deregulation, where airports could use increased participation from the air carriers are: willingness of air carriers to adjust schedules to reduce airport congestion and delay; and assistance in working out solutions to community conflicts.\(^9\) When local pressure has forced airports to impose use restrictions airlines quickly point out the airport’s obligations under the existing lease, the needs of interstate commerce, and the erosion of safety margins.

Notwithstanding air carrier objections, an airport may ultimately prevail in imposing restrictions if the airport serves a market important to the carrier.\(^9\) While such market advantages have helped some airports, there is still an overall absence of regular coordination between airports and air carriers. The most publicized example of such disharmony has been the refusal of major airlines to support airport expansion projects, which might make room for competition from other air carriers.\(^9\)

While there is seldom a clear right or wrong answer to these airport/air carrier issues, the present distant relationship means alternatives are seldom discussed or considered. As a result both communities and the nation’s air transportation system suffer the consequences.

G. **EVEN IF AN AIRPORT IS COMMITTED TO LIMITING AIRCRAFT NOISE IMPACTS, SELECTING AND IMPLEMENTING NOISE ABATEMENT ACTIONS REQUIRES CAREFUL PLANNING, A PUBLIC WILL FOR SUCH ACTIONS, AND LEADERSHIP**

Finding ways to limit the effects of aircraft noise remains among an

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\(^9\) Of course, at the center of this conflict is the noise generated by jet aircraft, many operated by air carriers. Several factors reduce the air carriers’ interest in finding necessary solutions concerning noise impacts.

- Airlines and pilots have a strong interest in avoiding loss of life and the liability associated with unsafe aircraft operations. If noise abatement actions, either collectively or specifically, are perceived as eroding safety, the airlines will resist.
- Landowners near airports are not directly the “customer” of the airlines. Consequently, they are not able to influence market decisions.
- To date, homeowners have not had the political support sufficient to embarrass or challenge aviation industry decisions relating to noise abatement.
- There are no “moral inhibitions” against air carriers operating noisy aircraft, since aviation activities are viewed as benefiting the public.
- The airports, not the air carriers, are liable for noise injuries.

\(^9\) Examples of this include Lindbergh Field (San Diego) and John Wayne Airport (Orange County, California). O’Dell, *Battle for John Wayne’s Golden Slots*, L.A. Times, Mar. 5, 1989, § 4, at 1, col. 2.

\(^9\) See Feldman, *Path to Additional Airport Capacity has Many Potholes*, 25 AIR TRANSPORT WORLD 18 (1988) (discussing US Air’s delay in supporting expansion plans for Pittsburgh Airport). Of course, commitment to a major airport expansion is an important investment decision for an airline. Such decisions must compete with other decisions involving new aircraft acquisitions, maintenance facilities, and other capital needs.
airport proprietor's more vexing challenges. In response to continuing pressure airports have considered many "noise abatement actions" which can reduce noise levels for residential dwellers or shift noise impacts. A comprehensive noise abatement program usually requires cooperation among several local jurisdictions and government agencies, and routine attention to the problem after abatement actions are initiated. Such intergovernmental cooperation and careful attention to the problem are not common. Also, as illustrated below, other institutional and policy concerns can scuttle otherwise well-intended noise control measures.

95. See generally GENERAL ACCOUNTING OFFICE, AIRCRAFT NOISE: EIGHT AIRPORTS' EFFORTS TO MITIGATE NOISE (RCED-89-189 (1989)).

96. Among the many noise abatement actions are: changes in runway location, length, or strength to shift operations away from populated areas; displaced runway thresholds; preferential or rotational runway use programs; preferential flight track use; restricted time/location of engine maintenance runups; limits on numbers/types of certain operations; limits on types of aircraft; curfews; increased glideslope angle; power and flap management; acquisition of land or easements; compatible use zoning; building code provisions; sound insulation of existing buildings; real property noise notices to prospective buyers; purchase assurance guarantees; noise-related landing fees; build high-speed exit taxiways; construct noise barriers; establish noise abatement office at airport; promote redevelopment programs; initiate tax incentives for compatible land uses. A. HARRIS, R. MILLER & J. MAHONY, A GUIDANCE DOCUMENT ON AIRPORT NOISE CONTROL (FAA Report No. FAA-EE-80-37 (1980)). The effectiveness of such measures is determined by the reduction of people living within high noise areas, and the reduction of the number of sensitive sites (schools, churches, hospitals, parkland) impacted. Id., ch. 2, at 6.


97. Typically noise abatement strategies include several actions which must be implemented by local governments which are not sponsors of the airport. See METROPOLITAN WASHINGTON AIRPORTS, FAR 150 NOISE COMPATIBILITY PROGRAM WASHINGTON DULLES INTERNATIONAL AIRPORT (Jan. 1985) (report recommended 19 noise abatement actions, ten of which to be implemented by local governments).

98. It is a major task to ensure noise control on a day-to-day basis. Included among the regular decisions which have noise impact consequences are: control of air traffic in the terminal area; issuance of building permits; approval of utility extensions and street improvements; subdivision approvals; location decisions for public facilities; airline and airport capital investment decisions.

99. Not all noise abatement actions are warmly accepted by local residents. At Los Angeles International Airport a 15,000-foot-long sound barrier wall was constructed to reduce noise transmissions. Five families which benefited from the sound barrier sued the airport contending the wall was an eyesore that depreciated their property values. Hager, High Court Upholds Right to Sue Over Airport Jet Noise, L.A. Times, Feb. 25, 1986, § 2, at 1, col. 4.
1. **POLITICAL, FISCAL, AND OTHER CONSTRAINTS LIMIT AN AIRPORT’S ABILITY TO PURCHASE PROPERTY IN AREAS OF HIGH NOISE IMPACT**

From time to time coordinated airport planning may lead to the purchase of noise-impacted homes, relocation of families within the community, and redevelopment of the property with more compatible uses. But the local public may prevent such actions if large numbers of families have to be relocated. Other factors which curtail the acquisition of noise-impacted property include:

- removal of property from local government tax rolls is seldom well received;
- during fiscally-constrained times the high cost of land acquisition may not compete well with other public projects;
- strong real estate investors typically object to public bodies entering the land acquisition and development market;
- proposed redevelopment actions for acquired land can conflict with existing community comprehensive planning; and
- additional resources necessary to manage the real estate and relocation effort may burden limited airport administrative capability.

Studies of families facing relocation suggest that people have greater social and psychological problems with moving, than financial concerns. People can also harbor suspicions against outsiders who propose "rehabilitation" plans for their neighborhoods.

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104. A working-class, largely Latino immigrant community (Lennox in Los Angeles County) of 20,000 near the Los Angeles International Airport was studied for possible conversion to light industrial/commercial use. The plan was developed by those living outside the community and was viewed with suspicion by residents. In order to accomplish "revitalization" the City of Hawthorne wanted to annex Lennox. Hawthorne was challenged by the City of Inglewood, which had similar plans. Efforts to involve the Latino majority in planning was difficult, causing Anglo residents to take a disproportionate role in responding to issues of Lennox's future. Many of the
Again, the impacts of such constraints may be significantly reduced if the airport plans well, especially with the help of experienced real estate professionals.

2. **While Sound-Proofing of Homes Is Becoming a Commonly Proposed Noise Abatement Strategy, It Is Not Always Clear That the Costs Are Justified**

When local governments won't zone out residential development near an airport, and the airport fails to implement operational changes, a common compromise is to offer to sound insulate homes. In making such offers most airports seek in return an easement in the airspace above the homeowner's property. This is often troubling to land owners, who are reluctant to give up any rights in their property.

The construction costs associated with sound insulation can run about $20,000 per residential structure. Some have questions about the wisdom of such expense. The cost of soundproofing often exceeds the original cost of the home, and many homeowners around airports have learned to live with the noise. Additionally, sound attenuation provides little relief during summer months when windows are opened and outdoor activities are common.

As in the case of relocating families from high noise areas, the airport operator may run into public opposition to the expense or process of sound attenuating homes. Of course, if the airport can neither move nor insulate residential dwellings too close to the airport it is left with the continuing bad will of its neighbors. Both the airport and its neighbors become losers for failure to take any action. For many airports the residents were not citizens, could not vote, or speak English. Rotella, *County's Renewal Plan for Lennox Stirs Hopes, Fears*, L.A. Times, Feb. 24, 1989, § 2, at 8, col. 5.


The common methods for acoustical treatment of structures includes: sealing or weather-stripping windows, doors, vents, and external openings; replacing hollow-core doors with solid doors; installing central air conditioning, acoustically treated ceiling panels, wall panels, and double-glazed windows; eliminating windows; and insulating entryways, attics, and crawl spaces. U.S. DEP’T OF HOUSING AND URBAN DEVELOPMENT, AIRCRAFT NOISE IMPACT: PLANNING GUIDELINES FOR LOCAL AGENCIES 112-15, 211-28 (TE/NA-472 (1972)); J. WESLER, RESIDENTIAL SOUND INSULATION: HOW TO DO IT (1987) (Wyle Laboratories Technical Note #3).

Of course, one way to soundproof would be to build structures below-ground. *School Burrows Underground to Save Space, Dodge Airplanes*, L.A. Times, Feb. 5, 1989, § 8, at 6, col. 5.


resolution of this dilemma is a litmus test of its planning and leadership talent.

3. **Scientific Understanding of Aircraft Noise and Its Effects Provides an Important Baseline in Resolving Disputes Between Airports and Their Neighbors**

Because of important advances in science and technology society can now travel farther and faster than ever before, but must cope with the discomfort and other effects of aviation activity. Scientists have contributed to a reduction of these affects by designing quieter aircraft engines, and developing predictive models of aircraft noise intrusion into communities. With the latter information some airports now commit considerable time and resources in determining the noise impact “contour lines” which conceptually eminently from the airport. They then try to convince local governments, air carriers, the Federal Aviation Administration, and others to adjust their planning and activities based on these science-based predictive lines.109

While such contour line modeling forms an important baseline for analysis of land use alternatives, there remain many facts which science has yet to quantify or clarify. Included among the limits of science in this area are: the inability to convincingly assess the risk of harm to human health; the absence of fact-based principles to assess the full social cost of aircraft noise impacts; and the failure to establish a proximate causal relationship between aviation activity and various health and welfare problems experienced by airport neighbors.110

Notwithstanding such problems, the airport operator’s use of science-based principles can be an important stepping stone for eventual resolution of local conflicts. But, the airport’s credible use of these principles requires the dedication of resources to hire or train employees competent in using science in the airport and community planning arenas.

H. **Airports Also Have Difficulties in Planning and Implementing Remedies for Airport Capacity Deficiencies**

Solving noise complaints can lead to enhancement of airport capacity.111 Such solutions, among others, are important in an era when air-

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111. With homes immediately adjacent to its airport and with the potential for increased aviation traffic, the T.F. Green State Airport in Rhode Island spent $900,000 to build a noise and blast
ports serving many metropolitan regions have become chokepoints for air
traffic;\textsuperscript{112} and corporations consider a community's airport capacity in se-
lecting locations for commercial/industrial activity.\textsuperscript{113}

But the days of the dream fix, such as "seadromes,"\textsuperscript{114} to airport
capacity shortfalls may be past. Constraints limiting major expansion of
airport capacity have become institutionalized and enjoy strong public
and political support.\textsuperscript{115} Any serious progress in increasing capacity re-
quires able planning and a commitment to long range goals in the place
of expediency.

1. \textbf{THE PRACTICE OF "BANKING" LAND FOR FUTURE EXPANSION NEEDS
HAS NOT BEEN WIDELY ACCEPTED IN THE UNITED STATES}

In the last few years a small number of urban airports were able to
significantly expand airport capacity largely because they owned addi-
tional developable land.\textsuperscript{116} In some cases this property had been

\begin{itemize}
\item barrier of precast concrete panels on top of a landscaped earth berm. They also imposed a
curfew after 11:00 p.m. These actions cut down on the noise complaints and made it possible to
seek more airline service for the area. \textit{Rhode Island Airport Studying Expansion Needs}, \textit{Airport
F.}, Oct. 1985, at 34.
\item 112. \textit{Transportation Research Board, Future Development of the U.S. Airport Net-
work} 18 (1988).
\item 113. \textit{Conway, Time to Reconsider Fly-in Sites}, \textit{30 Industrial Development & Site Selec-
\item 114. See S. Gomes, \textit{State Airport System Planning}, ch. 4 at 23 (1976) (discussing plan-
ning for overwater airports to serve New York City, Cleveland, Chicago, Detroit, Los Angeles,
Long Beach and New Orleans). In the late 1960s Southern California airport planners were
considering a "seadrome" in 240 feet of water in Santa Monica Bay. The seadrome would have
covered 2870 acres, with 80 to 120 gate positions. R. Shinn, \textit{Regional Airport Planning} 61-
\item 115. \textit{Southern California Ass'n of Governments, California Aviation System Study: Sup-
\item 116. After deregulation the Dayton Ohio International Airport dramatically increased its ca-
pacity. This was possible because the airport owned 364 acres available for immediate develop-
ment, the field was surrounded largely by farmland, and most general aviation traffic operated
out of Dayton General Airport South, a GA reliever airport owned by the City of Dayton. Scearce,
\textit{Deregulation Winner: Dayton Grows From Mid-Sized Local Airport to Big-Time Hub}, \textit{Airport F.},
Feb. 1985, at 42. Compare Dayton with the Burbank Airport, which has little room to grow. At
Burbank the passenger terminal violated FAA safety guidelines because it is too close to the
runway. But plans to build another terminal away from the runway had to be scrapped because
the proposed site was too close to a classified government research area used by Lockheed
Corporation. The only remaining site for the terminal would displace 1,457 auto parking spaces,
which were all needed by the airport. Additionally, the FAA was pressing Burbank to abandon
the use of one runway because it was too short for many commercial aircraft. McGarry, \textit{Burbank

One of the more important capacity enhancement actions is the addition of a runway to an
airport. One runway, properly equipped for independent IFR operations, can increase an air-
port's capacity from 20 to 50 percent. But, an 11,000 foot runway, with safety buffers covers 130
acres. An additional 450 acres surrounding the runway must be clear of structures. \textit{Office of
Technology Assessment, Airport and Air Traffic Control System} 113 (1982). The FAA
"banked" or acquired to ensure its availability for future airport operations.\textsuperscript{117} For several practical reasons\textsuperscript{118} land banking has often been advocated as a necessary practice in meeting the nation's long-term aviation infrastructure needs. Nevertheless land banking is not commonly practiced in the United States for several reasons:\textsuperscript{119}

- acquisition of large tracts of land by public agencies can cause shifts in local political power and wealth;
- programs to meet long-range requirements experience difficulty in competing with more urgent, immediate needs for limited public funds;
- depending on state law, an airport authority may be unable to prove "necessity" for the land acquisition, have jurisdictional limitations on where property may be acquired, or be restricted in financing for land banking purposes;
- during the stage in which the land is underutilized, the public agency may face high land management costs, and confront challenges to continued ownership under government real property disposal policies; and
- Congress has failed to support a national land use policy necessary for a successful land banking program.

2. \textbf{THERE IS NO WIDESPREAD EFFORT TO CONVERT UNDERUTILIZED AIRPORTS TO MORE ACTIVE COMPONENTS OF THE NATIONAL SYSTEM OF AIRPORTS}

Some have argued that the airport capacity problem can be solved by increasing the use of hundreds of underutilized airports in the United States.\textsuperscript{120} Many of these airports are former military airfields having long runways and considerable undeveloped acreage.\textsuperscript{121} Other airports are predicted the United States will need 30,000 more acres by the year 2000 to accommodate airport capacity expansion. DOT/FAA, AIRPORT CAPACITY ENHANCEMENT PLAN, ch. 2 at 7 (DOT/FAA/CP/88-4) (1988)).

\textsuperscript{117} The Pittsburgh Airport is able to double its present capacity because Allegheny County had the foresight to accumulate land for future airport growth over the past 20 years. \textit{Lack of Airport Capacity Creates "Crisis of Confidence" for Industry}, 129 AVIATION WEEK & SPACE TECH., Nov. 21, 1988, at 98.

\textsuperscript{118} Among the advantages of early land acquisition: land values are lower; there is a wider choice of sites; and existing owners have less power to hold out for higher prices when the transfer of title is not mandatory.


\textsuperscript{121} Between 1961 and 1986 the following military air bases were closed and are still operating as airports. (Approximate acres transferred and length of main runway are provided, if available).

Brookley AFB/Mobile, Alabama
(1,960 acres/9,600' runway)
underutilized because they were overbuilt by their sponsors, or have lost

<table>
<thead>
<tr>
<th>Air Force Base</th>
<th>Location</th>
<th>Acres</th>
<th>Runway Length</th>
</tr>
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<tbody>
<tr>
<td>Craig AFB/Selma, Alabama</td>
<td>(2,250 acres/8,000' runway)</td>
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<tr>
<td>McCoy AFB/Orlando, Florida</td>
<td>(2,900 acres/12,000' runway)</td>
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<tr>
<td>Sanford Naval Air Station/Sanford, Florida</td>
<td>(8,000' runway)</td>
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<tr>
<td>Glynco Naval Air Station/Brunswick, Georgia</td>
<td>(4,400 acres/8,000' runway)</td>
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<tr>
<td>Schilling AFB/Salina, Kansas</td>
<td>(2,000 acres/13,000' runway)</td>
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<tr>
<td>Forbes AFB/Topeka, Kansas</td>
<td>(3,500 acres/10,000' runway)</td>
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<tr>
<td>Dow Air Force Base/Bangor, Maine</td>
<td>(11,400' runway)</td>
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<tr>
<td>Presque Isle AFB/Presque Isle, Maine</td>
<td>(1,580 acres/7,400' runway)</td>
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<tr>
<td>Kincheloe AFB/Sault Saint Marie, Michigan</td>
<td>(3,600 acres/7,200' runway)</td>
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<tr>
<td>Duluth AFB/Duluth, Minnesota</td>
<td>(2,200 acres/10,000' runway)</td>
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<tr>
<td>Greenville AFB/Greenville, Mississippi</td>
<td>(2,030 acres/8,000' runway)</td>
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<tr>
<td>Richards-Gebrau AFB/Kansas City, Missouri</td>
<td>(2,300 acres/9,200' runway)</td>
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<tr>
<td>Glasgow AFB/Glasgow, Montana</td>
<td>(5,500 acres/13,500' runway)</td>
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<td>Lincoln AFB/Lincoln, Nebraska</td>
<td>(12,900' runway)</td>
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<td>Stead AFB/Reno, Nevada</td>
<td>(3,100 acres/8,000' runway)</td>
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<tr>
<td>Grenier AFB/Manchester, New Hampshire</td>
<td>(7,000' runway)</td>
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<tr>
<td>Stewart AFB/Newburgh, New York</td>
<td>(1,900 acres/11,800' runway)</td>
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<td>Rickenbacker AFB/Columbus, Ohio</td>
<td>(2,060 acres/12,000' runway)</td>
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<tr>
<td>Clinton County AFB/Wilmington, Ohio</td>
<td>(1,370 acres/9,000' runway)</td>
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<tr>
<td>Clinton-Sherman AFB/Burns Flat, Oklahoma</td>
<td>(3,100 acres/13,500' runway)</td>
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<tr>
<td>Olmsted AFB/Harrisburg, Pennsylvania</td>
<td>(9,500' runway)</td>
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<tr>
<td>Quonset Point NAS/North Kingstown, Rhode Island</td>
<td>(8,000' runway)</td>
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<tr>
<td>Donaldson AFB/Greenville, South Carolina</td>
<td>(2,400 acres/8,000' runway)</td>
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<tr>
<td>Sewart AFB/Smyrna, Tennessee</td>
<td>(2,800 acres/8,000' runway)</td>
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<tr>
<td>Amarillo AFB/Amarillo, Texas</td>
<td>(2,800 acres/13,500' runway)</td>
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<tr>
<td>Webb AFB/Big Spring, Texas</td>
<td>(2,300 acres/8,800' runway)</td>
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<tr>
<td>Harlingen AFB/Harlingen, Texas</td>
<td>(1,600 acres/8,300' runway)</td>
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<tr>
<td>Laredo AFB/Laredo, Texas</td>
<td>(1,900 acres/8,200' runway)</td>
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<tr>
<td>Fort Wolters/Mineral Wells, Texas</td>
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Airports Policy in the United States

(5,000' runway)
Perrin AFB/Sherman-Dennison, Texas
(1,870 acres/9,000' runway)
James Connally AFB/Waco, Texas
(1,500 acres/8,600' runway)
Larsen AFB/Moses Lake, Washington
(7,200 acres/13,500' runway)
Truax Field/Madison, Wisconsin
(9,000' runway)


In 1988, The Defense Secretary's Commission on Base Realignment and Closures recommended the following military airfields for closure:

- Chanute AFB/Rantoul, Illinois
- George AFB/Victorville, California
- Mather AFB/Sacramento, California
- Norton AFB/San Bernardino, California
- Pease AFB/Portsmouth, New Hampshire


Besides closures, some active military airfields are able to accommodate the joint civil/military use of the facility. Twenty-four joint use facilities are now in existence. When requested by a local government, the military service responsible for the field will evaluate the potential for joint use based on: airspace limitations, airfield configuration, navigation aids, land availability, aircraft arresting systems, encroachment, security, and environmental impact. Joint use may not be approved if:

- the field is used by a nuclear alert force;
- the field has an intensive pilot training mission;
- the joint use proposal would require co-location of military and civil aircraft; or
- access to the civil facilities would require route access through the military installation.


Also, military property adjacent to airports has been transferred quite often to accommodate the expansion of civil airports. J. Miller, STAPLETON INTERNATIONAL AIRPORT: THE FIRST FIFTY YEARS 87-89, 95-96, 107-110, 118, 131 (1983) (discussing transfers of property belonging to the Army's Rocky Mountain Arsenal to allow expansion of Stapleton); Hancock, Information on Land Exchanges, MCRD San Diego: 1919-1989, July 10, 1989 (unpublished manuscript) (citing several transfers of Marine Corps property to Lindbergh Field).

During WWII the number of airports in the United States doubled, as hundreds of communities donated or sold land to the government for the war effort. In a few short years the government spent $3.2 billion to construct runways and other airport facilities. At the end of the conflict the War Assets Administration (WAA) returned about 700 airports back to local governments. Many of these became the foundation of subsequent airport development in the nation. C. Dearling & W. Owen, NATIONAL TRANSPORTATION POLICY 29-30 (1949); A HISTORY OF THE UNITED STATES AIR FORCE: 1907-1957 189 (A. Goldberg ed. 1957); Borland, That Excess Military Airport, AIRPORTS, Mar. 1948, at 24; Colbert, Airports as Base of Air Power, AVIATION WEEK, Feb. 23, 1948, at 69; Hoehling, They're Giving Away 400 Airports, May, 1947, at 26.

But not all excess military airfields are converted to civil aviation uses. In 1964 the Air Force closed all flight operations at Bolling Air Force Base, across the Potomac River from National Airport. While many advocated the base's use for general aviation activity to relieve congestion at National Airport, the Air Force converted the installation to an administrative facility, along with
previous aviation business to other airports in the region.\textsuperscript{122}

An important use of such facilities is the diversion of general aviation activity from congested hub airports.\textsuperscript{123} In other cases the facilities could be improved to accommodate commercial aviation use. Notwithstanding these advantages, several factors limit the conversion of such fields to more intense use.

- Many underutilized airports are in regions of the country without a large demand for increased aviation activity.
- Notwithstanding existing acreage and facilities, underutilized airports typically need significant capital investment to return them to productive capacity.\textsuperscript{124}
- Portions of the airport property may have been committed to non-aviation public uses which enjoy strong local support.
- If expansion of the airport would compete for aviation activity with a major airport in the region, the sponsors of the larger airport (and the airlines based at that airport) may exert considerable political clout to curtail growth of the smaller field.\textsuperscript{125}
- Many communities elect to limit airport growth to avoid problems of noise and other effects.\textsuperscript{126}

\begin{flushleft}
the construction of military family housing. R. BURKHARDT, THE FEDERAL AVIATION ADMINISTRATION 144-45 (1967).
\end{flushleft}

\textsuperscript{122} Major airlines serving Alaska have pulled out of the Juneau and Fairbanks airports, to consolidate operations at Anchorage. Fried, Air Biggest Transport Segment, ALASKA J. COM., July 18, 1988, at 8.

\textsuperscript{123} See Walker, Taking Off; Airport Expansion is Under Way, L.A. Times, Aug. 9, 1988, § 2, at 1, col. 1 (discussing efforts by John Wayne Airport to squeeze out GA aircraft); Atlanta Encouraged to Build Second Airport, 5 AIRPORT 202 (1988) (Atlanta wants to spend $537 million on a major GA airport south of the city to allow for increased capacity at the Hartsfield Airport).

\textsuperscript{124} In 1968 the Air Force transferred Olmstead Air Force Base near Harrisburg, Pennsylvania to the state for use as a National Guard facility. During the next four years the operation of the base became a significant drain on the budget of the state’s Military Department. The cost of maintaining the extensive and old infrastructure was high. In 1972 the field was transferred to the Pennsylvania Department of Transportation for economic development purposes. The Transportation Department built a road access, vehicle parking, and terminal facilities to attract commercial aviation activity. Later attempts to transfer the airport to the local government were unsuccessful because of extensive Trichlorethylene (TCE) contamination from the prior Air Force ownership. State and federal clean up costs have been and will continue to be high. NAT’L GOVERNOR’S ASSOCIATION, SUCCESSFUL AIRPORT CAPACITY EXPANSION, Feb. 1989, at 24-27.

\textsuperscript{125} Two airports with significant growth potential curtailed by competition with other airports in the region are: former Richards-Gebaur Air Force Base (Kansas City); and Stewart (former Air Force Base) International Airport (New York Area). Feldman, supra note 41, at 18. Richards-Gebaur AFB transferred to Kansas City, AIRPORT F., Oct. 1985, at 61.

\textsuperscript{126} E.g., Brayton, MNAA Agrees to Seek Development of Smyrna Airport, NASHVILLE BUS. J., Dec. 19, 1988, at 14 (discussing successful effort by local residents to limit the civil aviation use of former Stewart Air Force Base). One of the critical reliever airports for Kennedy and LaGuardia, Long Island MacArthur Airport, has been kept from expanding by its owner, the Town of Islip, to limit noise impacts. Kornfeld, Airport Growth: Problems Amid Promise, N.Y. Times, Apr. 24, 1988, § 12L1, at 1, col. 1. See also Kornfeld, Republic Airport has Growth Pains, N.Y. Times, Oct. 1, 1989, § 12L1, at 1, col. 1.
Of course, the longer an airport goes underutilized, the greater the likelihood it will be converted to uses which make future airport expansion unlikely. In some regions of the country aviation interests have expressed concern over the sale of airport properties to commercial, industrial, and mixed-use developers.\textsuperscript{127} If land values continue to rise, and local governments look for means to fund important community programs, the loss of airport property will likely continue.\textsuperscript{128}

3. **FAILURE TO RESPOND TO ENVIRONMENTAL CONCERNS OR SATISFATORILY COMPLETE STATUTORY ENVIRONMENTAL DOCUMENTATION REQUIREMENTS DELAY OR SIDETRACK MAJOR AIRPORT PROJECTS**

During the last two decades the public has become more and more concerned with the environmental consequences of public works initiatives. Such concerns are aggravated when a public agency conducts planning in a secret, careless, or haphazard manner. The public distrust which this generates can be translated into opposition through the legal and political process.

Among the most potent legal tactics available to frustrated citizens is the right to sue over agency non-compliance with federal and state environmental documentation requirements. In 1969 Congress passed the National Environmental Policy Act\textsuperscript{129} which required all federal agencies to consider the environmental consequences of proposed “major federal actions significantly affecting the quality of the human environment.” Because of this, and similar state laws, airports must begin early in the planning process to identify, and if possible mitigate, the environmental consequences of major actions. The following deficiencies in preparing

\textsuperscript{127} Day, Small Airports Nose Diving in Number, Wash. Post, Sept. 21, 1987, § F1; Garbarine, Developers Home in on Small Airports, N.Y. Times, Jan. 15, 1989, § 10, at 13, col. 1; Haines, The Waiting Game, AOPA PILOT, Aug. 1989, at 63. In October 1988, most of New Jersey’s small airports shut down for a day to protest the continuing loss of airports within the state. In 5 years the number of airports had shrunk fourteen percent as property was converted to shopping malls and industrial parks. Also, the airports sought recognition that local communities were not supporting their airports through local compatible use zoning. Worthington, NJ Airport Protest Triggers Legislative Hearing on Concerns, AIRPORT SERVICES, Apr. 1989, at 10.

\textsuperscript{128} With property valued at $33 million Linden, New Jersey wanted to sell its airport to developers. But, the sale required special legislation to remove a deed restriction which provided that the property be maintained for aviation uses. Elliott, Move to Close Linden May Affect Other GA Airports, AIRPORT SERVICES, Feb. 1987, at 10.

such documentation can lead to significant delay in project approval and implementation:\textsuperscript{130}

\begin{itemize}
  \item failure to explore rigorously and evaluate objectively all reasonable alternatives;
  \item lack of complete and thorough discussion of environmental consequences of the proposed action and each alternative;
  \item failure to identify the conflicts between the proposed action and the objectives of federal, regional, state, and local land use plans, policies and controls;
  \item insufficient consideration of the cumulative impact on the environment resulting from the incremental impact of the proposed action when added to other past, present, and reasonably foreseeable future actions;
  \item failure to exercise good faith in disclosing to the public all information necessary for adequate opportunity to comment on the proposed action, its alternatives, and the environmental consequences; and
  \item lack of assessment and consideration of all public comments to the agency proposal, or failure to respond fully to all comments raised.
\end{itemize}

While airport operators express significant frustration over these requirements, faithful adherence to this process can be a systematic and thorough way to ensure that a project is integrated into the community. While the cost to the airport of such integration can be high, it may be necessary in order for the airport to compete for declining resources available to meet social requirements. One way to force prioritization among competing demands on limited land, air, and water resources is to require justification and public negotiations similar to this environmental documentation process.\textsuperscript{131}

4. **ALSO, AN AIRPORT’S ABILITY TO OBTAIN PROJECT FUNDING HAS A MARKED INFLUENCE ON EXPANSION POTENTIAL**

Another important determinant of airport expansion potential is ac-

\textsuperscript{130} The classic case was the plan to build the Westway highway in New York City. Ackman, *Highway to Nowhere: NEPA, Environmental Review and the Westway Case*, 21 COLUM. J.L. & SOC. PROBS. 325 (1988).

Among the more frustrating airport projects of the last twenty years was the Everglades Jetport in Southern Florida. The airport was planned in a 39-square-mile tract in the Big Cypress Swamp. With initial approval from federal, state, and local agencies ground was broken on September 18, 1968. But, within five weeks efforts to obtain a road access right-of-way raised concerns from the National Park Service and by the local flood control district. The right-of-way question snowballed from a local to a national issue. Under close congressional and Park Service scrutiny, it was learned that environmental considerations played almost no part in the siting decision. Further study revealed likely serious environmental damage to the Big Cypress Swamp. This caused the state and local governments to look for another site. Eventually the state concluded there was no need for a new major airport in the region. The original site was abandoned for commercial aviation purposes. E. WILLIAMS & A. MASSA, *SITING OF MAJOR FACILITIES: A PRACTICAL APPROACH* 16-17 (1983).

cess to funds.\textsuperscript{132} Capital expenditures for large and medium hub airports run about $1\textsuperscript{billion per year. About half of that is for new capacity. The federal share of that investment represents about thirty-three percent, with eleven percent coming from state funds. The remainder (fifty-six percent) must be generated locally. Many airports turn to the bond market for this funding.\textsuperscript{133}

But an airport’s ability to access private capital is entirely a function of financial performance. Purchasers of bonds want assurances that an airport can generate net revenue sufficient to pay interest and principal on bonds.

This financial health is measured by two rating agencies in New York that deal with bond issues: Standard and Poors (S & P); and Moody’s Investors Service. These agencies rate airport performance, which influences the interest rate and sale of a bond issue.\textsuperscript{134} Among the important factors\textsuperscript{135} influencing airport ratings are:

- an airport’s status in the nation-wide system of airports;
- existence of another airport in the region which may compete for aviation business, thus reducing revenue potential;
- whether an airport relies too much on tourism for its aviation activity;
- if there is a good mix of air carriers.
- the forecasted demand of airport activity;
- health of the local economy;
- the interrelationship between airport and airlines based at the airport;
- the financial health of the carriers serving the airport; and
- the airport proprietor’s historic coverage of debt service.

\textsuperscript{132} Delays in expanding both Laguardia and Kennedy Airports were caused, in part, by New York City’s fiscal crisis during the 1970s. Green & Tuchman, No Where to Go But Up, ENGINEERING NEWS-REC., Oct. 22, 1987, at 22.

\textsuperscript{133} TRANSPORTATION RESEARCH BOARD, THE CHANGING GOVERNMENT ROLE IN AIRPORTS 28-31, CIRCULAR 316 (1987). Generally, airports spend only 15\textsuperscript{percent of their capital budget on airside capacity expansion. The remainder is for roads, parking facilities, terminals and other landside projects. NAT’L COUNCIL ON PUBLIC WORKS IMPROVEMENT, THE NATION’S PUBLIC WORKS: REPORT ON AIRPORTS AND AIRWAYS 41 (1987). During 1988 there was an almost 200\textsuperscript{percent increase over the previous year in the airport revenue bond volume. Minerva, Airports Adopt to Deregulation, CREDIT WEEK, Aug. 22, 1988, at 1; Market for U.S. Municipal Airport Bonds Soars, AIRPORT HIGHLIGHTS, Dec. 5, 1988, at 2.

Venture capital groups have looked at airports for potential investment opportunities. Most believe, however, that airport improvement funding should remain under public sponsorship due to the strong political issues and unpredictability of noise abatement costs. Venture Capitalist to Seek Airport Profit Opportunities, AIRPORTS, June 20, 1989, at 1. See also ROTH, Airport Privatization, 36 PROC. ACAD. POL. SCI. 74 (1987).

\textsuperscript{134} Ross, Facilities Planning from a Financial Perspective, AIRPORT SERVICES, July 1986, at 47. Continued uncertainties in the airline industry keep all U.S. airports from receiving the highest credit rating. Minerva, Airport Rating Criteria Update, CREDIT WEEK, Aug. 22, 1988, at 3.

\textsuperscript{135} Not an important factor in rating airport performance is the threat of law suits. Bond dealers believe that most noise suits are settled for only a small fraction of the claim. Walters, California Airport Authorities Weigh Financial Impact of Ruling on Jet Noise, BOND BUYER, Mar. 4, 1986, at 4.
Also, investment institutions recognize the importance of accountability, planning, and leadership in the financial health of the airport.\textsuperscript{136}

III. FEDERAL AIRPORT POLICY

A. \textit{The Federal Aviation Administration, While Balancing Diverse National Objectives, Has the Federal Responsibility for Aircraft Noise Control and Airport Capacity Enhancement}

The primary federal responsibility for the control of airport noise and the enhancement of airport capacity belongs to the Federal Aviation Administration (FAA) within the Department of Transportation. The FAA,\textsuperscript{137} formerly the Federal Aviation Agency, was established by the Federal Aviation Act of 1958.\textsuperscript{138} Under that Act, the FAA has several statutory obligations, including:

- regulating air commerce to promote its development and safety, and fulfill the requirements of national defense;
- controlling the use of navigable airspace in the interest of safety and efficiency;
- certifying airmen, airplanes, and certain airports; and
- developing regulations to control aircraft noise, and other environmental effects of civil aviation.

While Congress gave the FAA broad powers over these and other duties, the federal statutes restrict the Agency's federal authority over owners or operators of airports in the exercise of their "proprietary powers and rights."\textsuperscript{139} The intent of this provision was to recognize the role of airports, owned by local authorities, in the national system of air transportation. But the appropriate extent of that local role is frequently debated, and is not always resolved within federal law.

Besides airport owners and operators, the Federal Aviation Act recognizes the importance of "air carriers," meaning those individuals or

\textsuperscript{136} See Minerva, supra note 134, at 3.
\textsuperscript{137} The Federal Aviation Administration is a large federal agency with an extensive data file on airmen, aircraft, and airports. The Agency is run by an Administrator and several Associate Administrators who oversee aviation safety, air traffic, airway facilities, airports, aviation standards, national airspace system development, regulation and certification, human resource management and policy, planning, and international aviation. The Administrator is represented by nine regional offices in the United States, each with jurisdiction over a multistate area. These offices carry out policies and enforce the rules and regulations developed by FAA Headquarters. The FAA also has international regional offices, and a training academy in Oklahoma City. At the local level the FAA has various airport district offices, civil aviation security field offices, aviation medical clinics, aircraft certification offices, manufacturing inspection district offices, towers, centers, and flight standard offices.
business entities which use aircraft to carry persons or property for compensation. By statute the FAA is to promote the development of the air commerce in which these carriers operate. Unfortunately, the diversity and competition among those in the aviation industry make it difficult for the FAA to select among various alternatives in promoting air commerce.

In addition to the role of airports and air carriers, FAA policy is influenced by competing concerns within the executive and legislative branches of the federal government. The Department of Transportation, the Department of Defense, the Department of Justice, the Office of Management and Budget, and congressional members and committees can exercise considerable influence over FAA actions. Among the issues of importance to these government bodies and individuals are:

- The safe operation of aircraft to reduce the loss of life, and injury to persons and property, to the maximum extent possible;
- The security of aviation passengers from terrorist activity;
- The need to bring deficit spending under control;
- The assurance of sufficient airspace for combat readiness training;
- The protection of states and local governments against unreasonable, intrusive interference from the federal government;
- The protection of homeowners in the vicinity of aviation activity against high levels of aircraft noise.

One consequence of these competing missions is that airport problems may not receive much attention within the Agency. Because of the FAA's direct responsibility of and investment in air traffic control
equipment and personnel, and the publicity received by aircraft accidents, the Agency dedicates more resources to airspace management and safety. The FAA's primary interests in airports center on the administration of federal grants to airports, and on those airport issues which are linked with the Agency's air traffic and safety responsibilities.

B. FAA’s Efforts to Control Aircraft Noise and Its Effects Have Been Subject to Limitations Within the Federal System of the United States

1. FAA Regulation has Caused a Measurable Reduction in Aircraft Noise Emissions, But Several Factors Restrict the Agency’s Ability to Accelerate Further Reductions in Aircraft Noise

Soon after the introduction of jet-powered aircraft into the commercial fleet, homeowners near busy airports began petitioning their congressmen for relief. Consequently, during the 1960s considerable congressional interest focused on the problem of aircraft noise. This public and legislative interest caused the President to appoint his Science Advisor to study alternatives to reduce aircraft noise impacts. Then, with the creation of the Department of Transportation in 1966, the overall coordination of this issue shifted to the Secretary of Transportation.

Also, during the 1960s the National Aeronautics and Space Administration, the FAA, and several segments of the aviation industry researched engine and airframe changes to reduce aircraft noise. These studies indicated that noise reduction was feasible, and could benefit many Americans.

Based on this effort, and with the support of the Secretary of Transportation, Congress in 1968 amended the Federal Aviation Act requiring the FAA to prescribe standards and regulations necessary to control and abate aircraft noise. Such control was to be accomplished by adopting minimum noise standards and adding noise criteria to aircraft certification requirements. In applying this law, however, the FAA was to

146. The Secretary of Transportation was to “promote and undertake research and development relating to transportation, including noise abatement, with particular attention to aircraft noise.” 49 U.S.C.A. § 1653(a) (West 1976) (repealed 1983).
147. For a summary of the early research see EPA, AIRCRAFT/AIRPORT NOISE STUDY REPORT: NOISE SOURCE ABATEMENT TECHNOLOGY AND COST ANALYSIS INCLUDING RETROFITTING (1973). For modern design changes to reduce aircraft noise see NATO REPORT No. 163, AIRCRAFT NOISE IN A MODERN SOCIETY (1987); Kandebo, HSCT Propulsion Studies Focus on Reducing Emissions Noise, AVIATION WEEK & SPACE TECH., July 10, 1989, at 34.
assure that any standard was "consistent with the highest degree of safety" and "economically reasonable, technologically practicable, and appropriate for the particular type of aircraft, aircraft engine, appliance, or certificate to which it will apply."

Based on this statute, in 1969 the FAA published Federal Aviation Regulation (FAR) Part 36 establishing the maximum allowable noise levels for aircraft certified after that date.149 Aircraft which were certified prior to the publication of the 1969 standard, and which were not thereafter modified to satisfy the 1969 standard, became known as "stage 1" aircraft. Aircraft meeting the 1969 standard are now referred to as "stage 2" aircraft. In 1977, the FAA revised its 1969 rule adopting a stricter standard for aircraft noise emissions for all aircraft certified after that date. These aircraft became known as "stage 3" aircraft, and are significantly quieter than stage 1 planes.150

During the mid-1970s the FAA was faced with pressure151 to adopt a

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149. Noise Standards: Aircraft Type Certification, 34 Fed. Reg. 18, 355 (1969), codified at 14 C.F.R. 36 (1989). With the publication of these standards the FAA stated that the Agency was making no determination that the noise levels were or should be acceptable to individual airport proprietors responsible for local concerns about noise impacts. See id. § 36.5.

150. The substantial noise reductions between earlier stage 1 aircraft and more recent stage 3 aircraft can be illustrated by comparing the Boeing 707-320 and the similarly-sized Boeing 757-200. The approach decibel reading of a stage 1 707-320 was 120.4 dB compared with 95.0 dB for the stage 3 757-200. It is generally accepted that a reduction of 10 dB in noise level represents a halving of the loudness of sound as perceived by the average listener. Thus, a reduction of 25.4 dB provides an 83% reduction in perceived loudness. WESLER, STAGE 3 AIRCRAFT: WILL THEY REDUCE NOISE? (Wyle Laboratories Technical Note No. 2, 1987).

151. After the publication of FAR Part 36, many in Congress became impatient with FAA activity in aircraft noise abatement actions. In order to spur on the FAA, Congress in 1972 amended the Federal Aviation Act giving the Environmental Protection Agency the authority to recommend additional noise regulations to the FAA. 49 U.S.C.A. app. § 1431. In 1972 the EPA
rule banning the operation of stage 1 aircraft in the United States. After much public debate and agency review, the FAA in 1976 implemented a regulation prohibiting the operation of stage 1 aircraft into U.S. airports on and after January 1, 1985.\textsuperscript{152}

While this stage 1 aircraft ban greatly reduced the noise emissions of individual aircraft operations, the increase in aviation activity occurring after the deregulation of the airline industry eroded much of the advantage. Today, Congress is under pressure from airport neighbors who claim noise levels have increased and want a ban on stage 2 aircraft.\textsuperscript{153}

But, the elimination of all stage 2 aircraft would have economic impacts on the aviation industry. In 1988 stage 2 aircraft made up fifty-eight percent of all commercial aircraft operated by U.S. airlines, and performed seventy-two percent of all departures.\textsuperscript{154} Stage 2 airplanes had a 1988 market value of $30 billion and would cost $50 billion to replace immediately.\textsuperscript{155} Of course, the cost of replacement declines if the indus-

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\textsuperscript{153} \textit{E.g.}, Minnesota State Legislature Joint Resolution Urging the United States Congress to Adopt Stage 2 Aircraft Fleet Addition and Operation Ban Deadline, \textit{reprinted in} 134 CONG. REC. S5240 (daily ed. Apr. 29, 1988).

The Minneapolis-St. Paul Airport recently renegotiated the leases with air carriers imposing a fee for excess noise, which is intended to force the phase out of stage 2 aircraft using the airport. \textit{Minnesota Airport Includes Airline Noise Fees in New Lease, 6 AIRPORTS} 463 (1989).


try is given enough years to retire stage 2 aircraft. The FAA estimates that a phase out target date of the year 2005 would reduce industry costs to $3.5 billion.

In addition to the high cost of conversion, the carriers and the FAA have raised other problems with an early phase out of stage 2 aircraft:

- An operating ban of stage 2 aircraft in the United States would severely impact many third world air carriers who cannot afford new aircraft.
- The production capacity of U.S. manufacturers is limited in meeting a rapid conversion to an all stage 3 fleet.
- An early phase out of stage 2 aircraft would have competitive repercussions because of differing fleet compositions among the affected air carriers.
- An early ban on stage 2 aircraft would increase the operating costs for airlines, driving up air fares, and limiting service to the public.
- There are several policy questions surrounding whether or not, or how to compensate air carriers for the added cost of fleet modernization.

156. Presently, however, stage 3 aircraft are not being bought as replacements but as fleet additions. Stage 3 acquisitions are more in response to the need for greater seat capacity than a direct response to aircraft noise regulations. Not only are stage 2 aircraft not being retired, but there is the possibility that additional stage 2 aircraft may be "dumped" on the United States if European countries successfully implement a proposed stage 3 only rule. See Proctor, Capacity Constraints Will Influence Fleet Composition Through 2010, AVIATION WEEK & SPACE TECH., Nov. 21, 1988, at 87.


160. One segment of the air carrier industry, air cargo companies, operate primarily stage 2 aircraft and would be severely impacted by an operating ban. Interest Groups Struggle with Aircraft Noise Standards, CARGO FACTS, Mar. 1989, at 5; Stage 3 Cargo Conversion Would Cost $15.9 Billion, 1 AIRPORT NOISE REP. 23 (1989); Noise and Old Age, CARGO FACTS, Oct./Nov. 1988, at 5.

161. The air carrier industry is split concerning the federal "compensation" for their losses if the FAA regulates an accelerated fleet modernization. Compare letter from Edward J. Driscoll, National Air Carrier Association, to FAA (Mar. 6, 1989) (FAA Rules Docket File No. 25790) (claiming the industry should be made financially whole for any losses they incur) with letter from Julie H. Ellis, Federal Express Corporation, to FAA (Mar. 17, 1989) (FAA Rules Docket File No. 25790) (suggesting air carriers could accept financial losses if the federal government would guarantee access to airports without use restrictions). Suggestions that the Congress provide investment tax credits or loan guarantees for accelerated fleet modernization run into several problems, including: the inability to extend financial assistance to foreign-based operations; the question of application to general aviation and corporate aircraft operators; the potential that federal financing would spur over-investment by marginal operators; and the increased costs to FAA of administering such a program.

If the federal government offers to "compensate" air carriers by assuring access to airports, the federal government will likely have to assume the liability for noise impacts.

The public perception is that it is unfair to provide air carriers any compensation, since they have flown for decades without paying the true social costs of their activity. Rather, any stage 2
• Impacts of a stage 2 operating ban on corporate and business aircraft owners would have to be considered.

The FAA has properly noted that any ban of stage 2 aircraft should not be considered without a comprehensive program for aircraft and airport noise control. Such a strategy should include: improved noise reduction technology for aircraft; operational procedures designed for maximum reduction or aircraft noise; sensible land use planning and control; and direct action, such as soundproofing of buildings or relocation of noise-impacted families and individuals. Of course, each of these actions raises other issues, including federal liability, federal land use planning, and federal budget impacts. Because of the political sensitivity and competing federal policies associated with these issues, the FAA has yet to move ahead with a specific course of action.

Besides achieving a balanced program, the FAA must also define the costs and benefits of various aircraft noise abatement strategies, as required by Executive Order and the Federal Aviation Act. But, the application of cost-benefit analysis has always been difficult in the area of alternative aircraft noise abatement strategies. Accurate analysis requires forecasts of aviation activity and information about air carrier plan-
ning which are often inaccurate or unavailable.\textsuperscript{166} Also, there are many unquantifiable variables pertaining to noise impacts in a neighborhood. For example, valuing the benefits of a quiet environment requires more information than is now available about the social and psychological effects of noise.\textsuperscript{167} Also, the possible effect on housing market prices is difficult to isolate from other market influences, except in the most serious cases.\textsuperscript{168} Additionally, the losses in time and disruption in schools and offices are not commonly reflected in the market prices of these properties.

2. **THE FAA HAS BEGUN TO ENCOURAGE BETTER LAND USE PLANNING AROUND AIRPORTS, BUT NEEDS TO BECOME MORE OF A PARTICIPANT IN LOCAL NEGOTIATIONS**

During the early years in which aviation was growing in the United States, cities and communities were experimenting with various methods to control the uses of land which degraded public "health, welfare, and safety." In 1926, a local land use control regulation called "zoning" was upheld as constitutional by the United States Supreme Court.\textsuperscript{169} Thereafter zoning grew to become common in urban communities. And, many who were familiar with airports and their neighbors advocated the use of zoning to protect aviation activity and safeguard the lives of prospective homeowners.\textsuperscript{170}

\textsuperscript{166} While cost-benefit analysis may consider the economic impacts on air carriers and homeowners, it often does not consider the effects on the airport owner or operator. See generally Trumball, Who Has Standing in Cost-Benefit Analysis?, 9 J. POL'Y ANALYSIS & MGMT. 201 (1990).


\textsuperscript{168} A commonly used method of valuing the social cost of airport noise is through a comparison of real estate values both inside and outside high noise zones. But, this methodology comes under considerable criticism.

- Many people do not have the surplus resources to move to quieter neighborhoods.
- It is difficult for real estate appraisers to untangle the effects of noise on house prices from many other effects.
- There is no accurate method to determine costs of noise impacts on many non-residential properties, such as shopping centers, parks, churches, schools, and so forth.
- Many non-perceived losses (such as long-term effects on physical or mental health) are not reflected in real estate prices.

See also D. Pearce, **SOCIAL COST OF NOISE** (1976).


\textsuperscript{170} See Air Transport Ass'n of America, Airline Airport Design Recommendations 5 (1946); Dworkin, Planning for Airports in Urban Environments, 5 URBAN L. 472 (1973); Fenerty, Legal
While the federal government expressed some early concern about tall structures which intruded into navigable airspace,\textsuperscript{171} the federal agencies responsible for aviation activity generally deferred to local governments regarding land use matters. Unfortunately, because of fragmented local jurisdiction and poor local planning, land use controls are not common around many airports in the United States.\textsuperscript{172} The failure to control incompatible land uses has measurably reduced the capacity of many airports, and has led to much fingerpointing by competing parties.\textsuperscript{173}

In 1962, the Federal Aviation Agency noted the lack of a federal role in airport environs land use planning as a weakness in federal airport pol-


Airport zoning ordinances, if enacted by local governments, primarily restrict the height of structures near an airport and promote noise-compatible uses on private land. Many such ordinances prohibit or limit residences, schools, and hospitals in noise sensitive areas. But, airport zoning laws generally permit commercial, industrial, and agricultural activities. Height restrictions ("vertical zoning") regulate the height of structures on a graduated basis from the runways. Other hazards may also be controlled, including: activities which produce smoke which could impede a pilot's visibility; uses which create electrical interferences with radio communications between planes and an airport; and air traffic hazards resulting from the improper location of additional airports close to existing airfields. P. ROHAN, \textit{ZONING AND LAND USE CONTROL}, ch. 15 (1989).

Other nations handle incompatible land use near major airports in different ways.

France: Many public airports have purchased extensive aviation easements over surrounding land.

Germany: Citizens can seek damages to their property interests through an administrative process.

Japan: Citizens may seek compensation for losses in court.

Switzerland: Law mandates noise zoning around airports. Citizens impacted by zoning may claim damages within 5 years after government approval of the zoning plan.


173. "From a philosophical standpoint, why should the Federal Government be expected to take local officials off the hook for the failure of local officials to provide for proper zoning?" Statement of Congressman Gene Snyder, \textit{Airport and Aircraft Noise Reduction, Hearings on
icy.\textsuperscript{174} Again, in 1971 a joint Department of Transportation-National Aeronautics and Space Administration study recommended that the federal government adopt a policy encouraging compatible land use planning near airports.\textsuperscript{175} At the same time several of the major metropolitan airports became concerned about the growth of homes near their fields, and sought the assistance of the U.S. Department of Housing and Urban Development (HUD). As a result of HUD funding, several airports conducted noise compatibility studies during the early 1970s.\textsuperscript{176} HUD's experience helped set the framework for later FAA involvement in this area.\textsuperscript{177}

During the mid-1970s the FAA began a pilot program sponsoring noise control and land use compatibility studies for a few airports around the country. But, for many airports without a history of noise conflicts, such studies were not warmly accepted by airport managers and local communities.\textsuperscript{178}

\textsuperscript{174} Office of Management Services, FAA, \textit{The Airport's Functions in FAA} 21-22 (June 30, 1962).

\textsuperscript{175} DOT/NASA Civil Aviation Research and Development Policy Study: Supporting Papers 6-14 (DOT-TST-10-5 (1971)).

\textsuperscript{176} See EPA, Legal and Institutional Analysis of Aircraft and Airport Noise and Apportionment of Authority Between Federal, State, and Local Governments, ch. 2 at 30-31 (1973).

\textsuperscript{177} U.S. Dep't of Housing and Urban Development, Aircraft Noise Impact: Planning Guidelines for Local Agencies (TE/NA-472 (1972)).


When an airport complained of the absence of local land use restrictions before hearings of the Illinois Pollution Control Board, the local governments responded by saying they were unable to zone effectively because the airport refused to define its long range operational plans. Pavlicek, \textit{O'Hare International Airport: Impervious to Proposed State Efforts to Limit Airport Noise}, 47 J. Air L. & Com. 413, 444-45 (1982).

Many airports were leary of the noise exposure maps used in noise compatibility studies. They feared the creation of noise contour lines would lead to law suits from homeowners. \textit{Airport and Aircraft Noise Reduction, Hearings before the Subcomm. on Aviation of the House Comm. on Public Works and Transportation}, 95th Cong., 1st Sess. 266, 295, 334 (1977) (remarks of Daniel T. Murphy, National Association of Counties; George J. Bean, Hillsborough County, Florida, Aviation Authority; Walter Rockenstein, Minneapolis, Minnesota).

A successful study which arose out of this FAA effort involved the Seattle-Tacoma Airport. \textit{DOT/FAA, Planning for the Airport and Its Environs: The SEA-TAC Success Story} (FAA-EQ-78-15 (1978)).
During the 1970s, as Congress held hearings on the problem of airport noise, numerous witnesses explained that federal action to control aircraft noise emissions would be ineffective unless controls were provided to preclude incompatible land uses near airports. Finally, in 1979 Congress passed the Aviation Safety and Noise Abatement Act giving the FAA specific responsibilities to promote better land use planning and control around airports. That Act directed the FAA to:

- establish systems to measure noise and to determine the exposure of individuals to noise from airports;
- identify land uses which are normally compatible with various exposures of individuals to noise; and
- establish a program to assist airports to prepare noise exposure maps and develop noise compatibility initiatives.

Based on this statutory authority, the FAA developed and implemented FAR Part 150, which provides federal guidelines and a federally-funded program to assist airports and local governments in noise control and land use compatibility planning. Part 150 has several features which are becoming common planning tools for airports:

- The FAA has recommended limiting certain land uses, especially residential dwellings, within a noise zone defined by the day-night average sound level (DNL) 65 dB contour line depicted on a noise exposure map.
- The FAA has developed a methodology for the preparation of noise expo-


181. The FAA has stated the following goals for its Part 150 program: reduce noncompatible land uses near airport; improve land use planning and control around airports; establish a comprehensive airport noise abatement plan; bring together the parties that have the ability to implement solutions; and promote airport capacity. DOT/FAA, Part 150 Interchange, July 11, 1988. FAR Part 150 is codified at 14 C.F.R. § 150 (1990).

sure maps.\textsuperscript{183}

- The FAA published guidelines for the preparation, and FAA approval,\textsuperscript{184} of noise compatibility programs which adopt various noise abatement actions for particular airports.
- Upon completion of a noise compatibility program, an airport may be eligible for federal funds to implement the FAA-approved noise abatement actions.

At the end of 1988 over 200 FAA-sponsored "Part 150" reviews were either completed or nearing completion.\textsuperscript{185} Many of these programs have led to changes in flight operations, decisions to acquire noise-impacted land, better exchanges of information between government agencies, and adoption of zoning restrictions.\textsuperscript{186} Notwithstanding some success, Part 150 is still in its infancy and may need further refinement. Based on a recent congressionally-directed analysis of Part 150, several program weaknesses were identified by those who had participated in the process:\textsuperscript{187}

- Part 150 has no compliance process or enforcement authority to ensure that approved noise compatibility program measures are implemented.
- The Part 150 process often raises unrealistic public expectations regarding the prospects for noise abatement.
- Consultation and coordination under Part 150 vary widely, with many noise compatibility programs developed with only minimal public, local government, and aviation industry input.
- In some cases, senior airport management participate very little in the Part 150 review, allowing consultants to run the study.
- Air traffic control personnel frequently oppose operational changes recommended for reasons of noise abatement, citing a pilot's prerogatives, safety, the need for efficiency, and air traffic controller workload.
- Some Part 150 studies have been used improperly for capacity enhancement with no real noise reduction benefits.
- Noise exposure maps may become out-of-date because of unforeseen changes in operations.
- There is no FAA-sponsored training for airports and consultants on how to prepare and implement Part 150.
- Because of limited FAA manpower, FAA is frequently absent during the

\textsuperscript{183} Id.

\textsuperscript{184} The FAA may not approve a noise compatibility program, or a portion thereof, if: (inter alia) the program measure(s) would create an undue burden on interstate or foreign commerce (including any unjust discrimination); the program measure(s) are not reasonably consistent with achieving the goals of reducing existing noncompatible land uses around the airport and of preventing the introduction of additional noncompatible land uses; the flight procedure recommendations reduce the level of aviation safety, or adversely affect the efficient use and management of the navigable airspace and air traffic system. 14 C.F.R. § 150.35(b) (1990).


\textsuperscript{186} FAA, RECORD OF APPROVAL, DANBURY MUNICIPAL AIRPORT NOISE COMPATIBILITY PROGRAM, Aug. 22, 1988.

\textsuperscript{187} See DOT/FAA, Part 150 Interchange, July 11, 1988; Numerous letters to FAA in FAA Docket File Number 25660.
very important formative stages of the Part 150 process. 188

- Since local governments do not have a stake in the outcome of a Part 150 review, they are often uncommitted to support and implement noise compatibility program measures.
- The lack of up-to-date, quality maps of land surrounding airports often make the drawing of noise exposure contour lines of little value.
- There are often property owners beyond the DNL 65 dB noise contour line who believe their interests are ignored by the airport.
- In some communities, a Part 150 study is perceived as just another in a series of airport noise reports all of which are costly and never improve the situation.
- The quality of consultant services varies widely.
- Airports are unclear about the standards under which the FAA reviews noise compatibility programs, causing airport authorities considerable embarrassment when measures which they negotiated in good faith are disapproved by the FAA.
- Part 150 studies and airport master plans are so interconnected that they should be prepared simultaneously, but they often are not.
- Public participation in the Part 150 process is not always encouraged. 189
- Many suggest that the FAA should provide data concerning single event noise levels, rather than using exclusively the day-night average noise exposure level. 190
- The relationship between part 150 reviews and the FAA’s responsibilities under the National Environmental Policy Act is unclear.
- Most cost/benefit analyses found in Part 150 reports are of poor quality and incomplete.

A troubling aspect among these program weaknesses is the absence of FAA representatives during the development of the airport noise compatibility plans. The recommendations which are often carefully negotiated at the local level have profound effects on the future of airports in the national air transportation system. A greater FAA role in such negotiations would be beneficial for several reasons including: the need to protect the billions of dollars in federal capital investment in U.S. airports; the

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188. This point has been stressed frequently by airport managers and airlines. E.g., Government Policies on Aircraft Noise: Hearings before the Subcomm. on Aviation of the House Comm. on Public Works and Transportation, 99th Cong., 2d Sess. 46,586 (1986) (testimony of Clifton A. Moore, General Manager, City of Los Angeles Department of Airports; and Clark Onstad, Vice President, Texas Air Corporation).

189. The statute establishing the Part 150 program provides that an airport operator should provide “notice and an opportunity for a public hearing” before submitting a noise compatibility program for FAA approval. 49 U.S.C. App. § 2104(a) (1982). The FAA has interpreted this as a duty of the airport and not of the FAA. Consequently, the FAA has not published guidance on public participation in the Part 150 process. See FAA PART 150 INTERCHANGE, Aug. & Sept. 1988, at 2.

190. E.g., Letter from Richard E. Sanderson, U.S. EPA, to FAA (Jan. 18, 1989) (suggesting the FAA add to part 150 noise exposure maps the location of areas where single event decibel levels will exceed: 80 dB, the level when sleep may be disturbed at night; and 98 dB, the level when activities in schools, churches, and hospitals will be disturbed).
opportunity for the FAA to gain a sense of local priorities and concerns important in providing federal program support; and the potential to integrate airport surface and airspace planning.

3. **The Authority of Local Governments Over Airport Use and Adjacent Land Development Continue to Be Used as a Reason for Limiting FAA Efforts to Regulate Uniformly Airport Noise and Its Effects Within a National Air Transportation System**

As it has moved forward with FAR Part 150, the FAA has been careful to point out that specific land use planning and noise abatement actions are matters within the discretion of local governments. The FAA position is summarized in this 1976 Department of Transportation Noise Abatement Policy Statement.

Airport proprietors are primarily responsible for planning and implementing actions designed to reduce the effect of noise on residents in the surrounding area. Such actions include optimal site location, improvements in airport design, noise abatement ground procedures, land acquisition, and restrictions on airport use that do not unjustly discriminate against any user, impede the federal interest in safety and management of the air navigation system, or unreasonably interfere with interstate or foreign commerce.191

Consistent with this position, airport operators frequently exercise their authority to impose use restrictions intended to limit noise impacts on surrounding communities. Such restrictions, however, have been a bitter pill for air carriers, which complain of increased operating costs,192 safety concerns,193 and constantly changing airport regulations throughout the Nation.194

192. Added costs include: the value of lost flights, cost of purchasing quieter planes, increased flight delay costs.
193. A major aircraft accident in 1988 was the crash near Detroit of a Northwest DC-9. In reporting its findings the National Transportation Safety Board found that the cockpit crew workload and stress had contributed to the accident. The crew knew it was running late and might miss a noise-related curfew that night at John Wayne Airport in Santa Ana, California. Remarks of Captain Richard Deeds, Airline Pilots Association, before the American Bar Association’s Aircraft Noise and Airport Access Panel (June 17, 1988) p. 88.
194. Air carriers are faced with local political pressure to impose even greater use restrictions, almost before the ink dries on the previously approved agreement. Without any national standards or guidelines the airlines are unable to effectively challenge the rash of local actions. Ellett, The National Air Transportation System: Design by City Hall?, 21st J. AIR. L. & COM. 1987; Henderson, Airlines Seek to Clip Board Wings; Noise Issue Pits Carriers, Agency they say, Wash. Post, July 18, 1988, at D1. A similar feeling of nobody-being-in-charge was reflected 30 years ago by Congressman Albert H. Busch:

My experience proved that each time I tried to pinpoint responsibility for noise nuisance there was "buck passing" from one agency to another. To me, it seemed necessary that we go into this question of responsibility and determine who was responsible in each given instance for a particular problem and then, if there was no specified area of
One air carrier association, the Air Transport Association of America, has repeatedly urged the FAA to assert greater federal control to limit the spread of use restrictions. But, the FAA has been impaired from moving boldly against use restrictions for several reasons.

- The legislative history behind the Federal Aviation Act and its Amendments supports broad local government authority in dealing with airport noise.
- The FAA has been unable to define clearly and convincingly when a use restriction unduly burdens interstate commerce in violation of the United States Constitution.
- Past Administrations have resisted preempting local airport noise abatement decisions for fear of having to assume the liability for noise injuries.
- The FAA has not been able to demonstrate that the costs of locally-imposed use restrictions outweigh any benefits.
- During the Reagan Administration, the Department of Justice was reluctant to sue states and local governments on behalf of the United States.

An important case which considered the issue of an airport use restriction's burden on interstate commerce was United States v. County of Westchester, 340 U.S. 349 (1951), federal courts have typically required proof of both a "national objective" and a "conflict" before overturning local actions. Note, A Framework for Preemption Analysis, 88 Yale L.J. 363 (1978).

An important case which considered the issue of an airport use restriction's burden on interstate commerce was United States v. County of Westchester, 571 F. Supp. 786 (S.D.N.Y. 1983). But, because of Justice Department policy limiting suits against local governments, the issue has not been frequently litigated.
It is difficult for the FAA to challenge the basis for a use restriction, because Agency representatives seldom are part of the process which decides the restriction is needed.202 Some use restrictions are beneficial to federal interests.203

Notwithstanding these limitations, the last two FAA administrators during the Reagan Administration, Donald Engen and Allan McArtor, advocated the need for a "national noise policy"204 which would have: mandated the submission of any noise-based operating restriction to FAA for review; established a private right of action for air carriers to litigate airport use restrictions; allowed airports to impose noise-based charges to help finance noise abatement projects; and imposed a stage 2 aircraft operating ban effective in the year 2000 or 2005. But, both Administrators failed to win the support of their Secretary of Transportation.205 Among the important justifications in 1988 for the Secretary of Transpor-

take vigorous legal actions against airports which imposed use restrictions which burdened inter-
state commerce. Helms, Noise Pollution and Airport Regulation, 47 J. AIR L. & COM. 405, 411 (1982). But, no such wave of legal action was forthcoming. Frankly, use of the courts is not a very good method to fashion a national airport policy. The FAA's ability to move quickly against airports is hampered by Justice Department concepts about the proper federal/state balance of authority. Even if justice approval and support is obtained, a case may languish in the courts for two, three, or more years. Also, results in court cases can leave the federal government and the airport with lingering bitterness, which impair future working relationships.

Some have suggested a private right of action which would allow air carriers to sue airports for failure to comply with federal statutory requirements. The pros and cons of such a right are discussed in Ceruzzi, Quasi-Regulation of a Deregulated Industry by a Safety Agency, 54 J. AIR L. & COM. 889, 918-22 (1989).


203. The FAA has agreed to restrictions barring scheduled air carrier service from a new general aviation reliever airport in Palm Beach County. The restriction was supported by the FAA because the construction of the new airport reduces congestion at Palm Beach International, and the sponsor of the GA airport also operated Palm Beach International and could "assure that the air carrier needs on the Palm Beach area are fully met." Letter from Quentin S. Taylor, FAA, to Bruce V. Pelly, Palm Beach International Airport (July 6, 1988).

Because of restrictions the early opposition to the Concorde aircraft subsided, allowing reg-
ular service in 1986. Allen, Ten Years of Concorde Operation: The SST is a Proven Airport-


The idea of a "national noise policy" is not new. E.g., Note, Jet Noise in Airport Areas: A National Solution Required, 51 MINN. L. REV. 1087 (1967).

205. In 1986 Secretary Elizabeth Dole returned Administrator Engen's proposal to the FAA stating that several issues were not resolved: the economic impact on air carriers; international repercussions; federal liability for noise damages; and the likelihood of strong resistance from local governments. Memorandum from Elizabeth Dole to Donald Engen (Oct. 2, 1986). In 1988 Secretary Burnley halted Administrator McArtor's promotion of a national noise policy stating it would be presumptive for the federal government to tell local communities what to do. Secretary Burnley cited President Reagan's Executive Order 12,612. Collogan, The Furor over Airport Ac-
cess, BUS. & COM. AVIATION, May, 1988, at 106.
tation's rejection of a "national noise policy" was President Reagan's Executive Order on Federalism.\textsuperscript{206} That Order announced an Executive Branch policy favoring local solutions to conflicts unless there was a clear "problem of national scope."\textsuperscript{207}

When the Bush Administration took office, the issue of a national airport noise policy came up again. Many hoped the Administration's proposal to publish a national transportation policy would lead to the formation of a comprehensive, broad-based aviation noise position. Unfortunately, when the policy was finally unveiled in February 1990 no such policy was present. The Report merely stated:

The [aircraft noise] issue is complex, involving concerns over liability for noise impacts, the financial cost of upgrading aircraft noise control standards, and protection of interstate commerce. Interested parties, including the airline industry and State and local governments, have presented a panoply of options ranging from a completely hands-off approach to the issue at the Federal level, to continuation of the current system, to total preemption of State and local regulation of aviation noise. The Department [of Transportation] is committed to improving environmental quality and providing leadership that will promote the effective utilization of system capacity in order to meet the demands of interstate commerce while recognizing the rights of State and local governments to impose land use controls. The impact of noise restrictions, phasing out of stage 2 aircraft, and effective local land use controls around airports should all be considered in resolving this issue.\textsuperscript{208}


\textsuperscript{207} President Reagan's Federalism Executive Order directs federal agencies to take the concerns of local governments and states into account when developing and implementing agency policy initiatives. The Order's goal is to achieve federal objectives with the least possible adverse effects on the operations and functions of states and local governments. The Executive Order has several features intended to limit federal intrusiveness in sub-federal government affairs.

- Federal agencies must consult with affected states or their political subdivisions during the development of proposals with federalism implications.
- The Office of Management and Budget (OMB) will assess an agency's performance under the Executive Order when the agency submits its regulatory and legislative initiatives for OMB review.
- The Order states that federal agencies may not propose regulations or new legislation affecting the states unless the problem is truly national in scope, and the states, acting individually or together, cannot effectively deal with the problem.

\textsuperscript{208} DEPARTMENT OF TRANSPORTATION, MOVING AMERICA: NEW DIRECTIONS, NEW OPPORTUNITIES 74-75 (1990). Whether a national noise policy ought to include a national noise standard is a matter of considerable controversy. Wesler, Federal Noise Standard Not Workable, 1 AIRPORT NOISE REP. 191 (1989).

For a comparative analysis of how other nations deal with aircraft noise problems see ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, FIGHTING NOISE: STRENGTHENING NOISE ABATEMENT POLICIES (1986).
C. FAA'S AIRWAY AND AIRPORT CAPACITY EXPANSION INITIATIVES FACE MULTIPLE ACCOUNTABILITY AND PLANNING CHALLENGES

1. FAA'S ONCE BROAD DISCRETION IN MANAGING AIRSPACE HAS COME UNDER GREATER PUBLIC SCRUTINY BECAUSE OF AIRCRAFT NOISE

With mounting concern over capacity shortfalls in the national air transportation system, the FAA is committing more resources to finding solutions to reduce airways and airports congestion. Since the FAA's talent and experience are weighted toward the management of the airways, much of the Agency's focus has been on improving the flow of traffic in navigable airspace.

An example of this focus was the creation of "flow control" in the 1980s. Through this process the FAA seeks to control more efficiently the movement of civil aircraft between major airports. The Agency's Central Flow Control facility in Washington, D.C. uses computers which monitor the national weather picture and anticipated aircraft operations. From this facility FAA personnel are able to smooth air traffic demand among the regions of the country, by rerouting traffic and allowing delays to be taken on the ground at the point of departure rather than in holding patterns at the destination airport. While this approach cannot always be aware of all localized flight conditions, and may result in erroneous decisions in select cases, it has had an overall beneficial impact on the system.

In addition to such centralized control, the FAA is also considering alternatives to better manage traffic in the vicinity of airports. Here the problem is largely the existing FAA rules which disperse aircraft because of poor weather conditions, wake turbulence, and other problems. But, with advances in technology, the FAA may be able to amend its procedures to reduce spacing, and thus increase the volume of traffic which the airways can accommodate. Matters which are receiving FAA attention in this regard, include:

209. OFFICE OF TECHNOLOGY ASSESSMENT, AIRPORT AND AIR TRAFFIC CONTROL SYSTEM 17-18 (1982); Poritzky, Airports, Airports—Where's the Capacity?, AEROSPACE AM., Jan. 1985, at 27. Flow control was used during the FAA air controller's strike to manage air traffic safely with a smaller workforce.

210. Central Flow Control has its opponents, such as general aviation users, which believe that flow control is an infringement on the public right of transit. Also, the military services are concerned because flow control could lead to losses in special use airspace.

• improving real-time information on winds and wind gradients;
• gathering actual aircraft performance data to support safe separation reductions;
• applying simulation modeling techniques to evaluate alternative traffic flows;
• developing cockpit traffic displays to provide better situation and traffic information to pilots; and
• reviewing different technology and procedures to allow the simultaneous or near simultaneous use of more than one arrival runway during most weather conditions.

Also, the Agency’s air traffic managers are studying multiple options to increase the number of routes into and out of major airports. The first test of such initiatives occurred in 1987 when the FAA began to reroute traffic in and out of LaGuardia, Kennedy, and Newark Airports. But, this effort, called the “Expanded East Coast Plan,” created noise impacts over several New Jersey communities which had not previously perceived a noise problem. Angry homeowners eventually sought the support of their congressmen who put considerable pressure on the FAA to shift flight corridors away from certain communities. In studying the circumstances surrounding the Expanded East Coast Plan, the General Accounting Office noted several factors which may have hindered a resolution of the controversy:

212. For twenty years the FAA has been promoting the Microwave Landing System (MLS) to enhance system capacity and mitigate noise complaints. The success of that system, however, requires the support of the airports and users to be implemented. To date, support for MLS has not materialized. NAT'L COUNCIL ON PUBLIC WORKS IMPROVEMENT, THE NATION'S PUBLIC WORKS: REPORT ON AIRPORTS AND AIRWAYS 60 (1987); Feldman, Noise Growing as Major U.S. Orphan Paying for Noise Control, AIR TRANSPORT WORLD, Dec. 1987, at 32; Stretching Airports, FAA HEADQUARTERS INTERCOM., Apr. 25, 1989, at 1.

213. The FAA is studying or planning to study routing redesigns for the following airports: Los Angeles, Boston, Chicago, Dallas-Fort Worth, Denver, Houston, Kansas City, Miami, Atlanta, Indianapolis, Jacksonville, Anchorage, Albuquerque, and Salt Lake City. DOT/FAA, AIRPORT CAPACITY ENHANCEMENT PLAN (DOT/FAA/CP-89-4 (1989)).

214. Opponents of the Expanded East Coast Plan organized early and well. Many kept private logs of aviation activity and wrote frequently to the Port Authority, New York State, New Jersey State, the FAA Regional Office, and FAA Headquarters. The citizen groups had ammunition to show government incompetence when they received inconsistent letters from different government offices. Robert Kaplan of Marlboro, New Jersey claimed to have letters from FAA Headquarters and the FAA Regional Office, one letter stating the aircraft flying over his house were Kennedy and Laguardia departures at 9000 to 17,000 feet above ground level, the other told Mr. Kaplan he was hearing arrival traffic at 3000 feet. Winerip, Our Towns: Thirty Seconds Over Marlboro, An Aerial Din, N.Y. Times, Dec. 6, 1988, § B, at 1, col. 1. See also Leading Fight Against Airport Noise, N.Y. Times, Nov. 6, 1988, sec. 12NJ, at 1, col. 1; Witkin, Plan to Avert Air Traffic Delays on East Coast is Starting Today, N.Y. Times, Feb. 12, 1987, at A1, col. 3.


216. GENERAL ACCOUNTING OFFICE, AIRCRAFT NOISE: IMPLEMENTATION OF FAA’S EXPANDED EAST COAST PLAN (RCE-88-143 (1988)).
The FAA had not prepared an environmental assessment of the planned route changes.\(^{217}\)

The FAA did not seek public review and comment on the proposed plan.

The FAA did not evaluate the extent to which the economic benefits of its plan might be offset by social costs in the affected communities.

FAA’s method of evaluating potential community responses to aircraft noise did not alert agency planners to the strong community opposition which occurred.

FAA’s approach to evaluating the impacts of noise and alternatives to mitigate its effects,\(^{218}\) differed from the evaluation strategies of the State of New Jersey and the Port Authority of New York and New Jersey.

As a result of the controversy over the Expanded East Coast Plan, the FAA is reviewing its policy and procedures concerning “enroute noise”\(^{219}\) and air traffic operational changes. In particular, the Agency’s leadership is taking a careful look at how community impacts are considered during the early stages of air traffic planning.\(^{220}\) Without a commit-

\(^{217}\) Since the route changes in the Expanded East Coast Plan all occurred at altitudes over 3000 feet above ground level, planners relied on a categorical exclusion in the FAA’s environmental regulations which waived the requirement for an environmental assessment for flights at those altitudes. But, the GAO noted that the FAA’s regulations recommend an environmental assessment for any categorically-excluded action which has the potential for public controversy. Notwithstanding this recommendation, the FAA did not prepare an environmental assessment even after the public concern was obvious. Id.

It is not uncommon for the FAA and airports to receive noise complaints for flights above 3000 feet. E.g., Departure Noise, AVIATION WEEK & SPACE TECH., Feb. 27, 1989, at 15 (citing fact that Raleigh-Durham Airport receives noise complaints from residents of Fayetteville sixty miles south of the airport at 10,000 feet).

\(^{218}\) Notwithstanding early ineptness in dealing with New Jersey residents, the FAA in 1988 began working with the Port Authority to monitor noise levels, adjust flight routes, and consider various citizen recommendations. Rangel, Pact is Reached to Cut Jet Noise Over New Jersey, N.Y. Times, Aug. 29, 1988, § B, at 3, col. 6.


\(^{220}\) See GENERAL ACCOUNTING OFFICE, AIRCRAFT NOISE: STATUS AND MANAGEMENT OF FAA’s WEST COAST PLAN (RCED-89-84 May 1989). In 1989, FAA Headquarters sponsored a 3-day policy review to look at possible changes to integrate environmental concerns into agency decision making. In particular there needs to be a closer working relationship and accountability between the ATC and community relations functions of the Agency. Interview with James Densmore, Office of Environment, FAA, in Washington, D.C. (Aug. 29, 1989).
ment to resolve community conflicts early in the planning process, it is likely that important air traffic control changes will be delayed because of public opposition.

2. **While FAA Forecasts in Support of Airways Capacity Enhancement are Useful, Additional Resources May be Required to Develop Credible Airport Activity Predictions**

Among the important factors influencing airway and airport capacity enhancement planning is the prediction of future aviation demand. While such forecasting is important for the efficient use of government resources, it is a challenging endeavor with many critics.221

Of course, aviation forecasting is risk-laden because commercial air transport activity is closely tied to the everchanging, often unpredictable domestic and international economic environment.222 Present conditions which affect economic activity, and thereby air transportation, include:223 widening gaps between wealth and poverty; declining personal savings; regional and international migration pressures; corporate mergers and buyouts; constantly changing technology;224 shifts in government tax, fiscal and monetary policies;225 changes in production, marketing, and dis-

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221. *E.g.*, D. Nelkin, Jetport: The Boston Airport Controversy 51 (1974); Milch, Inverted Pyramids: The Use and Misuse of Aviation Forecasting, 6 SOC. STUD. SCI. 5 (1976) (claiming that aviation forecasting is like an inverted pyramid because great decisions stand on little, and often questionable, information).

See also Massey, Airports Spin the Wheel of Fortune, AM. DEMOGRAPHICS, Feb. 1988, at 42.


224. An example of changing technology is the development of the "tiltrotor" aircraft under a joint Marine Corps/Federal Aviation Administration program. The aircraft combines the speed of fixed-wing planes with the advantage of vertical-takeoff-and-landing capability. Fleets of these aircraft in the civil sector could serve short-haul routes from facilities close to city centers, relieving congestion at major airports. But, the operating costs would likely be significant; and the increased aviation activity out of small airfields would likely generate noise complaints. See Frank, A New Angle in Transportation: Tiltrotor Aircraft May Solve the Problem of Congestion at Civilian Airports, L.A. Times, July 4, 1989, § 4, at 1, col. 2; Takagi, STOL May Give Flight to Aviation Industry, JAPAN ECON. J., Apr. 15, 1989, at 28 (discussing Japanese development of tiltrotor aircraft); Vine, Tilt-Rotor Aircraft: A Cure for Airport Congestion, 26 Airport Services, Nov. 1986, at 43. But the tiltrotor research and development program was put in jeopardy when the Secretary of Defense cut the funding for the plane from the President's Defense Budget. Morgan, Private Interests Converge and Clash as Funding Lines are Drawn, Wash. Post, July 25, 1989, § 2, at A4.

225. Changes in political climate, including which party is controlling the national agenda, affect economic conditions for business and industry. Beck, Parties, Administrations, and Ameri-
tribution of goods caused by the use of advanced information systems; and improvements in communication.\textsuperscript{226}

Notwithstanding the challenges of tracking and interpreting such factors, experienced FAA personal have developed a favorable reputation in publishing forecasts of air transportation activity.\textsuperscript{227} Among the forecasts which they prepare and distribute are:\textsuperscript{228} air carrier forecasts; regional forecasts; commuters forecasts; general aviation forecasts; FAA workload forecasts; and terminal area forecasts. These forecasts are used by the FAA to plan and budget for air traffic personnel and equipment.\textsuperscript{229} But using such forecasts in airport infrastructure planning has always been problematic. While there are formulas for converting national, state, and regional forecasts into individual airport forecasts,\textsuperscript{230} the special needs of airport planners and the diversity of local conditions usually require additional forecast refinement. The following considerations are associated with preparing forecasts for airport purposes:\textsuperscript{231}

- local traffic pattern operations;
- mix of aircraft based at or using airport;
- different air cargo,\textsuperscript{232} air mail, international, and passenger requirements;
- estimates of peak hour activity;


\textsuperscript{226} Many have suggested that air travel may be reduced with advances in telecommunications. \textit{See} Pool, \textit{The Communications/Transportation Tradeoff}, in \textit{Transportation Policy} 181 (A. Alshuler ed. 1979).


\textsuperscript{229} The FAA Forecasting System: Theory and Practice presented by the FAA’s Forecasting Branch at the Regional Workshop on Aviation Forecasting and Economic Planning, Mar. 2 to 6, 1987, (Bangkok, Thailand). \textit{See also} FAA, FAA AVIATION FORECASTS: FISCAL YEARS 1989-2000, 168 (FAA-APO-89-1 (1989)).

\textsuperscript{230} FAA, AIRPORT MASTER PLANS, June 1985, at 24-27 (Advisory Circular 150/5070-6A).

\textsuperscript{231} \textit{Id.} at 23. \textit{See also} J. Wiley, \textit{Airport Administration and Management} 92 (1986).

\textsuperscript{232} A special challenge is the forecasting of air cargo activity. Distinctly different patterns of demand exist between air cargo and passenger traffic. Whereas passengers prefer day-time travel, the demand for cargo service is greater at night. Passenger traffic is high during vacation periods. But, when people are on holiday—and because they are—cargo activity is down. The geographic distribution of passengers and cargo is likewise quite different. Major tourist destinations are not likely important centers for cargo. While passengers are of comparable size with similar requirements, cargo comes in varying sizes and may require special handling (because it is alive, or because it is dead and needs refrigeration). Also, air cargo is a very fragmented industry. Freight can be handled by a hundred or more companies at an airport, and there is no industry standard for shipment size, configuration, or documentation. R. De Neufville, \textit{Air Cargo in the 1980s and Beyond} (1984).
local demographic factors; \(^{233}\)
- likelihood of highway and other infrastructure support for airport expansion initiatives;
- secondary development associated with airport activity, and its effect on the community/region;
- existence of alternate airports which might accommodate or capture additional aviation activity; \(^{234}\)
- timing of the forecast to be most useful for master plan and environmental decision making; \(^{235}\)
- valid methods to collect and audit data used in support of airport forecasts; and
- influence of local political climate on future air transportation growth in community/region.

Typically, the FAA relies on airport sponsors to collect data, prepare, and validate many forecasts as part of the airport master planning process. Some experts have claimed such locally-generated forecasts lack quality and uniformity, and suggest ways for the FAA to promote better airport forecasts: \(^{236}\)

- standardize the kinds of data to be collected in support of airport forecasting;
- develop uniform units of measurement and uniform data collection periods for airport forecasts;
- improve the comparison of forecasts among airports within the same region, and between airports and regional/state/national forecasts;
- increase FAA-sponsored education of forecasting skills for airport planners and their consultants;
- disseminate FAA-prepared studies and information in a timely manner when needed for airport forecasting efforts; and
- create a library of all airport master plans and forecasts for use by airport planners at all levels of government.

Of course, all these considerations mean the development of airport activity forecasts can be a costly enterprise. But, if valid forecasts are not created, the public and the aviation industry risk poor planning, and the inefficient use of scarce resources. Assuming the problem is primarily money and not know-how, the decision whether to adequately fund airport activity forecast becomes an important policy choice for government officials.

\(^{233}\) Local factors which influence demand for airport services include: changes in absolute median family income; in-migration as a percentage of population; level of government employment; changes in level of manufacturing employment; accessibility to institutions of higher learning; tourist expenditures. S. GOMES, STATE AIRPORT SYSTEM PLANNING, ch. 5 (1976).


\(^{235}\) An example of a mistimed forecast which disrupted the decision-making process is discussed in E. BRIGHT, AIRPORT AREA PLANNING AND IMPLEMENTATION 49-52 (1980).

3. **IMPROVED AIRPORT PLANNING COULD SUPPORT BETTER ALLOCATION OF FEDERAL, STATE, AND LOCAL RESOURCES**

Assuming credible airport activity forecasts can be developed, they become an important part of government planning for airport capacity enhancement. In such planning the federal government contributes by publishing the National Plan of Integrated Airport Systems and by funding state and regional airport system plans, and individual airport master plans. Of course, airport planning, like forecasting, is under constant scrutiny by those interested in a more efficient use of resources.

The most comprehensive airports plan in the United States is the biannual National Plan of Integrated Airport Systems (NPIAS) published by the FAA. In the NPIAS the FAA draws selectively from individual airport, regional, and state plans and studies to identify airport construction projects potentially eligible for federal funding. While not every airport in the United States is listed, the NPIAS lists all commercial and reliever airports, and many of general aviation airports. The bulk of the plan is a state by state cataloguing of airports, including information about numbers of based aircraft, annual operations, and planned projects combined under five broad construction/acquisition categories. Additionally, the NPIAS summarizes selected policies and concerns relating to airport development in the United States. Among the topics covered are: airport

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238. The preparation of an airport master plan can be one of the more important vehicles to foster consensus among diverse interests. A good master plan has the following characteristics: Anticipates issues and data required by applicable environmental reviews; involves public, community, regional, national leaders and users; ensures that all relevant community plans, goals, and objectives are identified and every effort is made to develop an airport plan consistent with them; clarifies institutional responsibilities necessary for project implementation; establishes schedules, financial resource plans; has specific land use planning, real estate acquisition or exchange, and economic development plans; identifies the airport’s role in the regional and national air transportation systems; has a credible cost-benefit analysis of any potentially-controversial projects; thoroughly investigates all reasonable capacity enhancement alternatives; contains details of all off-airport planned development and socio-economic factors; carefully analyzes land banking opportunities; sponsor conducts one-on-one meetings with affected entities, rather than just written communication; forecasts aviation activity; discusses ground access problems and alternatives. FAA, AIRPORT MASTER PLANS (Advisory Circular No. 150/5070-6A, 1985). See also Gilbert, New Airports Won’t Come Easy, AIRPORT SERVICES, May, 1988, at 30.

activity forecasting policy and process; airport congestion information; FAA policy concerning airport safety; discussion of ground access to airports; review of non-construction alternatives to increasing airport capacity; affects of airline deregulation; and airport financing options.

As a compilation of state, regional, and local government construction plans, the NPIAS has been criticized as too narrowly focused on public works infrastructure. Also, the NPIAS fails to prioritize among the many airport capacity enhancement alternatives. Likely, additional or more detailed information could be provided to make it a more useful national planning tool. Such information might include:

- analysis and prioritization of airports as contributors, or likely contributors, to local, regional, and national economies;
- data concerning the population served by each airport;
- prioritization of projects intended to enhance airport capacity;
- a plan of action and prioritization of initiatives to reduce the conflicts over airport noise;
- the identification of additional real estate interests needed for capacity enhancement or noise abatement, along with a prioritization for acquisition;
- additional information and implementation plans for all non-construction alternatives to capacity deficiencies; and
- a review of other government agency activities which affect federal interests in airports.


242. During the passage of the Airport and Airway Safety and Capacity Expansion Act of 1987, the House and Senate conferees emphasized the need for a national airport plan which prioritized airport capacity enhancement projects, especially in metropolitan areas. 133 Cong. Rec. H11696 (Dec. 18, 1987) (remarks of Congressman Hammerschmidt).

243. Much of the controversy over the NPIAS and its predecessors has been over efforts to define the “federal interest” in airports. But, it may not be possible or even desirable to develop a single simple definition of federal interest. It appears that Congress prefers to define federal involvement in airports broadly. Additionally, the federal interest is shaped by tradition and precedent, and by changing national goals and policies from outside the transportation sphere.

The FAA’s position is that federal responsibility for an adequate system of airports is not coextensive with the federal interest in safety. While FAA’s interest in safety extends to every landing area in the nation, the Agency’s concern for a national system of airports “extends only to those public use airports which make a significant contribution to air transportation needs.” FAA Order 5090.38, Sept. 9, 1985, Field Formulation of the National Plan of Integrated Airport Systems (NPIAS).
Much of the data for these analyses is already within the FAA. But, the publication and wide dissemination of such information has been restricted for political and budgetary reasons within the executive branch.\footnote{244}

4. **Many of the Uncertainties Associated with the Federal Role in Airport Development Are Accented in the Federal Airport Grants Program**

Generally, the NPIAS and other airport planning occur as a condition to and in support of government funded airport construction projects. For years\footnote{245} the federal government has contributed considerable resources...
to airport development. The current federal airport grant program, known as the Airport Improvement Program (AIP), is administered by the FAA. Under the AIP, an airport listed in the NPIAS can apply for federal funds in support of several types of airport projects. In applying for a grant, the airport sponsor or other eligible grant recipient must make certain "assurances" that legal requirements have been complied with, and must agree to several conditions upon the receipt of federal funds.

Within the last few years the federal expenditures for airports have increased to about $1 billion annually. But this amount still satisfies less than half the projects recognized and approved in the NPIAS. Given these annual deficiencies, the FAA must select among projects.

246. The two most important factors influencing airport development are real estate ownership and revenue sources.


248. AIP projects include: site preparation; airfield paving, marking, and signage; airfield lighting and electrical work; navigational aids; terminal, airport roads, walkways construction; safety, security, and support equipment; land acquisition for airport development and noise compatibility; residential noise attenuation. Projects which the FAA will not fund under AIP are: fuel farms; landscaping, general aviation terminals; communication systems (except that which is used for safety/security); hangars; and public parking facilities for passenger automobiles. DOT/FAA, AIRPORT IMPROVEMENT PROGRAM (AIP) HANDBOOK (Oct. 24, 1989) (FAA Order 5100.38A). The FAA has recently reassessed how it will administer AIP funds used for noise abatement projects. DOT, ELIGIBILITY OF NOISE ABATEMENT PROPOSALS FOR GRANTS-IN-AID UNDER THE AIRPORT IMPROVEMENT PROGRAM (DOT/FAA/PP-89-2 (1989)).

249. There are about 30 "assurances" which a grant recipient must make. They include such things as sponsor authority and fund availability; good title; consistency with local plans and consideration of local interest; consultation with users and public hearings; air and water quality standards; accounting, audit, and recordkeeping requirements; minimum wage compliance; civil rights; and economic nondiscrimination. Special conditions, which are attached to the grant agreement, vary depending on the project and its intended use. Id. See discussion of statutory obligations of recipients of federal airport grants-in-aid funds in Ceruzzi, Quasi-Regulation of a Deregulated Industry by a Safety Agency, 54 J. AIR L. & COM. 889, 909-16 (1989).

250. DOT, AIRPORT IMPROVEMENT PROGRAM EFFECTIVENESS STUDY (DOT-P-36-87-6 (1987)). Generally, the states have not made large contributions to airport development. But, that trend may be changing with states such as Maryland and Florida supporting airport development as a key to the states' long term economic growth. See NAT'L GOVERNORS' ASS'N, SUCCESSFUL AIRPORT CAPACITY EXPANSION (1989) (citing recent state expenditures to: develop marketing plans to attract air carrier business; speed up master planning and construction of airport projects; create citizen advisory groups to solve conflicts over noise; support better coordination between airport and highway planning; and purchase necessary land for present and future airport needs).

251. Total annual demand for airport capital investment, including all airside and landside projects, is $5.6 billion in the United States. But, not all projects are eligible for federal aid. Projects eligible for AIP funds total about $2.5 billion annually. NAT'L COUNCIL ON PUBLIC WORKS IMPROVEMENT, THE NATION'S PUBLIC WORKS: REPORT ON AIRPORTS AND AIRWAYS 35-37 (1987).
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based on its interpretation of the federal interest in airports. 252

Within the discretionary authority provided the FAA, the Agency has
given higher priority to airport projects which enhance capacity and re­
duce delays, especially in the major metropolitan areas. 253 While, such
emphasis is important to the commercial aviation sector and to their pas­
sengers, it is not mandated by the law. Rather, the statutes emphasize
that federal funds shall support a "balanced" system of airports. 254 Regularly, members of the U.S. House of Representatives remind the FAA
that smaller, uncongested rural airports shall receive AIP funding. 255

Others criticize FAA’s management of airport grant funds as placing
insufficient emphasis on the efficient use of existing facilities, or on certain
long term problems. Illustrative of these concerns are the following:

- grant funds are not managed aggressively to reduce the impact of persis­
tent environmental problems;
- too low a priority is given to the acquisition of land for future airport develop­
ment (land banking);
- neither the administration of AIP funds, nor the funds themselves, contrib­

252. Of course, valid prioritization can only occur after the project sponsor satisfies numer­
onous prerequisites, including adequate planning and environmental documentation. There is a
concern that project proponents, once they make an early commitment to pursue a particular
project, will rush the required preliminaries. See E. Bright, AIRPORT AREA PLANNING AND IMPE­
LEMENTATION 168-70 (1980).

253. DOT, AIRPORT IMPROVEMENT PROGRAM EFFECTIVENESS STUDY (DOT-P-36-87-6 (1987));
DOT, A FAA BENEFIT-COST ANALYSIS OF THE AIRPORT IMPROVEMENT PROGRAM (AIP), FISCAL
YEARS 1982 THROUGH 1985 (FAA-APC-86-3 (1986)); FAA Order 5100.38, AIRPORT IMPROVE­
MENT PROGRAM (AIP) HANDBOOK, at 29-32 (Feb. 11, 1985); Poritzky, Airports, Airports—Where’s
the Capacity, AEROSPACE Am., Jan. 1985, at 27. Such emphasis is not new. See Statement of
FAA Administrator Najeeb Halaby printed in R. BURKHARDT, THE FEDERAL AVIATION ADMINIS­
TRACTION 156-59 (1967).

Among the criticisms lodged against the FAA’s interest in large airport capacity expansion
are the following:

- given the lack of national planning which supports these expenditures, the federal
government is not getting the most benefit for its money; and
- since many large airports are dominated by only one or two carriers, substantial fed­
eral grants to these airports may be an inappropriate subsidy to select commercial
airline corporations.

Minerva, Airports Adopt to Deregulation, Credit Week, Standard & Poor’s, at 1, Aug. 22, 1988.

Interestingly, the Reagan Administration considered eliminating aid to large airports during
the early 1980s, as a means to reduce federal expenditures. Eventually, those favoring retention
of federal influence over airport capacity in metropolitan areas prevailed. See DOT/FAA, THE
EFFECT OF AIRPORT DEFEDERALIZATION (DOT-P-36-87-4 (1987)); J. PLAIGNAUD, AIRPORTS AND

defining the federal interest in federal grant programs, see CONGRESSIONAL BUDGET OFFICE, THE
FEDERAL GOVERNMENT IN A FEDERAL SYSTEM CURRENT INTERGOVERNMENTAL PROGRAMS AND OP­
TIONS FOR CHANGE (1983).

255. See, e.g., S. RHOADS, POLICY ANALYSIS IN THE FEDERAL AVIATION ADMINISTRATION 35-
38 (1974); Letter from Representatives Glenn Anderson, John Paul Hammerschmidt, Newt Ging­
rich, and Norman Mineta to FAA Administrator Allan McArtor, Apr. 12, 1988.
ute significantly to curtailing incompatible development in the vicinity of airports;\textsuperscript{256} and

- the FAA does not require grant recipients to consider and adopt noninvestment capacity enhancement solutions as part of the grant application process.\textsuperscript{257}

Similar concerns have been raised about the Airports and Airways Trust Fund,\textsuperscript{258} used to support the AIP. That fund was created in 1970 to finance airport and airway improvements through proceeds of user

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{256} 49 U.S.C. § 2210(a)(5) (Supp. 1989) requires that an AIP grant applicant provide the FAA an assurance that "appropriate action, including the adoption of zoning laws has been or will be taken, to the extent reasonable, to restrict the use of land adjacent to or in the immediate vicinity of the airport to activities and purposes compatible with normal airport operations, including landing and takeoff of aircraft." The FAA requires grant applicants to provide a "brief description" of their efforts at achieving land use compatibility, or if no action was taken, why not. FAA, AIRPORT IMPROVEMENT PROGRAM (AIP) HANDBOOK, at 163, Feb. 11, 1985 (FAA Order 5100.36). Generally, the needs for airport development, the typical disharmony among neighboring local jurisdiction, and the federal policy against interfering with local land use matters have discouraged the FAA from pursuing a tougher stand on land use compatibility through the AIP. See E. BRIGHT, AIRPORT AREA PLANNING AND IMPLEMENTATION 60-63 (1980); Airport and Aircraft Noise Reduction, Hearings before the Subcomm. on Aviation and the House Comm. on Public Works and Transportation, 95th Cong., 1st Sess. 3 (1977) (statement of Congressman Gene Snyder).
\item \textsuperscript{257} A. GHOBRIAL, ANALYSIS OF THE AIR NETWORK STRUCTURE: THE HUBBING PHENOMENON (1983); NAT'L COUNCIL ON PUBLIC WORKS IMPROVEMENT, THE NATION'S PUBLIC WORKS: REPORT ON AIRPORTS AND AIRWAYS 51-52 (1987); CONGRESSIONAL BUDGET OFFICE, NEW DIRECTIONS FOR THE NATION'S PUBLIC WORKS (1988). Berry, Airport Presence as Product Differentiation, 80 AM. ECON. REV. 394 (1990). The most commonly discussed non-construction alternative is "peak-hour pricing," meaning an increase in landing fees or some other charge for those aircraft using the airport during the most congested periods. Such funds would be used for added capacity expansion projects. The disadvantages of such congestion pricing include:
\begin{itemize}
\item the fee could possibly overcompensate for congestion problems, thus unfairly burdening system users;
\item the existence of additional funds could increase the pressure for new construction (an "embarrassment of riches") without careful consideration of community impacts;
\item fixing an appropriate peak-hour fee would be difficult because of differences in weekly and seasonal traffic flows; and
\item peak hour pricing would have a possible unwanted ripple effect on other airports in the system.
\end{itemize}
\item Eckert, An Evaluation of the Airport Development AID Program, in PERSPECTIVES ON FEDERAL TRANSPORTATION POLICY 117, 126-29 (J. Miller ed. 1975).
\end{itemize}
\end{footnotesize}
Users pay special taxes on aviation fuel, passenger tickets, international travel, air freight shipments, and so forth. Theoretically, a system of user charges should encourage aviation users to improve the efficiency of the system. But, under the Airports and Airways Trust Fund charges are not directly tied to the use of the system. Consequently, little economic efficiency is achieved through the collection of revenue.

5. **The FAA Has Supported Efforts to Acquire Real Property Interests for Airport Development and Noise Abatement, But the Agency Could Do More**

While the availability of funds for airport construction plays an important role in assuring capacity, an equally important factor is the ownership of sufficient real estate interests for aviation activity. An airport sponsor with substantial fee owned land and easements in surrounding property

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259. Since its creation, the Trust Fund has sparked controversy between the Congress and the President. Congress claims the fund is primarily an account for capital projects to assure adequate aviation system capacity. But, each Administration since 1971 has claimed that the Fund should help finance all aviation programs, including FAA operations. At various times over the past twenty years the Fund has shifted back and forth between being a capital account and a full user-pay system. Recently, the Congress has claimed the Executive Branch purposefully limited spending on capital projects, in order to use the fund surplus for operations and to count it as an offset against the growing federal budget deficit. Based on this perception, Congress passed legislation linking the FAA's use of Trust Fund revenue for FAA operations to the level of expenditures for capital projects. See H. MERTINS, NATIONAL TRANSPORTATION POLICY IN TRANSITION 50-51 (1972); CONGRESSIONAL BUDGET OFFICE, THE STATUS OF THE AIRPORT AND AIRWAY TRUST FUND (1988); NAT'L COUNCIL ON PUBLIC WORKS IMPROVEMENT, FEDERAL TRUST FUNDS: OPTIONS TO USE THE CASH (1987). The problem with this wrangling between the two branches of government is that the surplus in the Trust Fund continues to grow, creating a public perception that aviation system users are being denied benefits from the taxes they paid. Airport 1987, Pilot (Norfolk, Va.), May 17, 1987, Editorial, reprinted in 133 CONG. REC. E3348 (daily ed. Aug. 7, 1987).

260. Another item of contention has been the claim that general aviation users pay a much lower percent of the total cost of their burden on the system than do the commercial aviation users. Allegedly, the commercial sector pays nearly equivalent the amount of their burden on the system, while general aviation pays less than one-fourth of their burden. CONGRESSIONAL BUDGET OFFICE, NEW DIRECTIONS FOR THE NATION'S PUBLIC WORKS 58-59 (1988). Of course, such comparisons may be suspect because of the many different ways of determining both the "burden" and the "system". See DOT, AIRPORT AND AIRWAY COST ALLOCATION STUDY (1973) (citing at least ten ways to evaluate costs created by aviation activity).

261. The bulk of the Trust Fund revenue is collected from a tax on tickets. This tax and the other trust fund taxes are relatively easy to collect, but they are not a function of system usage. If the taxes were more closely associated with usage, greater system efficiency might be achieved. Suggested use-based fees might include: charges for flight plans with the amount of the fee dependent on the value of the air traffic control services used; variable landing fees based on the services provided by the airport. But, such fees are often opposed for reasons of safety and added administrative costs. CONGRESSIONAL BUDGET OFFICE, POLICIES FOR THE DEREGULATED AIRLINE INDUSTRY 68 (1988); NAT'L COUNCIL ON PUBLIC WORKS IMPROVEMENT, FEDERAL TRUST FUNDS: OPTIONS TO USE THE CASH (1987); A. SINHA, AIRPORT AND AIRWAY COSTS AND USER COST RESPONSIBILITY (1977).
has greater flexibility in satisfying the competing demands by aviation users and community leaders.

In support of this need for real estate interests, the federal government has made substantial contributions. Many of the nation’s airports operate on property acquired by the United States and then transferred to local governments for airport use. Additionally, federal grant funds have been frequently used by communities to purchase additional real property for airport development and for noise abatement.

Notwithstanding this good record, FAA’s policies toward airport land acquisition are typically conservative or cautious, rather than proactive.

- The FAA often takes a passive role in the identification and capture of federal surplus real property and other federal lands for airport purposes.
- Given the importance of land assembly to the development of airport capacity, the FAA has relatively few employees with real estate and land use planning experience/ responsibilities.
- While the Agency has recommended land banking in support of future airport development, its own AlP fund priority system makes such land acquisition less likely.

Of course, deference to local land use prerogatives is the more com-

262. As of 1986 there were 638 airports in the United States which owned property which was previously transferred by the federal government to local government for airport purposes. FAA, LIST OF PUBLIC AIRPORTS AFFECTED BY AGREEMENTS WITH THE FEDERAL GOVERNMENT, (FAA Order No. 5190.2Q (1986)).

263. During Fiscal Years 1986 and 1987 the FAA approved: twenty-eight AlP grants, totalling $92.2 million, for land acquisitions for noise abatement and obstacle clearance; and twenty-four grants, totalling $50.27 million, for airport development land. DOT/FAA, AIRPORT CAPACITY ENHANCEMENT PLAN, appendix G (DOT/FAA/CP/88-4 (1988)). Between 1973 and 1979 grant funds totalling $23 million assisted local governments to acquire private airports, for public use. GENERAL ACCOUNTING OFFICE, AIRCRAFT DELAYS AT MAJOR U.S. AIRPORTS CAN BE REDUCED 19 (CED-79-102 (1979)).

264. When a federal agency determines that property is excess to its needs, a report is made to the General Services Administration, which notifies all other federal agencies of the availability of such property. Such notifications are common, with numerous announcements disseminated monthly. Once federal agency screening is complete, local governments can request transfer of such property for certain public purposes, including airport development. At one time the FAA screened all federal surplus property for possible airport use. Now, FAA policy and manpower limitations confine the FAA role to validating a local government’s claim for federal land in support of an aviation requirement. While FAA personnel have on occasion assisted local governments to identify federal surplus property, such assistance is not uniform. FAA, FEDERAL SURPLUS PROPERTY FOR PUBLIC AIRPORT PURPOSES (FAA Order, 5150.2A (1972)); Interview with Leonard Sandelli, at the FAA Headquarters, Washington, D.C. Aug. 10, 1989.

265. Most of the FAA’s real estate specialists only acquire land for FAA purposes, such as towers, navigational aids, FAA administrative offices, and so forth. Few employees have significant responsibilities in support of the real estate acquisition needs of airport sponsors. Id.

266. See DOT/FAA, AIRPORT LAND BANKING (1977); DOT/NASA, CIVIL AVIATION RESEARCH AND DEVELOPMENT POLICY STUDY: SUPPORTING PAPERS, ch. 6 at 44 (DOT-TST-10-5 (1971)).

monly expressed reason for a limited FAA role in real estate matters. Nevertheless, the Agency may have to assume a strong leadership role in order to enhance national airport capacity development.

IV. PROPOSED AIRPORT POLICY PRINCIPLES

Much of the difficulty in resolving airport noise and capacity issues exists because of the lack of clear accountability and the frequent absence of cooperative planning and leadership in the private and public sectors. But, changes in the status quo should begin with a consideration of policy principles around which consensus and understanding can grow. The following policy principles serve such a beginning.

268. DOT/FAA, AIRPORT LAND BANKING (1977) (noting the broad powers and responsibility of local governments to decide the need for land acquisition and control).

269. There have been recent FAA efforts to make more land available for airport development or prevent the loss of airport land to non-aviation uses. E.g. McGarry, FAA Presses for Aviation Use of Land Near Van Nuys Airport, L.A. Times, Feb. 22, 1985, § 2, at 6, col. 5; Letter from James Molley, FAA, to Defense Secretary's Commission, Nov. 10, 1985 Base Realignment and Closure. The FAA missed an opportunity to have airport needs listed among alternative uses for federal land in a recent executive order. Exec. Order No. 12,682, 3 C.F.R. 229 (1990).


272. Nearly all previous studies of the airport noise and airport capacity issues have recommended specific actions to be taken, without considering whether such actions were consistent with more general policy principles. Failure to consider and resolve the relationship between policies and actions typically undermine the usefulness of such studies. Examples of notable reports which recommended specific courses of action include: President's Airport Commission, The Airport and Its Neighbors (1952) (Doolittle Report); Industry Task Force on Airport Capacity Improvement and Delay Reduction, Report of the Working Group on Aircraft Noise/Airport Capacity (1987).

One transportation policy commission reviewed dozens of transportation studies and reports, and found that nearly all shared the following weaknesses:

- Proposals focused more on commercial carrier trends and problems, and little on users, consumers, and tax payers.
- Political realities and externalities were generally ignored.
- Specific trade-offs between competing interests were seldom addressed.
- Prioritization of needs was typically absent.
- Planning was seldom comprehensive or long range.
POLICY PRINCIPLE ONE: SINCE AIRPORT PROBLEMS CANNOT BE SOLVED BY A SINGLE INSTITUTION OR GOVERNMENT AUTHORITY, ALL AFFECTED GROUPS MUST ACTIVELY COOPERATE IN FORMULATING AND SUPPORTING ACTIONS TO INCREASE FAIRNESS, EFFICIENCY, AND ACCOUNTABILITY

It has been said that the problems associated with airports in the United States are largely institutional rather than technical or economic. Even though aviation activity produces benefits for everyone, our federalism system has failed to promote clear accountability for the problems of fairness and efficiency associated with such benefits.


A good example of the type of policy principles development attempted here, is CONGRESSIONAL BUDGET OFFICE, FEDERAL POLICIES FOR INFRASTRUCTURE MANAGEMENT (1986).

273. Much of the solution to the problem of aircraft/airport noise is institutional rather than technological. A substantial portion of the problem can be solved if the parties involved—aircraft manufacturers, air carriers, pilots, airports, local communities and various agencies of the federal government—would work cooperatively. EPA, TOWARD A NATIONAL STRATEGY FOR NOISE CONTROL 45 (1977).

274. We live in a nation with a system of federalism based on a sharing of power and responsibility, with the various governments working toward shared goals. One author has characterized our system as "row boat federalism," which describes the federal system in terms of people in a boat. T. SANFORD, STORM OVER THE STATES 97 (1967). The governments are all in the same boat, tossed by the same waves, and dependent on each other's paddles. When anyone fails to row, they all move more slowly, and the waves become more dangerous for all. In row boat federalism, the participants might agree on some things, notably the desire to remain afloat (that is, to survive), they may or may not agree on their destination, who should sit where, or how the burdens should be divided. Cooperation is possible, but so is conflict.

One problem in "row boat federalism" is that of government accountability. If all levels of government participate in a program that fails, how do we know who deserves the blame? Who should receive credit for a success? Sharing of responsibilities creates enormous opportunities for scapegoating.

On the positive side, shared responsibility can lead to cooperative action. This is especially true if officials at each level actually share responsibility (are liable) which gives them an incentive to keep an eye on officials at other levels to avoid being blamed for failure.

From the citizen's perspective, most people have little interest in abstract debates over which level of government should be responsible for a given task. What most people care about is getting the policies they want. Of course, those seeking a particular result may argue for a certain level of government's control of an issue which most benefits their interest. But, they enter the picture not as political philosophers or students of federalism theory, but as practical oriented folks.


275. Technology cannot resolve conflicts over values. Airports are a policy problem because
What is needed is a new process which limits such incoherence and enhances participation and accountability among all. As a minimum that approach should incorporate planning procedures which include the following:

- There must be an evaluation whether any private or public interests are regularly absent from local, regional, state, or national airport planning, a determination of the cause of such absence, and the creation of incentives for their participation.
- There should be an effort, open to public scrutiny, to define the costs and benefits of various airport noise and airport capacity actions.

The consensus favoring airport development has been shattered. Technology may alleviate some pressures even with a resumption of growth, but those who want to anticipate demand must, now, either rebuild consensus by addressing problems associated with institutional structure, participation, and equity, or persist in continuous conflict. There are many options to explore, but they all evoke complex philosophical problems which, in the absence of consensus, cannot be avoided. Feldman, *Air Transportation Infrastructure as a Problem of Public Policy*, in *Current Issues in Transportation Policy* 17 (A. Altshuler ed. 1979).

276. Local government sponsorship of airports can cause certain inefficiencies in aviation. Such inefficiencies are more likely to occur because: the jurisdiction of the local government is not large enough to enable the benefits of the airport to be consumed primarily within the jurisdiction; the local government is not large enough to permit the realization of economies of scale; the unit of government should be responsible for a sufficient number of functions so that it provides a forum for resolution of conflicting interests, with significant opportunities to balance needs and resources. Zimmerman, *Solving Local Government Problems by Pragmatic Action*, 12 *Current Mun. Probs.* 39 (1985).

277. Many still remain optimistic that such cross-government cooperation is achievable in the United States, which has a history of citizens working together to solve difficult economic and social challenges. W. Zelinsky, *Nation into State* (1988). In such an effort, the FAA would be more of a gardener, understanding and rechanneling natural forces for a more productive effort, than an engineer. The challenge is to get those with distinct interests to accept the call for consensus as an opportunity, rather than a threat. See Flynn, *The Effects of Environmental Characteristics on the Institutionalization of Public Transportation*, TRANSP. J., Spring, 1987, at 30; Jackson & Dutton, *Discerning Threats and Opportunities*, 33 *Admin. Sci. Q.* 370 (1988); Newland, *Shared Responsibility*, THE BUREAUCRAT, Spring 1989, at 37.

• Consideration should be given to initiatives which increase public education and dispute resolution.
• There must be a change in our system so the federal government, local governments with land use control responsibilities, and the aircraft operators are mutually accountable with airport proprietors for the planning and implementation of airport decisions.

**POLICY PRINCIPLE TWO:** SINCE AIRPORTS IN THE UNITED STATES OPERATE UNDER A CITIZEN FRANCHISE REQUIRING PUBLIC CONFIDENCE, ALL AIRPORT DECISION MAKERS MUST ACCOUNT FOR PUBLIC CONCERNS IN PLANNING AND IMPLEMENTATION

Airports have no vested rights. A successful airport development project must not only be analytically sound, but must earn public support. Consequently, airport and airspace decision makers have a responsibility to communicate with elected officials and to foster public dialogue and support. Potential public acceptance is dependent upon whether the affected community understands and accepts the need for the development or change; receives complete, truthful, and unbiased information about the impacts; and recognizes that public concerns have been considered adequately and fairly. The only way to ensure these conditions is by designing a program to achieve them.280 Included

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279. G. DOWNS & P. LARKEY, THE SEARCH FOR GOVERNMENT EFFICIENCY 135-36 (1986) (advocating significant government resources to deal with the "chaotic, often frenzied" world of public interest and political support).

Public participation in important government decisions is consistent with the constitutional values of the Nation, and is in close alliance with civil and national pride. Lane, Individualism, Civic Virtue, and Public Administration, 20 ADMIN. & SOC'Y 30 (1988); Long, The Citizenships: Local, State, and National, 23 URB. AFF. Q. 4 (1987); Nigro & Richardson, Self-Interest Properly Understood: The American Character and Public Administration, 19 ADMIN. & SOC'Y 157 (1987). When government is unresponsive to the right of citizen participation, communities may react by expanding the focus of the debate beyond the specific issue. J. LOGAN & H. MOLOTCH, URBAN FORTUNES: THE POLITICAL ECONOMY OF PLACE 134 (1987).

among the hallmarks of a quality public acceptance program are:

- purposeful\(^{281}\) efforts to educate the public and elected officials in the need for and the benefits of the project;
- willingness to define and discuss the aviation activity associated with the proposal and its possible impacts on various interests in the community;
- significant time and resources devoted to learning about the community values and objectives\(^{282}\) impacted by the project; and
- a demonstrated commitment to the development of mitigation measures appropriate to the situation.\(^{283}\)

**Policy Principle Three: Aviation Industry Groups and Various Levels of Government Are Responsible for Resolving Disputes Over Airport Noise, Including Providing "Just Compensation" to Property Owners and Balancing the Many General Welfare Needs**

Near airports, quiet is a scarce resource which causes fierce competition. By-and-large the aircraft operators, the federal government, airports, and their neighbors approach this problem with a narrow perspective, rather than accepting a balanced solution.\(^{284}\) Frequent reactions from these diverse parties include:

- the spending of considerable time and effort articulating one side’s needs and interests;
- the reluctance to learn about the plight of the other side, and their concerns;
- the rationalizing away of any injustice; and
- the strict adherence to procedural requirements.

Depending on a variety of factors, this system of narrow concern often produces lopsided results: where either many airport neighbors go

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\(^{281}\) A key to any significant change in policy is the creation of political discourse on the issue of concern. While such discourse may occur as a result of a crisis, such as a major aircraft accident, government agencies can purposefully interject issues into the political arena and encourage public attention to the problem. Forster, *Questioning and Organizing Attention: Toward a Critical Theory of Planning and Administrative Practice*, 13 ADMIN. & SOC’Y 161 (1981).

\(^{282}\) A commonly cited weakness of national public works planning is the absence of appreciation for local “symbols of politics.” Successful planning which impacts community land must dedicate adequate resources in recognizing and accommodating local values, objectives, and traditions. Trilling, *Land Use Policy and the Symbolic Politics of Environmental Conflict*, in *THE LAND USE POLICY DEBATE IN THE UNITED STATES* 91 (J. de Neufville ed. 1981).

\(^{283}\) Of course, public officials have an obligation to clarify government decisions so that formation of false private land use expectations is minimized. Beatley, *The Role of Expectations and Promises in Land Use Decisionmaking*, 22 POL’Y SCI. 27 (1989).

uncompensated for, or must live with, high levels of aircraft noise; or the
airport and the national air transport system must accept severe restric­
tions on operations in the face of growing community, regional, and na­
tional need for aviation services. Important to reducing such imbalance
are at least two principles of good government in the United States.

First of these principles is the responsibility of government and the
private sector to promote the general welfare of its citizens. At the com­
munity level this general welfare is commonly known as quality of life.285
Such quality of life includes access to transportation, opportunities for ed­
ucation, control of crime, opportunities for employment, availability of rec­
reational facilities, clean air and water, quiet, and so forth. But, the
achievement of community quality of life is often pitted against the impact
of community choices on the general welfare of other communities, the
region, state, and Nation. In order to allocate limited resources to achieve
the optimum general welfare under specific circumstances, public and
private interests at all levels of government must participate in coopera­
tive planning and should accept less than a full satisfaction of self-interest.

The second principle is reflected in the Just Compensation Clause286
of the United States Constitution. The spirit of that principle is that dispro­
portionately placed burdens on private property will be avoided.287 While
the exact formula for such compensation continues to be debated, public
and private sector interests should strive to compensate noise impacted
property owners when fairness dictates.288 Indirectly such compensation
may also reduce the level of political controversy associated with airport
development projects and airport operations,289 and may cause more ef­

285. Myers, Building Knowledge About Quality of Life for Urban Planning, 54 J. AM. PLAN.
286. U.S. CONST. amend V.
287. See Kmiec, The Original Understanding of the Taking Clause is Neither Weak or Obtuse,
88 COLUM. L. REV. 1630 (1988); Peterson, The Takings Clause: In Search of Underlying Princi­
288. Within the last two decades is has become more common to compensate for environ­
mental pollution injuries. Muskie, Reflections on a Quarter Century of Environmental Activism, 18
289. Bacow & Milkey, Overcoming Local Opposition to Hazardous Waste Facilities: The
Massachusetts Approach, 6 HARV. ENVT. L. REV. 265 (1982); O'Hare, Not on My Block, You
Notwithstanding the advantage of negotiated compensation, public works project proponents
seldom use this tactic. Reasons for such reluctance include:
• project proponents usually underestimate the power and determination of the
  opposition;
• proponents are inexperienced in packaging alternatives in ways that invite compromise;
• proponents may have a difficult time determining with whom they should negotiate;
and
• the act of offering to compensate is perceived as inviting a flood of interests which
  will seek compensation and which will render the project too costly.
efficient decision making about airports and airways.\footnote{290}

In order to further these two principles it may be necessary to adopt a new statutory or regulatory approach. The preparation of that new approach, should begin with a consideration of these guides:\footnote{291}

- Self-interest should be discouraged and parties should be persuaded to negotiate, which includes feedback and interaction.\footnote{292}
- The allocation method should consider any reasonable alternative to eliminate or reduce the noise impacts without eliminating the proposed project or operation.
- Benefits transferred to private interests or neighborhoods because of disproportionate burdens may appropriately include alternatives to money compensation.
- Compensating private interests which are precluded from recovering by statutes of limitations may, nevertheless, be required as a matter of fairness.\footnote{293}
- Quality of life in the impacted community should always be considered.\footnote{294}
- Adequate resources should be provided to determine the nature and extent of the noise impacts on airport neighbors.
- The amount of the existing capital investment in airport and related facilities, along with the length of operation of the airport, should be considered.
- The importance of the proposed project or operation to the community, state, and Nation should be clearly defined.
- Private interests within the areas of highest noise levels, and with exposure to more frequent aircraft activity, may have a greater justification to partici-

\footnote{M. O’HARE, L. BACOW & D. SANDERSON, FACILITY SITING AND PUBLIC OPPOSITION 91-93 (1983).
290. This “better calculations” theory of public finance suggests that compensation for social impacts encourages government agencies to balance more carefully the costs of their actions against the benefits. Tullock, Achieving Regulation: The Public Noise Perspective, REGULATION, Nov./Dec. 1978, at 50.
participate in negotiations, and obtain relief.\textsuperscript{295}

- The extent to which any interest has materially relied on any existing institutional arrangements should be considered.
- Any advantage which an interest obtains because of its proximity to the airport should be considered in determining net compensation.
- Recovery may be barred if the alleged injury was the loss of value from speculative future land development.
- If uncertainties make it difficult for a landowner to calculate the value of any injury, those responsible for the aviation activity must bear some, if not all, of the burden of the uncertainty.\textsuperscript{296}

**Policy Principle Four:** *There are Certain Airport-Related Issues of National Concern Which Must Be Clearly Defined and Accepted*

The United States has evolved into what some believe is a true nation-state,\textsuperscript{297} with potential to solve complex economic, social, and physical environment problems. Such potential is more readily achieved, however, when public and private sector interests act "responsibly,"\textsuperscript{298} meaning purposefully to achieve objectives in the public interest.

Unfortunately, in the area of airport noise and airport capacity such public interests have either not been well defined or been too vague to promote accountability. Some of the public debate concerning airports and airways ought to focus on the root national general welfare issues, with a view toward better definition or clarity. Among the more important questions of national public concern associated with airports are these:

- Assuming that both safety and noise are serious externalities of aviation activity, why does safety attract greater federal interest and resources than

\textsuperscript{295} Also, the ability of the private interest to reasonably avoid the impacts may be considered. Blume & Rubenfeld, *Compensation for Takings: An Economic Analysis*, 10 Res. L. & Econ. 53 (1987).


\textsuperscript{298} Factors in defining "responsibility" in achieving public interests include:

- individuals who make important decisions affecting the public are accountable to somebody who has the power to veto decisions or remove the decisionmakers from authority;
- decisionmakers operate under special constitutional, statutory, or regulatory charters which contain specific objective criteria useful in evaluating actions and performance;
- individuals or institutions with special knowledge useful in furthering a public interest are charged with sharing such knowledge with others; and
- public and private sector actions are explicable, meaning susceptible to rational explanation, conditioned upon attempts to obtain the relevant facts, and upon consideration of the consequences.

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does noise?\textsuperscript{299} Is it in the Nation’s best interest for the federal government to shoulder more of the responsibility in solving the airport noise problem?

- Should scarce federal resources be spent on airport infrastructure without a clear demonstration of how that expenditure will increase system capacity?
- If there are competing national interests which may override the requirement for system capacity, what are they and are they clearly defined?\textsuperscript{300}
- Are the long term interests of aviation better served by the present improvisation in airport development, or is a more systematic and analytical method needed? Why?\textsuperscript{301}
- When does the federal interest under the Commerce Clause of the United States lead to the preemption of airport use restrictions?\textsuperscript{302}

\textsuperscript{299} Control of externalities is considered a legitimate role of government, but one that is not always successful. See Shepsle & Weingast, \textit{Political Solutions to Market Problems}, 78 AM. POL. SCI. REV. 417 (1984). When the externalities cross state boundaries, such as exporting noise and safety problems outside a state, a stronger federal role may be required. See Brilmaker, \textit{Shaping and Sharing in Democratic Theory: Towards a Political Philosophy of Interstate Equality}, 15 FLA. ST. U.L. REV. 389 (1987); Ruhl, \textit{Interstate Pollution Control and Resource Development Planning: Outmoded Approaches or Outmoded Politics?}, 28 NAT. RESOURCES J. 293 (1988).

\textsuperscript{300} Of course, system capacity increases may not be the only legitimate cause for federal expenditures at airports. But, the purposes ought to be more clearly defined and prioritized. See Bodde, \textit{The Federal Financing of Large-Scale Engineering Projects}, 10 TECH. SOC’Y 5 (1988).

Principles justifying a federal role in regulating airports and the aviation industry include:

- the exercise of enumerated constitutional powers such as the Commerce Clause or Just Compensation Clause;
- the need for federal involvement because of the magnitude of the fiscal problem;
- the need to address the multistate dimensions of the aviation activity; or
- the need for national uniformity in the face of discriminatory, unfair, or inefficient local rules.


\textsuperscript{302} The constitutional restraint upon state control of commerce found in the Commerce Clause was a reasoned and reasonable reaction to the Nation’s near disastrous experience under the Articles of Confederation, when commercial anarchy reigned. Since its adoption, however, the definition of what is commerce, and how to regulate it have been disputed. The powers of the Commerce Clause were first extensively used during Theodore Roosevelt’s era of “New Nationalism.” During those years, the federal Commerce Power was used like a federal police power, to attack health and social problems considered harmful to the public. This interpretation of the Commerce Clause was further expanded and institutionalized between 1937 and 1942.
• What should be the role of airport activity forecasting? How much resource should be dedicated to this effort?

**POLICY PRINCIPLE FIVE:** **ASSUMING THAT THE FAILURE TO CONTROL INCOMPATIBLE LAND USES ON AND IN THE VICINITY OF AIRPORTS HARMs BOTH PUBLIC AND PRIVATE INTERESTS, SUBSTANTIVE AND PROCEDURAL STANDARDS FOR AIRPORT AREA LAND USE PLANNING CAN REDUCE INCONSISTENCY, INEQUITY, AND INEFFICIENCY**

A pervasive, complex, and costly problem associated with airport development and operations is the incompatible use of land on and in the vicinity of airports. These highly desirable properties are the focus of many local, regional, state, and national initiatives, both public and private. In many cases the diverse interests in airport area real property go uncoordinated leading to inconsistent, irrational, inequitable, and ineffi-

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when the United States Supreme Court decided a series of cases sanctioning almost limitless congressional power.

But, during the last decade of national politics calling for reduced federal government the exercise of authority under the Commerce Clause has waned. See ACADEMY FOR STATE AND LOCAL GOVERNMENT, PREEMPTION: DRAWING THE LINE 40-43, 61-63 (1986) (discussing Reagan Administration decisions concerning the federal role in dealing with problems of non-uniform local/state regulations affecting weight and length of trucks on interstate highways, and regulating the transportation of hazardous materials).

303. See W. ASCHER & W. OVERHOLT, STRATEGIC PLANNING AND FORECASTING (1983). A recent book discusses the “lessons learned” by those who have sought to forecast future events and understand social trends:

• There is an extraordinary capacity of the human mind and spirit to master complex problems, which we are a long way from having exhausted.
• From time to time a leader steps forward and has a significant impact on society.
• Predicting the future requires a careful interpretation of the present.
• People’s perceptions of reality are important and should not be ignored.
• The use of words provides many traps since meanings evolve continually.
• Interdisciplinary teamwork involving mutual respect and trust is necessary to solve complex problems and to achieve synergistic results.
• There is a public-private nexus whenever major, successful social problems are achieved.
• Doomsday scenarios, erroneous forecasts, and outrageous statements attract the media and conference-goers.
• It takes extra effort to avoid accepting, using, and promoting irrelevant information.

**WHAT I HAVE LEARNED: THINKING ABOUT THE FUTURE THEN AND NOW** (M. Marien & L. Jennings eds. 1987).

In 1988 one writer suggested that future economic growth in the United States would depend on the nation’s ability to deal with the following issues: termination of the cold war; defining policies for information technology and its impacts; the continuation of inequality among citizens; lawyerization of society; problems of the aging society and the medical-industrial complex; drug abuse; new waves of immigrants; deteriorating infrastructure; fragmentation of vested interests; global environmental degradation; AIDS and other diseases; absence of long-rang planning. Linstone, Issues for America: An Agenda of Problems and Opportunities, 34 TECH. FORECASTING & SOCIAL CHANGE 203 (1988). See also Golden, Cheer Up, Things Could Be Worse: Problems and Opportunities for the Decades Ahead, 11 TECH. SOC’Y 297 (1989) (adding to the list of issues: literacy, changing roles of women, single-parent households, energy-shortages).
Such decision making affects not only the community and its airport, but has long range, far reaching impacts on the region, state, and the Nation.

Fortunately, similar problems have been identified and are being addressed by the federal government, states, and local governments in other contexts: floodplains, coastal zones, land surrounding nuclear plants, and so forth. Such recent experience, along with the lessons learned under the FAA FAR Part 150 Program, could form the basis for a national debate concerning airport vicinity land use planning and control. That debate should consider several important issues...
about private and public land ownership, and land policy.

- How can public confidence in airport vicinity land use planning and control be achieved?\(^{311}\)
- What information is needed to effectively plan and control uses on and near airports, and how would such information be collected and managed?\(^{312}\)
- To what extent should bargaining between competing interests be promoted?\(^{313}\)
- Is there a legitimate role for government in purchasing and redeveloping property near airports?\(^{314}\)
- Who should provide the resources necessary for successful airport vicinity land use planning and control?

POLICY PRINCIPLE SIX: PUBLIC ACQUISITION AND EFFECTIVE MANAGEMENT OF AIRPORT REAL PROPERTY INTERESTS ARE ESSENTIAL FOR THE LONG RANGE NEEDS OF AVIATION IN THE UNITED STATES

The public ownership and management of real estate\(^{315}\) have a profound effect on the institutional and policy choices available to solve
airport problems. Appropriate exercise of the eminent domain power for future project development, more productive utilization of available public land resources, and acquisition of restrictive easements in land near airports can increase the likelihood of satisfying the long term air transportation requirements.

Unfortunately, too little attention is given to these important matters by any level of government. Taking the lead from some private corporations, government should evaluate the need for and benefits of better real property acquisition and management programs.

**POLICY PRINCIPLE SEVEN:** If liability for injury caused by aircraft noise was shared by those private and public interests involved in aviation activity and airport vicinity land use control, some of the barriers to cooperative airport decision making could be removed.

Under the current rule of law only airport proprietors, not the FAA, nor the air carriers, nor local land use planning agencies, nor any other, are liable for losses suffered by airport neighbors from aviation noise. Interestingly, this sole liability principle has had a profound impact on government and private sector policies toward airports. Airport proprietors point to the hardship of their liability as justification for retaining exclusive control over airport use restrictions. The FAA has carefully avoided using federal authority to resolve disputes arising from aircraft noise, fear-
ing the loss of immunity\textsuperscript{319} from liability. At least two other non-liable interests, the air carriers and local governments responsible for land use planning and control, have given only peripheral attention to the issue of aircraft noise impacts on citizens.

For two good policy reasons a broader-based liability for aircraft noise pollution injury ought to be considered:

\begin{itemize}
  \item Airport proprietors whose liability is reduced would be more supportive of national airport system plans.
  \item There would be greater cooperation among those liable for noise-related injuries in providing the needed resources, information, and attention to resolve conflicts.
\end{itemize}

Of course, legislation to spread liability should include provisions for just compensation to impacted property owners consistent with Policy Principle Three.

\textbf{POLICY PRINCIPLE EIGHT: IMPORTANT ACHIEVEMENTS IN AIRPORT DECISION MAKING WILL NOT OCCUR WITHOUT TALENTED AND COMMITTED LEADERS FROM THE PUBLIC AND PRIVATE SECTOR}

Fortunately there are many capable managers in the public and private sector who understand airport policy in the United States and who work very well at solving problems within their organizations. But the cross-institution issues discussed here may never be resolved unless leaders\textsuperscript{320} emerge who capture the attention of the diverse groups impacted by airport decision making, and inspire them to accept greater responsibility.\textsuperscript{321}

\begin{itemize}
  \item The FAA, not the airports, designate flight tracks which determine the areas where real estate interests should be acquired.
  \item The acquisition of land for long range development plans is costly and does not have the support of the FAA under the Airport Improvement Program.
  \item The increase in aviation activity following deregulation outstripped the proprietor’s reasonable resources to acquire real estate interests.
  \item Often the needed real estate interests are within the jurisdiction of other local governments which oppose acquisition.
\end{itemize}


While we are unaccustomed to thinking about leadership as a team effort, it is likely that real progress on these issues will require the banding together of various leaders from government and the private sector. The following are among the most important leadership talents needed for effective change in this area.

a) Airport policy leadership must be skilled in learning and communicating, rather than maneuvering. These leaders should accept a period of "logical incrementalism" when the various interests interact and come to know one another's differences. The better leadership approach involves cross-education and recognition of emerging consistencies. Thereafter, these leaders must be capable of communicating such consistencies with others.

b) This leadership corps must surely be individuals with technical and professional competence in the issues relating to airport problem solving. They should also possess the intuitive, social know-how and analytical skills to cull out the irrelevant or least important from the mass of information and issues associated with airport activity.

c) With their competence, and after a period of learning and communication, the leaders must be willing to make decisions or promote decisive action. Decisions need to be made in this area.

V. CONCLUSIONS AND RECOMMENDATIONS

Among the Nation's transportation policy issues, the conflicts associated with airports and airport activities have been among the more difficult to resolve. This paper suggests that changes in airport policy should focus on: enhancing private and public sector accountability for airport-related decisions; and promoting cooperative, long range planning.

It is assumed that the creation of a truly national air transportation system will require strong leadership to unify the diverse interests. Such leadership by a former Secretary of Transportation see Devine & Burnley, So You Want to Run an Agency, POL'Y REV., Winter 1989, at 8.

322. See Quirk, The Cooperative Resolution of Policy Conflict, 83 AM. POL. SCI. REV. 905 (1989). Normally, this education process takes time. Unfortunately, the turnover of key players in both government and the private sector makes it difficult to finish this important phase. Solutions to this problem are suggested in Young & Norris, Leadership Change and Action Planning, 48 PUB. ADMIN. REV. 564 (1988).


But, some argue that even with know-how and strategic planning the Nation cannot be lead through the economic and social problems until the citizens' confidence is restored in government. Farazmand, Crisis in the U.S. Administrative State, 21 ADMIN. & SOC'y 173 (1989).

leadership should include Congress, perhaps the House Committee on Public Works and Transportation, and the Executive Branch, likely the Secretary of Transportation.

The more conflict-laden issues, primarily those dealing with accountability, will require considerable public debate and eventually federal legislation. These issues ought to be addressed by Congress, which may use a combination of research, hearings, and national leadership councils.

Other airport problems, many related with planning, are within the existing legislative jurisdiction of the Secretary of Transportation. Naturally, most of these issues face competing transportation priorities. But here, the Secretary will have to demonstrate leadership: by testing his ability to unify diverse interests; and by choosing long term benefits over expediency.

CONGRESS RECOMMENDATIONS

CONGRESS RECOMMENDATION ONE: AMEND FEDERAL AVIATION LAW TO MORE CLEARLY DEFINE AIRPORT "PROPRIETARY POWERS AND RIGHTS" TO PREVENT THE FEDERAL AVIATION ADMINISTRATION FROM GIVING UNDUE DEFERENCE TO AIRPORT PROPRIETORS WHEN INTERSTATE AIR COMMERCE MATTERS ARE AT STAKE.

CONGRESS RECOMMENDATION TWO: TAKE ACTION TO SPREAD THE LEGAL LIABILITY FOR AIRCRAFT NOISE INJURIES AMONG BOTH PUBLIC AND PRIVATE SECTOR INTERESTS WHICH ARE RESPONSIBLE FOR THE CONTROL OF AIRCRAFT NOISE OR OF THE PHYSICAL ENVIRONMENT THROUGH WHICH THE NOISE EMANATES.

CONGRESS RECOMMENDATION THREE: ACT TO INCREASE THE PARTICIPATION AND ACCOUNTABILITY OF AIRCRAFT OPERATORS, AND LOCAL GOVERNMENTS HAVING JURISDICTION OVER AIRPORT VICINITY LAND USE CONTROL, IN NOISE COMPATIBILITY AND NATIONAL AIR TRANSPORTATION SYSTEM PLANNING.

DEPARTMENT OF TRANSPORTATION RECOMMENDATIONS

DOT RECOMMENDATION ONE: IN CLOSE CONSULTATION WITH THE DIVERSE AIRPORT INTEREST GROUPS, DEVELOP PROCEDURES AND THE FORMAT FOR A NATIONAL AIRPORT SYSTEM PLAN WHICH WILL SERVE AS THE PRIMARY AIRPORT POLICY AND LONG RANGE PLANNING DOCUMENT FOR THE NATION.

DOT RECOMMENDATION TWO: ESTABLISH A NATIONAL AIRPORT REAL PROPERTY ACQUISITION PROGRAM WITH SPECIFIC GOALS INCLUDING: THE IDENTIFICATION AND PRIORITIZATION OF LONG RANGE NATIONAL AIRPORT SYSTEM REAL PROPERTY REQUIREMENTS; THE TRAINING OF
AIRPORT PROPRIETORS IN THE PLANNING AND ACQUISITION OF REAL PROPERTY INTERESTS FOR AIRCRAFT NOISE ABATEMENT AND FUTURE AERONAUTICAL PURPOSES; AND THE INCREASED USE OF AVAILABLE FEDERAL PROPERTY FOR NATIONAL AIR TRANSPORTATION SYSTEM PURPOSES.

DOT RECOMMENDATION THREE: AFTER STUDYING FEDERAL AND STATE LAND USE CONTROL INITIATIVES (SUCH AS FLOODPLAINS, COASTAL ZONES, AND SO FORTH), ADOPT APPROPRIATE FEDERAL PROCEDURES, STANDARDS, AND INCENTIVES TO REDUCE INCOMPATIBLE DEVELOPMENT IN THE VICINITY OF NATIONAL-SYSTEM AIRPORTS.

DOT RECOMMENDATION FOUR: ENSURE THAT THE FAA AIRPORT SERVICES MANPOWER IS ADEQUATE TO REGULARLY PARTICIPATE WITH AIRPORT PROPRIETORS IN NEGOTIATING INDIVIDUAL NOISE COMPATIBILITY AND CAPACITY ENHANCEMENT AGREEMENTS.

DOT RECOMMENDATION FIVE: EVALUATE THE NEED FOR MORE COMMUNITY RELATIONS, REAL ESTATE, AND URBAN PLANNING PROFESSIONALS WITHIN THE NATIONAL AIR TRANSPORTATION SYSTEM; AND ADOPT APPROPRIATE BUDGET INITIATIVES TO INTEGRATE SUCH SKILLS INTO FAA AND AIRPORT PROPRIETOR EDUCATION, PLANNING, AND DECISIONMAKING.
To establish a program for airport system planning in the United States.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Airport System Planning Act of 1990."

SEC. 2. AMENDMENTS TO AIRPORT AND AIRWAY IMPROVEMENT ACT OF 1982.

(a) NATIONAL AIRPORT SYSTEM PLAN.—Section 504 of the Airport and Airway Improvement Act of 1982 (49 U.S.C. App. 2202) is amended—

(1) by striking subsections (a) and (c); and

(2) by redesignating subsections (b) and (d) as subsections (a) and (b), respectively.

(b) PROJECT GRANT APPLICATIONS.—

(1) PROPOSED PROJECTS.—Section 509(a)(1) of such Act (49 U.S.C. App. 2202(a)(1)) is amended by striking the second sentence and inserting the following: "No project grant application shall propose airport development or airport planning except in connection with public-use airports included in an Airport Capital Improvement Plan prepared pursuant to section 5 of the Airport System Planning Act of 1990."

(2) APPROVAL.—Section 509(b)(1) of such Act (49 U.S.C. App. 2202(b)(1)) is amended—

(A) by striking "and" at the end of subparagraph (D);

(B) by striking the period at the end of subparagraph (E) and inserting "; and "; and

(C) by adding at the end the following new subparagraph:

"(F) the project is reasonably consistent with airport and aviation system plans (existing at the time of approval of the project) of the State and the regional transportation planning authorities of the area in which the airport is located.""

SEC. 3. PERFORMANCE MEASURES FOR AIRPORTS.

(a) ESTABLISHMENT.—The Secretary shall establish performance measures to assist in airport planning. Such measures shall be developed to provide guidance in the following areas:

(1) Evaluating the extent and effects of air transportation delay and congestion at an airport.

(2) Evaluating the degree to which certain capital improve-
ments, pricing, and other actions may reduce air transportation delay and congestion at an airport.

(3) Evaluating the effect on other airports and the national air transportation system of use restrictions adopted by 1 or more airports.

(4) Planning roadways and surface transportation facilities to ensure the least constrained access to airports.

(5) Considering and managing the environmental consequences of airport activity in a manner which will reduce interference between airport activities and other activities.

(6) Judicious acquisition and effective control of airport real property interests to satisfy long-range needs for aeronautical land and measures of incompatibility in land uses in the vicinity of airports.

(7) Such other areas as the Secretary considers appropriate.

(b) PARTICIPATION.—The Secretary shall provide each State and each sponsor, owner, and operator of a public-use airport an opportunity to participate in the establishment of performance measures under this section.

(c) USE.—The Secretary shall use performance measures established under this section for evaluating individual airport improvement projects and for evaluating the needs of the Nation's system of airports in conducting planning activities under this Act.

(d) REPORT.—Not later than 180 days after the date of the enactment of this Act, the Secretary shall publish procedures for the establishment of performance measures under this section.

SEC. 4. STRATEGIC PLAN FOR AIRPORTS.

(a) STRATEGIC PLANNING FORUM.—

(1) IN GENERAL.—Not later than 1 year after the date of the enactment of this Act, and every 4 years thereafter, the Secretary shall conduct a national forum of Federal, State, and local government officials and appropriate private sector representatives to identify and evaluate long-range problems associated with public-use airports and objectives in solving such problems.

(2) NOTICE.—The Secretary shall publish notice of each forum to be conducted under this subsection not later than 180 days before the date of the first day of the forum. In providing such notice, the Secretary shall request that officials participating in the forum transmit to the Secretary, not later than 60 days before such date, a report which identifies and evaluates problems and objectives referred to in paragraph (1).

(3) PUBLICATION OF REPORT SUMMARIES.—Not later than 10 days before the date of the first day of the forum, the Secretary shall
publish in the Federal Register a summary of reports submitted to the Secretary pursuant to paragraph (2).

(b) STRATEGIC PLAN.—Not later than 1 year after the date of the last day of each forum to be conducted under this section, the Secretary shall transmit to Congress and the President a strategic plan for airports. Each plan shall include the following:

(1) Five, 10, and 20-year forecasts of aviation activity and the likelihood of serious congestion and delay problems at each public-use airport.

(2) Identification and discussion of the assumptions and methodology supporting such forecasts.

(3) A discussion of performance measures established by the Secretary under section 3.

(4) A summary of State planning activities conducted under section 6.

(5) A summary of planning by the Department of Transportation and the Department of Defense to make domestic military airports and airport facilities available for civil aviation uses.

(6) A description of State efforts to improve airport vicinity land use planning, including efforts to enact and implement the model State statute developed pursuant to section 8.

(7) A description in order of priority of 10 long-range national problems facing public-use airports, as determined by the Secretary, and possible solutions to remedy each such problem.

SEC. 5. AIRPORT CAPITAL IMPROVEMENT PLANNING.

(a) AIRPORT CAPITAL IMPROVEMENT PLAN.—Not later than January 15th of each year beginning after the date of the enactment of this Act, the Secretary shall transmit to Congress and the President an Airport Capital Improvement Plan. Each plan shall include—

(1) a list of airport improvement projects which may receive Federal funding in the next 5 fiscal years;

(2) a prioritization of such projects by program year;

(3) an evaluation of constraints on the development of such projects, including financial, environmental, technical, operational, and governmental constraints; and

(4) specific actions which may be taken to eliminate or reduce such constraints.

(b) CONSISTENCY WITH OTHER PLANNING.—The Secretary shall, to the maximum extent possible, ensure that each plan prepared pursuant to subsection (a) is consistent with the Federal airway capital investment plan, State aviation and airport system plans, public-use airport plans, and aviation plans adopted by other public agencies. Upon request of a
State, the sponsor, owner, or operator of a public-use airport, or the head of a public agency, the Secretary shall provide a written explanation of inconsistencies between a plan prepared pursuant to subsection (a) and any other aviation plan.

(c) PLANNING PROCESS.—The Secretary shall establish an airport capital improvement planning process under which items to be included in an Airport Capital Improvement Plan are updated and evaluated on an on-going basis.

SEC. 6. STATE AIRPORT SYSTEM PLANNING.

(a) FEDERAL COOPERATION IN STATE AIRPORT SYSTEM PLANNING.—

(1) IN GENERAL.—Upon request of the Governor of a State, the Secretary shall cooperate in the airport system planning of such State.

(2) SCOPE OF FEDERAL PARTICIPATION.—Subject to the Secretary's approval, the Governor of a State shall establish the scope of activities to be undertaken by the Secretary under this section. Such activities may include on-going Federal and State planning efforts, as well as the establishment of an annual joint planning meeting to exchange information, discuss problems, objectives, and alternative solutions, and develop joint policies.

(3) PUBLIC INFORMATION.—The Secretary and the Governor of a State shall make information available to the public concerning planning activities undertaken pursuant to this section.

(b) MINIMUM FEDERAL PARTICIPATION.—At a minimum, the Secretary shall participate in the airport system planning of a State—

(1) by providing the State necessary Federal coordination and information in the development of a State airport capital improvement plan;

(2) by assisting the State in the development of forecast assumptions and methodologies in support of a State airport system plan and individual airport planning;

(3) by providing the State, in a timely manner, information concerning advances in transportation technology and likely effects of such technology on State airport system planning;

(4) by providing the State with a Federal assessment of the need for civil use of Federal military airfields in such State; and

(5) by cooperating with the State in the planning of airport ground access alternatives in the State.

(c) AIRSPACE APPLICABILITY.—The Secretary shall consider the results of any State airport system planning in actions affecting the airspace system in the State.

(d) INTERMODAL AND MULTIMODAL PLANNING.—The Secretary shall
ensure active Federal participation in State intermodal and multimodal transportation system planning.

SEC. 7. AIRPORT FORECAST MODEL.

The Secretary shall, in consultation with the States and the sponsors, owners, and operators of public-use airports, establish guidelines for forecasting aviation activity at public-use airports and within each State. Such guidelines shall include recommendations for—

1. standardization of data to be collected in support of airport activity forecasts;
2. uniform units of measurement and uniform data collection periods; and
3. a methodology for developing credible forecast assumptions and analysis.

SEC. 8. AIRPORT VICINITY LAND USE PLANNING.

(a) MODEL STATE STATUTE.—The Secretary, in consultation with the States, shall develop a model State statute for airport vicinity land use planning. Such statute shall establish a planning process which addresses the following:

1. Orderly exchanges of information about land use, airport operations, and other public and private activities conducted in the vicinity of public-use airports.
2. Designation of an appropriate public agency to consider and resolve conflicting interests in the vicinity of public-use airports.
3. Means of improving compatibility of surrounding land uses with respect to airport noise exposure, risk of aircraft crash hazards, and building and structure height restrictions to protect the airspace used by aircraft.
4. Coordination of planning among Federal, State, regional, and local public agencies with activities conducted in the vicinity of public-use airports.
5. Methods for achieving the greatest degree of consistency in the planning of agencies referred to paragraph (4).

(b) MODEL STATE STATUTE IMPLEMENTATION.—After publication of the model State statute developed under subsection (a), the Secretary shall, upon request of the Governor of a State, assist the State in adopting the model statute in the State. Such assistance may include the support of a federally organized airport vicinity land use task group. Members of any such group shall have experience in the legislative, legal, and public relations aspects of airport vicinity land use planning, as well as familiarity with the model statute.

(c) REPORT.—The Secretary shall, upon development of a model
State statute under this section, transmit a report to Congress and the President containing a description of such statute.

SEC. 9 AIRPORT ECONOMIC SIGNIFICANCE.

(a) NATIONAL SIGNIFICANCE.—The Secretary shall conduct research and establish a methodology for determining the relationship between airport system capacity enhancement alternatives and the overall performance of the national economy, including the impact of such alternatives on private sector production of goods and services and on the Nation’s international competitiveness.

(b) REGIONAL SIGNIFICANCE.—The Secretary, in consultation with the States, shall establish a preferred methodology for estimating the regional economic significance of airports in the United States. Such methodology shall define categories of economic impact and benefit and specify the data required to determine the value of impacts and benefits. The Secretary may also develop an alternative methodology for estimating economic significance for use by airports unable to assemble the data required by the preferred methodology because of the expense of assembling such data. Any such alternative methodology shall include parameters to assist airports in determining various categories of impact and benefit.

SEC. 10. DEFINITIONS.

For the purposes of this Act, definitions contained in section 503 of the Airport and Airway Improvement Act of 1982 shall apply.
To establish the Council on Civil Aviation Noise.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Council on Civil Aviation Noise Act of 1990."

SEC. 2. ESTABLISHMENT.

There is established a council to be known as the "Council on Civil Aviation Noise" (hereinafter in this Act referred to as the "Council").

SEC. 3. DUTIES; REPORTS.

(a) DUTIES.—

(1) FORMULATION OF PRINCIPLES.—The Council shall formulate broad governmental, economic, and social principles to guide private and public actions to abate and control civil aviation noise and its impacts in the United States. In formulating such principles, the Council shall take into account the needs of individuals and institutions affected by civil aviation noise. Such needs include—

(A) clearer accountability by private and public interests involved in civil aviation decisionmaking;

(B) increased cooperation among interests affected by civil aviation noise in the development of noise abatement and control actions;

(C) a better process for identifying and responding to concerns of individuals relating to civil aviation noise;

(D) a means of balancing public and private interests on civil aviation issues and of balancing local, regional, State, national, and international interests on such issues; and

(E) clearer definition of national interests which should be considered by individuals making local, regional, and State decisions affecting civil aviation noise.

(2) RESEARCH.—In addition to its duties under paragraph (1), the Council shall conduct research to assist in the development of comprehensive Federal legislative and administrative initiatives on the issue of civil aviation noise. Such research shall include a study of—

(A) the costs and benefits of various civil aviation noise abatement and control actions;

(B) economic parameters to determine the need for and the
level of compensation for economic injury from civil aviation noise;

(C) the impact of various airport use restrictions on the flow of interstate and foreign commerce;

(D) safety considerations associated with civil aviation noise abatement and control actions;

(E) the technical and technological requirements for effective civil aviation noise abatement and control actions and the role of science in achieving better private and public decision-making in this area; and

(F) alternatives for raising revenues needed for noise abatement and control actions.

(b) REPORTS.—

(1) INITIAL REPORT.—Not later than 4 months after the date of the first meeting of the Council, the Council shall transmit to the President and Congress a report containing a brief description of—

(A) the principles formulated under subsection (a)(1); and

(B) the areas of research which the Council plans to pursue under subsection (a)(2).

(2) SUMMARY OF RESEARCH.—Not later than 12 months after the date of the first meeting of the Council, the Council shall transmit to the President and Congress a summary of its research under subsection (a)(2).

(3) FINAL REPORT.—Not later than 18 months after the date of the first meeting of the Council, the Council shall transmit to the President and Congress a final report containing the text of the reports transmitted under paragraphs (1) and (2) together with a description of comprehensive Federal legislative and administrative initiatives which promote the principles formulated by the Council under subsection (a)(1).

SEC. 4. MEMBERSHIP.

(a) NUMBER AND APPOINTMENT.—The Council shall be composed of 14 members appointed not later than 90 days after the date of the enactment of this Act as follows:

(1) The Secretary of Transportation.

(2) One Member of the Senate appointed by the President pro tempore of the Senate.

(3) One Member of the House of Representatives appointed by the Speaker of the House of Representatives.

(4) Eleven individuals appointed by the Secretary of Transportation in accordance with subsection (b).
(b) QUALIFICATIONS.—

(1) INTERESTS TO BE REPRESENTED.—Members appointed under subsection (a)(4) shall include the following:

(A) The Governor of a State with a civil aviation noise problem.
(B) A representative of a major public use airport.
(C) An elected official from two units of local government representing areas heavily impacted by civil aviation noise.
(D) A chief executive officer of a major commercial passenger air carrier.
(E) A chief executive officer of a major commercial cargo air carrier.
(F) An experienced air transport rated aircraft pilot.
(G) A representative of the aircraft manufacturing industry.
(H) Two homeowners living in communities heavily impacted by civil aviation noise.
(I) A representative of a public school or school district heavily impacted by civil aviation noise.

(2) QUALITIES.—Each member appointed under subsection (a)(4) shall possess the following qualities:

(A) Demonstrated leadership on civil aviation issues.
(B) Ability to credibly represent the concerns of the group which they represent.
(C) Ability to thoughtfully weigh and balance the diverse interests associated with civil aviation noise.

(c) CONTINUATION OF MEMBERSHIP.—If a member was appointed to the Council as a Member of Congress and that member leaves that office that individual may continue as a member for not longer than the 60-day period beginning on the date that individual leaves that office.

(d) TERMS; VACANCIES.—Members shall be appointed for the life of the Council. A vacancy in the Council shall be filled in the manner in which the original appointment was made.

(e) COMPENSATION; TRAVEL EXPENSES.—Members shall serve without pay. Each member appointed under subsection (a)(4) shall receive travel expenses, including per diem in lieu of subsistence, in accordance with sections 5702 and 5703 of Title 5, United States Code.

(f) QUORUM.—Seven members of the Council shall constitute a quorum but a lesser number may hold hearings.

(g) MEETINGS.—The Council shall meet at the call of the Chairman or a majority of its members. The first meeting of the Council shall be called
promptly by the Secretary of Transportation after the appointment of its members.

(h) CHAIRMAN; VICE CHAIRMAN.—At the first meeting of the Council, the members shall elect a chairman and vice chairman from among its members.

(i) VOTING.—Each member of the Council shall be entitled to 1 vote which shall be equal to the vote of every other member of the Council.

SEC. 5. ADVISORY GROUP.

(a) ESTABLISHMENT.—There is established an advisory group to provide such assistance and advice as the Council may request.

(b) MEMBERSHIP.—The advisory group shall be composed of 10 members as follows:

1. The Administrator of the Environmental Protection Agency, who shall be the Chairman of such group.
2. The Secretary of Housing and Urban Development.
3. The Secretary of Commerce.
4. The Chairman of the National Transportation Safety Board.
5. The Chairman of the National Governors Association.
6. The President of the National Conference of State Legislatures.
7. The President of the National Association of Counties.
8. The President of the National Association of Regional Councils.
9. The President of the National League of Cities.
10. The President of the United States Conference on Mayors.

(c) COMPENSATION.—The members of the advisory group shall serve without pay.

(d) TERMINATION.—The advisory group shall cease to exist upon the submission of the final report required in section 3(b)(3) of this Act.

(e) INTERNATIONAL ISSUES.—The Council shall also consult with the Secretary-General of the International Civil Aviation Organization and the Director General of the International Air Transport Association, as appropriate.

SEC. 6. DIRECTOR AND STAFF OF COUNCIL; EXPERTS AND CONSULTANTS.

(a) DIRECTOR.—The Council shall, without regard to section 5311(b) of Title 5, United States Code, have a Director who shall be appointed by the Council. The Director shall be paid at a rate not to exceed the rate of basic pay payable for level I of the Executive Schedule.

(b) QUALIFICATIONS OF DIRECTOR.—The Director shall be appointed
from among individuals who have demonstrated knowledge of aviation matters and a strong sense of public service in aviation.

(c) STAFF.—The Council may appoint and fix the pay of such additional personnel as the Chairman considers appropriate. Such additional personnel shall not exceed 10 individuals and each individual appointed shall be compensated at a rate not to exceed the annual rate of basic pay payable for GS-18 of the General Schedule.

(d) EXPERTS AND CONSULTANTS.—The Council may procure temporary and intermittent services under section 3109(b) of Title 5, United States Code.

(e) DEPARTMENT OF TRANSPORTATION STAFF.—Upon request of the Council, the Secretary of Transportation may detail not to exceed 10 employees of the Department of Transportation to the Council to assist it in carrying out its duties under this Act. Any detailing of personnel under this subsection shall be without reimbursement by the Council to the Department of Transportation.

SEC. 7. POWERS OF COUNCIL.

(a) HEARINGS AND SESSIONS.—The Council may, for the purpose of carrying out this Act, hold hearings, sit and act at times and places, take testimony, and receive evidence as the Council considers appropriate.

(b) POWERS OF MEMBERS AND AGENTS.—Any member or agent of the Council may, if so authorized by the Council, take any action which the Council is authorized to take by this section.

(c) RULES AND REGULATIONS.—The Council may adopt such rules and regulations as may be necessary to establish its procedures and to govern the manner of its operations, organization, and personnel.

(d) OBTAINING OFFICIAL DATA.—The Council may request from the head of any department or agency of the United States information and technical assistance necessary to enable it to carry out this Act. Each such department or agency shall to the extent permitted by law and subject to the exemptions set forth in section 552 of Title 5, United States Code, furnish such information or assistance to the Council, upon request of the Chairman or Vice Chairman of the Council.

(e) MAILS.—The Council may use the United States mails in the same manner and under the same conditions as other departments and agencies of the United States.

(f) ADMINISTRATIVE SUPPORT SERVICES.—Upon the request of the Council, the Administrator of General Services shall provide to the Council, on a reimbursable basis, the administrative support services necessary for the Council to carry out its duties under this Act.

(g) CONTRACT AUTHORITY.—The Council may contract with and compensate government and private agencies or persons for the purpose of
conducting research or surveys necessary to enable the council to discharge its duties under this Act, without regard to section 3709 of the Revised Statutes (41 U.S.C. § 5).

SEC. 8. TERMINATION.

(a) IN GENERAL.—The Council shall terminate 30 days after submitting its final report under section 3(b)(3).

(b) DISPOSITION OF REMAININGFUNDS ANDPROPERTY.—Any funds held by the Council on the date of its termination under subsection (a) shall be deposited in the general fund of the Treasury and credited as miscellaneous receipts. Any property (other than funds) held by the Council on such date shall be disposed of as excess or surplus property.

SEC. 9. SECRETARY OF TRANSPORTATION.

In each of the first 3 years beginning after the Council submits a final report pursuant to section 3(b)(3), the Secretary of Transportation shall submit to Congress a report which contains a description of Federal efforts to implement administrative initiatives recommended by the Council together with the Secretary's recommendations for such legislative actions as may be necessary to achieve a comprehensive Federal civil aviation noise policy which is consistent with the principles adopted by the Council.

SEC. 10. AUTHORIZATION OF APPROPRIATIONS.

There is authorized to be appropriated to carry out this Act $5,500,000 for each of fiscal years 1991 and 1992.

SEC. 11. BUDGET ACT COMPLIANCE.

Any spending authority, as defined in section 651(c)(2)(A) and (C) of the Congressional Budget Act of 1974 (2 U.S.C. § 651(c)(2)(A) and (C)), authorized by this Act shall be effective only to such extent and in such amounts as are provided in appropriation Acts.
Canadian Transport Liberalization: Planes, Trains, Trucks & Buses Rolling Across the Great White North*

PAUL STEPHEN DEMPSEY**
WILLIAM E. THOMS***
& SONJA CLAPP****

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V. DEREGULATION AND THE BUS INDUSTRY ................................. 183

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To this American visitor, Canada has always been a very attractive place, with an appeal that goes far beyond its trains. Geologically, the world’s second largest country has been graced with an incredible diversity of compelling scenery, from the 40-foot tides of the Bay of Fundy to the endless pines of western Ontario, from the yellow flatness of Saskatchewan to misty rain forests of coastal British Columbia. Culturally, Canada’s mix of French and English heritage provides an agreeable touch of Europe close to home. And socially, Montreal, Toronto and Vancouver are forceful reminders that big cities need be neither ugly nor dangerous unless people let them get that way.


I. INTRODUCTION

As a huge and disparate country, Canada has been dependent on good transportation lines to keep its people together and to safeguard its sovereignty. Railroad construction was mentioned in the British North America Act and was on the minds of the Fathers of Confederation. The
construction of the Canadian Pacific Railway kept the Canadian west from falling into the hands of James J. Hill and his Great Northern Railway. Rail service developed the ports of Vancouver, Prince Rupert, Thunder Bay and Churchill, thus giving export potential to the farmers of the Prairie Provinces. The Riel Rebellion, the last serious threat to Canadian sovereignty in the West, was crushed with the aid of the Canadian Pacific, which ferried crack troops from Montreal to Regina to put an end to the revolt.

Motor carriers of passengers and property made possible the development of communities not served by good rail service. Buses still serve Canadian communities and regions with no alternative service, as well as competing with trains and even planes in the urban corridors of Ontario and Quebec. Trucking companies, based on both sides of the Canadian-U.S. border, are able to use Canada’s excellent highway system to bring deliveries to small and medium-size cities and towns through the Dominion. Only a few reaches of the far north are not served by all-weather highways and even there, intermodal service allows trucks and trailers to be piggybacked to these remote communities by rail.

More than any other factor it has been the development of air service which has made Canada accessible to the whole world and has brought the most remote portions of the country into the Canadian community. There are no roads north of Thompson, Manitoba; there are no rails north of Churchill. But the arctic and subarctic regions are now linked with Toronto, Winnipeg, Montreal and Vancouver by daily air service, and the planes are relied upon for day-to-day transportation as well as the necessities of life. Canada’s two principal airlines, Air Canada and Canadian Airlines International, link the frozen tundra with the urban fringe along the U.S. border where 90% of the country’s population lives. Canadian airlines also show the Maple Leaf in every continent of the world through the international air routes of the two principal carriers. As a major airfaring nation, Canada has a tremendous stake in the future of international aviation. The headquarters of both the International Air Transport Association and the International Civil Aviation Organization (the U.N.’s specialized agency for air transportation) are located within a few blocks of each other within the city of Montreal.

II. DEREGULATION OF THE AIRLINE INDUSTRY IN THE UNITED STATES AND CANADA

A. INTRODUCTION

The mid-1970s was a turning point for the civil aviation industry in both Canada and the United States. The policy that emerged emphasized more reliance on competitive market forces and less governmental con-
trol of what was once a highly regulated industry. Both Canada and the United States began a process of "de facto deregulation" of their respective domestic airline industries which was subsequently codified by statute. Deregulation of the aviation industry had two dimensions. First, deregulation represented a new substantive policy of competition for domestic aviation. Second, deregulation was also the process of the regulatory changes and elimination of governmental controls.¹

In October, 1988 the United States marked the tenth anniversary of the promulgation of the Airline Deregulation Act of 1978.² The Act's purpose was to encourage, develop and attain an air transportation system which relied on market forces to determine the quality, variety and price of air service.³ Canada began reform of its economic regulatory framework in 1984, culminating the passage of the new National Transportation Act,⁴ effective January 1, 1988.⁵ Canadian deregulation, usually referred to by Canadians as "economic regulatory reform", is still unfolding. The reform is intended to ensure the existence of economic and efficient carriers and at the same time provide reasonable fares and adequate service to Canadians.⁶

During the past decade, the United States witnessed a number of significant developments within its aviation industry. There have been three distinct phases of deregulation:⁷

1) Expansion in the number of carriers in 1978, followed by a marked reduction of carriers in 1985;
2) Consolidation of carriers through mergers. Buyouts of smaller regional carriers;
3) Concentration among large carriers.

The U.S. deregulation experience has become a model for Canada and the rest of the free world.⁸ The model is not without flaws, including increased concentration and market power among major carriers, anticompetitive practices, bankruptcies, mergers, a gradual rise in airfares,

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³ See generally, 49 U.S.C. app. § 1302 (1982). Section 1302 of the ADA states that the Board in performing its functions shall consider the public interest. Id. Competition to the extent necessary to assure sound development of the airlines along with fostering of economic conditions is in the public interest. Id.
⁶ NTA, 1987, supra note 4 at art. 3(1).
⁷ 14TH ANNUAL FAA CONFERENCE, supra note 5 at 20.
⁸ Id. at 21.
minimal labor protection and serious safety concerns.\(^9\)

In this section we will examine the airline industry, its deregulation and post-deregulation effects in both the United States and Canada. Deregulation in the United States and Canada is similar, and yet unique. In order to achieve adequate and efficient air transportation, both countries have relied on: 1) the abolition of independent regulatory tribunal discretion in licensing and fare regulation, thereby opening the industry up to free market competition; and, 2) the suitability and effectiveness of competition laws to ensure fair market competition.\(^10\)

\section*{B. UNITED STATES}

\subsection*{1. DEREGULATION}

Prior to 1978, the United States airline industry was accustomed to extensive government regulation and intervention. The regulatory agency known as the Civil Aeronautics Board\(^11\) (CAB) promoted both the safety and economic aspects of civil aviation. The Federal Aviation Agency (FAA) assumed the control over the safety aspects of the U.S. airline industry in 1958. The CAB continued to exercise economic control over routes, fares, labor, mergers and acquisitions.

The CAB began the process of regulatory reform in 1977.\(^12\) Alfred Kahn was appointed chairman of the CAB by U.S. President Jimmy Carter. Kahn was a proponent of free market competition for the aviation industry and an advocate of deregulation.\(^13\) Prior to any legislative reform, Kahn embarked on a program of "\textit{de facto} deregulation" within the framework of the existing regulations.\(^14\) Some examples of Kahn's \textit{de facto} deregulation were as follows:

1. Low fares became a factor in carrier selection for service routes;
2. New route authority was granted to multiple carriers thereby allowing market forces to determine which carrier would most effectively service the route;
3. Carriers were given some pricing freedom.\(^15\)

\begin{itemize}
\item \textit{See generally}, P. DEMPSEY, \textsc{The Social and Economic Consequences of Deregulation} (1989).
\item Phillips, supra note 1 at 2.
\item Civil Aeronautics Act of 1938, ch. 601, 52 Stat. 973 (1938) (codified as amended at 49 U.S.C. app. § 1321(a) (1982)). In 1938, Congress passed the Civil Aeronautics Act which created a five-member independent regulatory agency known as the Civil Aeronautics Board (CAB). The CAB’s purpose was to promote and regulate the safety and economic aspects of civil aviation. \textit{Id.}
\item E. BAILEY, D. GRAHAM & D. KAPLAN, \textsc{Deregulating the Airlines} 12 (1985) [hereinafter E. BAILEY].
\item Phillips, supra note 1 at 5-6.
\item \textit{Id.}
\item \textit{Id.} at 6. Dempsey, \textsc{The Rise and Fall of the Civil Aeronautics Board: Opening Wide the Floodgates of Entry}, 11 Transp. L.J. 9 (1979).
\end{itemize}
The Airline Deregulation Act\textsuperscript{16} (ADA) was signed into law on October 28, 1978. The ADA proposed a gradual relaxation of the CAB's regulatory powers with a four year phase out over controls of rates and routes.\textsuperscript{17}

By January 1, 1982, the CAB's domestic route and licensing authority based upon "public convenience and necessity" expired and any existing carrier was allowed to enter any domestic route of its choice,\textsuperscript{18} so long as it could demonstrate that it was "fit, willing and able" to operate.\textsuperscript{19} Consistent with freedom of entry was freedom of exit from unprofitable markets.\textsuperscript{20} No application or agency approval was necessary for the abandonment of a route; only notice provisions were required. A provision for essential air service to small communities was included in the legislation.\textsuperscript{21}

The ADA sought to encourage competition in the domestic aviation industry by coupling greater pricing freedom for carriers with greater protection against anti-competitive pricing practices.\textsuperscript{22} With respect to fares, Section 102(3) of the ADA called for "the availability of adequate, economic, efficient and low price fares without unjust discrimination, undue preference or advantageous or unfair deceptive practices."\textsuperscript{23}

The CAB controlled rates until January, 1983. During the interim, between 1978 and 1983, carriers were given greater pricing freedom. The CAB was required to accept as "just and reasonable" any fare that represented an increase of up to 5\% above the standard industry fare level (SIFL) or as much as 50\% decrease below the SIFL.\textsuperscript{24} When the CAB's fair regulation function ceased entirely, it was the intent of Section 102(3) of the ADA to permit carrier pricing freedom so as to allow fares to stabilize at levels that would attract passengers as well as earn a profit for the airlines.

Section 102(7) of the ADA called for "the prevention of unfair, deceptive, predatory or anti-competitive practices in air transportation and the avoidance of:

a) unreasonable industry concentration, excessive market domination and monopoly power and

b) other conditions that would tend to allow one or more air carriers unreas-
sonably to increase prices, reduce services or exclude competition in air transportation.\textsuperscript{25}

More than a decade later, the empirical results are not significantly different from those predicted by deregulation's opponents. In fact, the air transportation system in the United States today appears to be antithetical to the above described purposes of the ADA.

2. \textbf{EFFECT OF Deregulation ON THE DOMESTIC AVIATION INDUSTRY IN THE UNITED STATES}

The manner in which U.S. commercial carriers conduct their business, as well as the domestic aviation structure as a whole, has been affected by deregulation.\textsuperscript{26} Deregulation has impacted service, airfares, airline financial performance, safety and labor protections.

Between 1938 and 1978 the CAB had adopted a protectionist attitude toward existing carriers.\textsuperscript{27} The CAB maintained the status quo by restricting both the entry of new carriers into existing routes and fare reductions to attract new passengers. Thus, carriers were protected from financial ruin resulting from destructive competition.\textsuperscript{28} Deregulation gave American carriers unlimited freedom of choice in route network planning decisions.\textsuperscript{29} The only existing barrier was raising enough capital to enter the market. Prior to deregulation there were approximately 36 interstate carriers. This number grew to 229 in early 1984, 22 of which were brand new carriers.\textsuperscript{30}

The United States is now experiencing excessive concentration among its major carriers and anti-competitive practices in the airline industry. "After a dozen years of warfare in the open skies above the United States and a wave of mergers, the domestic airlines have been consolidated into an industry of megacarriers."\textsuperscript{31} Approximately 214 airlines have disappeared or merged into harder carriers.\textsuperscript{32} Established carriers such as National, Western, Pacific Southwest, Frontier, Ozark and Republic have ceased to exist.\textsuperscript{33} Vanished is the fleet of early deregulation upstarts such as People Express, Muse Air, Air Florida, Pride Air, Jet America and Empire.

Prior to deregulation the five largest U.S. carriers controlled 63% of

\begin{itemize}
\item \textsuperscript{25} Id. at 9-10.
\item \textsuperscript{26} Id. at 13.
\item \textsuperscript{27} Id.
\item \textsuperscript{28} E. Bailey, supra note 12 at 95-96.
\item \textsuperscript{29} Phillips, supra note 1 at 13.
\item \textsuperscript{30} Id. at 14.
\item \textsuperscript{32} TIME, May 15, 1989 at 52, col. 1.
\item \textsuperscript{33} Id. at 52, col. 1-2.
\end{itemize}
the passenger business. Supporters of the deregulation hoped to reduce the concentration of the market share among the top carriers. The results have been to the contrary. Today, American Airlines is the largest carrier of domestic traffic, and operates 119 weekly flights to 13 European cities. Ranked by size, American is followed by United, Delta, Northwest and Continental. Together these five airlines control 70% of the industry's U.S. traffic.

Further diminishing the ranks of the U.S. carriers are bankruptcies and take-over bids. Among the more notable bankruptcies are Braniff (1982 and 1989), Continental (1983), Frontier (1986), and Eastern (1989). Pan Am is also on the verge of being swallowed up and or dismantled after losing $151 million during the first quarter of 1989 and a $73 million annual loss for 1988. Four airlines today have a negative net worth — Eastern, Continental, TWA and Pan Am.

Eastern entered Chapter 11 bankruptcy in March of 1989 after a strike by its machinists virtually shut it down. In April, 1989, former commissioner of major league baseball and financier Peter Ueberroth, bid $464 million to purchase the bankrupt Eastern. In May, 1989, wheeler-dealer Donald Trump's agreement to buy Eastern's shuttle operations for $365 million was briefly jeopardized by a higher bid from Phoenix-based America West Airlines. At the same time, Northwest was fighting a take-over by Denver oilman Marvin Davis, who bid $2.6 billion for the airline. In 1989 the Department of Transportation approved a $3.65 billion leveraged buyout of Northwest by a group of investors led by Alfred Checchi.

The possible takeover of Northwest prompted a bill in the 1989 Minnesota legislative session that would have extended the protections of Minnesota's anti-takeover law to Northwest Airlines. Part of the bill dealing with worker and consumer protections in the event of a takeover made it to the senate floor. Ultimately the bill failed to pass.

The development of the hub and spoke route system is a major change in commercial aviation and is today one of the major factors con-
tributing to the anti-competitive practices in the U.S. airline industry. The hub and spoke system is a method of feeding travelers from small cities into a central hub where they can catch connections on the same airline to other points.43

The CAB had favored a nonstop linear route system. Carriers had to provide this type of service to avoid losing their route authority in favor of other carriers.44 Many city-pair markets could not profitably support direct nonstop service. Therefore, the airlines often added routes which connected into the nonstop city-pair markets to add sufficient traffic flow. Both the nonstop and backup routes remained fairly stable under the authority of the CAB.45

Deregulation changed this essentially linear traffic pattern into a hub and spoke system because of the increased competition in the backup markets. Local carriers which had previously funneled their passengers to major carriers were now extending their routes to keep passengers until their final destination.46 During the early years of deregulation, major U.S. carriers endured their worst losses in history due to the onslaught of head-to-head competition until fortress hubs could be created. American and United suffered fewer losses because their east-west routes continued to attract business travelers who tended to pay full rates.47

Delta and Piedmont pioneered the hub and spoke system in the South. Major airlines began creating their own hub airports thereby saving on maintenance costs, baggage handling and other ground services.48 The major airlines also began merging with feeder airlines from the backup markets as well as with carriers from other regions. For example, Northwest bought Republic thereby gaining dominance in Minneapolis and Detroit; it also has hubs in Memphis and Milwaukee. Atlanta-based Delta bought Western taking over its hub in Salt Lake City. TWA purchased Ozark resulting in a domination of St. Louis.49

The airlines have benefited from the hub and spoke system in several ways. By linking flights at hubs and tightly coordinating arrivals and departures, airlines are able to offer more frequent service and carry more passengers to a wider variety of destinations than by flying linear route patterns.50 The hub and spoke system also allows the airline to carry

43. TIME, May 15, 1989, at 52. col. 2. See also, 14th ANNUAL FAA CONFERENCE, supra note 5 at 20.
44. Phillips, supra note 1 at 18.
45. Id.
46. Id.
48. Id. at 53, col. 3.
49. See generally, TIME, May 15, 1989, at 52-54.
50. Phillips, supra note 1 at 19.
more passengers from the point of origin to the final destination without having to turn them over to a competitor.

But for the airline passenger, hub and spoking has meant less non-stop service, more frequent changing of planes, use of smaller planes on connecting routes, more delays at hubs and higher airfares.\(^{51}\) With the concentration of between one and two carriers at each hub, there is less competition. There appears to be a direct relationship between the number of competitors and average fare levels.\(^{52}\) Since January, 1989, ticket prices have risen approximately 15%.\(^{53}\)

The hub and spoke system has also had a pronounced effect on traffic patterns in individual markets in the United States. There has been a general increase in weekly departures and boardings at large and medium hubs. Smaller hubs have had less of an increase, while non-hubs have had decreases. Many small communities have lost air service completely.\(^{54}\)

Airline travel in the United States has doubled from 240 million trips in 1977 to 447 million trips in 1987. But during this period, no major airports have opened. The focus of competition has now shifted from cut-rate fares to control of airport departure gates and takeoff and landing slots at the hubs.\(^{55}\) Many hubs are filled to capacity and there is little turnover in gates which hinders new applicants who wish to use the airport controlled by a major carrier. Many airlines that were unable to secure gates and takeoff and landing slots were forced out of business.\(^{56}\) As the public's demand for increased travel grows, the megacarriers controlling the hubs are easily able to add flights to meet this demand. New carriers are virtually barred from entering the market. Investors are reluctant to enter the airline business except as buyers of existing carriers and their gates and landing and takeoff slots.\(^{57}\)

U.S. Transportation Secretary Samuel Skinner has expressed concern about the concentration of mega airlines and their control of the

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\(^{51}\) Id.


\(^{53}\) TIME, May 15, 1989, at 52. If the passenger lives in a place at which his airport is dominated by one airline such as in Charlotte, Detroit or Minneapolis-St. Paul, he may be paying 27% more than passengers in competitive cities such as Los Angeles, Miami or Philadelphia. Grand Forks Herald, June 7, 1989, Part B at 5, col. 3. Accord, 14th ANNUAL FAA CONFERENCE, supra note 5 at 83.


\(^{55}\) TIME, May 15, 1989, at 53, col. 3. Accord, 14th ANNUAL FAA CONFERENCE, supra note 5 at 84.

\(^{56}\) TIME, May 15, 1989, at 53, col. 3.

\(^{57}\) Id. at 53-54.
hubs. Skinner believes that building new airports may be one solution. Building new airports and expanding existing ones would add more gates and hence more competition for existing carriers. The Dallas-Fort Worth airport, completed in 1974, was the last new airport built in the United States. In May of 1989 Denver voters approved the construction of a new huge airport, estimated to cost $2.3 billion. Serious congestion is expected at the nation’s approximately 58 airports by the year 2001. Seven major airports (Chicago, Detroit, Los Angeles, New York, Phoenix, St. Louis, and San Francisco) need to be replaced. New airports require massive sums of money and approximately 10 years to complete. Other than Denver, only Austin has proposed a new airport, slated for 1995.

Along with the concerns regarding concentration of mega carriers and their control of airport hubs is the competition in computer reservation systems (CRS). CRS is vital to an airline’s ability to compete and survive. The automated reservation systems are vast computer networks that major carriers use to disperse up-to-date flight information to travel agents. Travel agents linked to the system can check schedules, compare fares, book tickets and reserve hotel rooms and rental cars. The CRS network is vital to the airlines not only to fill its seats, but to fill seats in a profitable way. Travel agents depend heavily upon the CRS network to book passengers often at the expense of carriers without computers. American Airlines SABRE system (Semi-Automated Business Research Environment) is dominant and used by about 14,000 agencies to keep up with the 45 million fares of 281 airlines.

James Oberstar, U.S. House of Representatives (D-Minn.) stated that to sustain the energy of deregulation, there must be a market place in which there is not only competition, but also the underpinnings for competition. The CRS network is an economic underpinning that must be open to competition. The four top U.S. carriers control approximately 66% of the CRS market and nearly 87% of all flights are booked through carriers with CRS.

The major changes in U.S. commercial aviation during the past decade have threatened the economic underpinnings of deregulation as ex-

58. Id. at 54, col. 2.
59. Id.
63. Id.
64. Id.
65. Id. The second largest CRS network, United’s Apollo, is used by 10,000 agencies.
66. 14th ANNUAL FAA CONFERENCE, supra note 5 at 83.
67. Id. See also, TIME, May 15, 1989, at 54, col. 1.
pressed by the ADA. The competition needed to sustain the lower fares of deregulation is shrinking. Since 90% of all Canadians live within 150 miles of the United States border and avail themselves of many U.S. flights, Canadian airline consumers are also directly affected by the deregulation of the U.S. aviation industry. For the airline passenger, deregulation brought a brief period of low airfares and many new carriers serving the routes. The tourist-oriented traveler has probably received a major benefit through discount tickets with certain restrictions. Some airline passengers in high density markets and on long haul routes also reaped the benefit of discounts. The average business traveler in the United States has had the least benefit of deregulation and pays more for his airfare in real terms. With the advent of the hub and spoke route system and the bankruptcy and takeover of many new competitors, the average consumer now experiences more crowded planes, flight delays and rising airfares. Those passengers living in smaller cities or remote areas have limited and more expensive or no air service at all.

Concerns have been expressed that market domination by a small group of megacarriers could result in a highly uncompetitive airline industry. Instead of regulation resting with the government, competition will be thwarted by the power wielded by the megacarriers which control the scarce amount of space available at major airports, the computer reservations systems, the frequent flyer programs, and enjoy the scale economies of hub and spoke operations.

C. CANADA

The year 1984 marked the beginning of Canada's reform of its economic regulatory framework (i.e., deregulation) over airlines. Having embarked upon deregulation in a different manner and somewhat later, Canada has been able to observe some of the negative effects in the United States. Canadian airline deregulation has been unique in several ways. First, the United States has a specific policy for its aviation industry. Canada has a broad transportation policy which includes airlines, railways and motor carriers. Canada's flight patterns are principally transcontinental, from east to west, due to Canada's geography and population. Unlike the United States, Canada embarked upon deregulation with a mixture of private and government owned airlines. Finally, the Canadian government has not completely deregulated its airline industry.

68. See supra, note 24 and accompanying text.
70. FREEDOM TO MOVE IN CANADA'S A NEW TRANSPORTATION ENVIRONMENT, Minister of Supply and Services Canada 1988, Cat. No. T22-74/1988 E, 2-3, [hereinafter FREEDOM TO MOVE].
Canada's two major transcontinental carriers are Air Canada and Canadian Airlines International. Until 1989, Air Canada was a Crown Corporation wholly owned by the Canadian government; the Minister of Transportation acted as a trustee and shareholder for the Federal Government. In August of 1988, the Canadian government announced its intention to sell 45% of Air Canada to the public. A 100% sell-off was completed by the Fall of 1989.

Canada's second major carrier has always been privately owned. The Canadian Pacific Railway operated this, the second largest airline in Canada, formally known as Canadian Pacific Airlines, or more popularly as CP Air. In 1986, CP Air was purchased by Pacific Western Airlines (PWA), a former regional carrier, thus forming Canadian Airlines International.

In addition to the two transcontinental carriers, Canada's federal policy prior to 1984 also provided for four major regional carriers which supplemented the main line operations of the nationals. Each carrier was restricted to a section of Canada: 1) Pacific Western Airlines served western Canada and the Northwest Territories; 2) Transair Limited served the Prairie Provinces of Manitoba and Saskatchewan, the Northwest Territories and Ontario; 3) Quebecair served Quebec and Labrador; and, 4) Eastern Provincial Airways served the Maritime Provinces (New Brunswick, Nova Scotia, Prince Edward Island, Newfoundland), and Quebec. A third level consisted of smaller local carriers. Regulation of the transportation industry in Canada served to prevent the two transcontinental carriers from competing with the regionals.

1. **REGULATORY STRUCTURE PRIOR TO DEREGULATION**

Canada implemented deregulation on January 1, 1988. Prior to deregulation, transportation, including aviation, was governed by the policy guidelines of the National Transportation Act, 1967. The National Transportation Act created the Canadian Transport Commission (CTC) which functioned as an independent regulatory body for all modes of transportation including air, rail and motor carriers. The Aeronautics

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74. Phillips, *supra* note 1 at 49.
75. 14th ANNUAL FAA CONFERENCE, *supra* note 5 at 108.
77. Phillips, *supra* note 1 at 44. Until deregulation was implemented in Canada effective January 1, 1988 the economic regulation of Canada was governed by the policy guidelines outlined in the National Transportation Act, 1966-67, c. 69 and the licensing and fare control functions of the Air Transport Committee as enumerated in the Aeronautics Act R.S.C. c. 2. *Id.*
Act\textsuperscript{78} granted the CTC's Air Transport Committee (ATC) licensing and fare control in aviation using the familiar "public convenience and necessity" criteria.\textsuperscript{79} Despite the appearance of continued regulation by the above-named government bodies, the 1967 National Transportation Act marked the government's first move away from direct economic regulation and toward competition in the market place.\textsuperscript{80}

Section 3G of the 1967 National Transportation Act outlined the basic policy for all modes of transportation as an "... economic, efficient and adequate transportation system making the best use of all available modes of transportation at the lowest total cost."\textsuperscript{81} The Act, however, contained a limiting phrase, "... having due regard to national policy and to legal and constitutional requirements."\textsuperscript{82} "Due regard to national policy" referred to policy as outlined by the Minister of Transport. This limiting phrase prevented the move to complete regulation by market forces.

In 1969, the Minister of Transport announced a new policy clearly specifying the boundaries in which the regional carriers could operate.\textsuperscript{83} The regional carriers were "preferred vehicles" whose roles were to operate local and regional routes that supplemented the two major transcontinental carriers (i.e., Air Canada and the then CP Air).\textsuperscript{84} Thus, the regional carriers were placed in a protected and noncompetitive role.

One of the transcontinental carriers, Air Canada (A Crown Corporation), was created by the 1937 Trans-Canada Airlines Act.\textsuperscript{85} The 1937 Act reflected the Canadian government's desire to contribute to the economic and political integration of the country and to thwart the entry of American-owned carriers. Trans-Canada Airlines (known as Air Canada since 1964) was established to supply services no existing carrier was then providing.\textsuperscript{86} The Air Canada Act of 1977 revoked the Air Canada contract, thereby subjecting Air Canada's license applications to the discretion of the ATC. Prior to 1977, Air Canada was free from regulatory control by the ATC except in the matter of tariffs.\textsuperscript{87} Despite the revocation of Air Canada's contract, Air Canada remained the dominant carrier and

\textsuperscript{80} Ellison, \textit{The Rise and Decline of Protective Economic Airline Deregulation in Canada}. 15 TRANSP. L.J. 105, 110 (1986) [hereinafter Ellison].
\textsuperscript{81} \textit{id.}
\textsuperscript{82} \textit{id.} at 110-11.
\textsuperscript{83} \textit{id.} at 111.
\textsuperscript{84} \textit{id.} at 111-12.
\textsuperscript{85} Can. Stat. ch. 43 1937.
\textsuperscript{86} Ellison, supra note 80 at 107.
\textsuperscript{87} \textit{id.} at 110, 113.
price leader in domestic as well as international markets.  

Canada's domestic airline market was also affected by the international airline market. Beginning in the 1960's and continuing in the 1970's, there was a spectacular growth of international air charters (a large portion of that market being the tourist trade) with points of travel often originating in Canada to destinations in both the U.S. and Europe. Canada's regional carriers entered into low fare competition on these long-haul international routes competing with charters such as Wardair (Canada's largest international charter carrier during the mid 1970's) and the American carriers. Thus, the regionals began to access markets beyond their normal boundaries, and the carefully drawn regional carrier boundaries had eroded substantially by 1978.

One of the regional carriers, Pacific Western Airlines acquired another regional, Transair Limited. Subsequent policy decisions by the Minister of Transport and the ATC allowing several regional carriers access to Toronto further altered the regional air carrier policy. By 1981, all regional carriers served Toronto, that city being the major stopping point in the basically East/West trunk lines. The regionals began to fly east-west instead of their former predominantly north-south routes, thereby competing with the nationals.

The federal government's process of reevaluating the domestic aviation competition policy was prompted as Canada observed more and more Canadian passengers crossing the border to the United States to fly on the cheaper airlines such as People Express. Canada was also responding to the U.S. deregulation style prices. This reevaluation process involved numerous governmental departments and agencies. Two noteworthy recommendations came from the House of Commons Standing Committee on Transport and the ATC of the Canadian Transport Commission which conducted cross-country hearings on the issue of aviation

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88. Id. at 114. Although Air Canada's license applications were subject, as were all other domestic carriers to the discretion of the ATC, Air Canada still retained a favorable market position because its debt was backed by the Federal Government. Id.

89. Id. at 114-15.

90. Id. at 115. See also, MACLEAN'S, January 30, 1989 at 35, col. 1.

91. Phillips, supra note 1, at 50.

92. Ellison, supra note 80, at 119.

93. Id. at 114. It became cheaper for Canadian airline passengers to travel across North America to Canadian destinations than it was to travel across Canada to those same destinations. Id. International flights involving both Canadian airlines and foreign airlines are governed by bilateral agreements signed by the Canadian government and the government of the destination country. Cabotage restrictions mean that local traffic within Canada cannot be handled by foreign airlines. Thoms, supra note 79, at 138. The U.S. has successfully attracted passengers in Canada. Agreements allowing the U.S. to maintain customs and immigration agents at Canadian airports assist American carriers in attracting or retaining "through passengers" who connect to other planes of the same carrier at the U.S. hub airports. Id. at 139.
competition.94 The Standing Committee recommended reliance on competition to be a principal means of promoting efficient, convenient, adequate and stable air service. The ATC viewed competition as just another factor of "public convenience and necessity" to be emphasized in the mature southern Canadian markets.95 With these recommendations in mind, the then Minister of Transport, the Honorable Lloyd Axworthy, announced his "New Canadian Air Policy" in May of 1984 as a culmination of the work of the various committees.96 The essence of Axworthy's policy was less regulation and more competition.97 Full deregulation was not implemented, rather a policy of "liberalization" of the existing regulatory framework and its licensing and fare control functions was added.98 The CTC was still in place, but it was directed to use discretion in interpreting the "public convenience and necessity" to favor competition in the skies.99 A "use it or lost it" approach was adopted for carrier service on routes. Financially fit charter airlines were freed altogether from meeting entry requirements.100 Pricing controls were to be totally eliminated; fares were to be lowered within two years, although the maximum price controls would still remain in force.101

The "New Canadian Air Policy" had two major limitations. First, the Minister of Transport could exert pressure on the CTC to exercise discretion within the limits of national policy by virtue of his power to vary or rescind anything done by the CTC.102 Second, the new air policy did not apply to all of Canada. A demarcation line of 50 degrees north in the East and 55 degrees north in the West, Winnipeg being the middle, was drawn. (See Table 1.) The new liberalized policy would apply to the traffic south of that line in which over 90% of the Canadian people live.103 The North would continue to be regulated since its population is smaller and therefore unable to withstand the deleterious effects of excessive competition. In some remote areas, air service is the only mode of transportation.

The "New Canadian Air Policy" eliminated the historic division between the "big two" (Air Canada and Canadian Airlines International for-

94. Phillips, supra note 1 at 50-51.
95. Id. at 54.
96. Id. at 50.
97. Thoms, supra note 79, at 140.
98. Phillips, supra 1 at 50.
99. Thoms, supra note 79, at 140.
100. Id. at 140-141.
101. Id. at 141.
102. Phillips, supra note 1, at 56.
103. Thoms, supra note 79, at 141. The North comprises about 5 percent of Canada’s air carrier activity. 14th ANNUAL FAA CONFERENCE, supra note 5 at 110.
### Table 1

<table>
<thead>
<tr>
<th>Geographic Scope of Liberalization</th>
</tr>
</thead>
<tbody>
<tr>
<td>REGULATED ZONE</td>
</tr>
<tr>
<td>LIBERALIZED ZONE</td>
</tr>
</tbody>
</table>

merly known as CP Air) and the regional and charter carriers. The Minister stated that any new or existing carrier may henceforth be considered, upon application to the CTC, for any type of domestic service, thus making the concept of regional carriers obsolete, as any airline could now apply to serve any region in Canada.

Restrictions that prohibited or limited the frequency of nonstop and turnaround services, and the types and sizes of aircraft or routes were eliminated from existing certificates. The new policy called for greater freedom of entry into routes. The CTC was asked to give greater weight to the benefits of increased competition as a factor of "public convenience and necessity." In line with freer entry, carriers were also given freedom to exit routes subject to certain notice requirements.

The "New Canadian Air Policy" can be compared to the regulatory reform implemented by Alfred Kahn when he was appointed chairman of the CAB in the United States in 1977. In licensing, both national policies required the respective regulatory agencies (CAB and CTC) to rely on market competition as a prime factor in determining "public convenience and necessity." Kahn proposed "zones of reasonableness" to achieve pricing freedom. Axworthy accepted "zones of flexibility" wherein the ATC would determine whether fares were just and reasonable. Unlike the United States Airline Deregulation Act which abolished the CAB, the ATC continued to function and exercise its discretion. Axworthy had to continue to work within the existing regulatory system. The Canadian system gave much broader discretion to the ATC by not legislating specific policy objectives and factors to be used by the ATC in exercising its discretion. Thus, Axworthy ran into difficulty when he was faced with implementing his policy in a manner acceptable to the public but which was ultimately unacceptable to the ATC's view of proper exercise of discretion. Four months later in September 1984, the Liberal government was defeated by the Conservatives under the leadership of Brian Mulroney.

2. **Deregulation of the Canadian Airline Industry**

With this background in mind, we turn to Canada's deregulation under the control of the Conservative government. The Honorable John C. Crosbie, Minister of Transport until 1989, stated that the transportation costs in Canada were higher than they need be. The new system, according to Crosbie, would make Canadian transportation more efficient,
cost-effective and competitive. Less regulation would result in greater choices and competitive airfares. Canadians would be offered more flights at more convenient times and with a variety of fares. There would be provisions for air service to northern and remote communities. "The result is a made-in-Canada transportation policy that reflects this country's unique transportation requirements," said Crosbie. Although it is the second largest country in the world, Canada has a small population. Its transportation system ties the vast nation together.

In July, 1985, the government issued a discussion paper entitled "Freedom to Move." The proposals in this document evolved into the new National Transportation Act as set out in Bill C-18 of the National Transportation Act, 1987, which became effective January 1, 1988.

The National Transportation Act, 1987, abolished the Canadian Transport Commission (CTC) and replaced it with the National Transportation Agency (NTA). The powers of the NTA are to be tailored to the new regulatory "Freedom to Move" approach. The NTA is to respond to public interest, industry needs and policy direction from the government. The legislation calls for the establishment of regional NTA offices in western Canada and the Atlantic provinces.

The NTA has the authority to grant transportation licenses, review public complaints, and help resolve disputes between shippers and transportation firms. One of the NTA's most important functions involves resolving disputes, both public and private, affecting transportation. Dispute resolution can be accomplished through voluntary mediation or arbitration. In keeping with the emphasis on minimal regulation, the Agency can in most instances take action only upon request. Since the Minister of Transport is accountable to Parliament for both the national transportation policy and the Agency's actions, the Minister may issue binding directions upon the Agency.

The NTA is also required to consider the new national transportation

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109. FREEDOM TO MOVE, supra note 70, at i, Foreword.
110. Id.
114. Id.
115. Id.
116. Id. But see, National Transportation Act, 1987, supra note 4 at § 35 (1)(2)(3) (The Agency may inquire into complaints, licensing matters and safety matters).
118. FREEDOM TO MOVE, supra note 70 at 11, col. 2. The government may issue general policy or other binding directions to the Agency. The government may also alter any decision, order or regulation made by the Agency. Id. See also, NTA, 1987, supra note 4 at Part I, § 23.
policy in all its decision making. The policy's principles and objectives are: 1) a safe transportation system; 2) a transportation system to serve the needs of shippers and travelers; 3) competition in market forces as the prime means for providing Canadians with efficient transportation at the lowest possible cost; 4) regulations to be kept simple and at a minimum to encourage competition within the transportation industry; 5) transportation as the key to regional economic development; 6) carriers being required to bear a fair and reasonable share of the cost of facilities provided at public expense and to be compensated for publicly imposed duties; and 7) access to transportation as a basic necessity for Canadians, including disabled travelers.\footnote{FREEDOM TO MOVE, supra note 70, at 4, col. 1. See also, National Transportation Act, 1987, supra note 4 at Part I, § 3.}

The new policy is already apparent in air transportation. The licensing and control of entry into and exit from the industry has abolished the "public convenience and necessity" test. Any carrier may enter a domestic route if it meets the "fit, willing and able" test which focuses on the safety of the carrier and adequate liability insurance.\footnote{Id. at Part II, §§ 67, 72.} The firm must also be 75% Canadian-owned or controlled.\footnote{Id. at Part II, §§ 67, 72.} (The United States has similar statutory restriction over foreign ownership of its flag carriers.) Service, route or equipment restrictions are abolished. The result is carriers which have added new routes to their services, introduced more efficient aircraft in certain markets and offered innovative pricing arrangements. (See Tables 2 & 3.) It should be noted that carriers with only a generic domestic license for southern routes are permitted to fly in or out of the North, but may not fly the northern routes.\footnote{Id. at Part II, § 76.} Carriers wishing to discontinue or reduce service on unprofitable routes need only give 120 days advance notice of their intention to stop or reduce air service. Shorter notices may also be approved by the NTA.\footnote{Id. at Part II, § 79 (1).}

Competitive passenger fares and cargo rates are encouraged by permitting carriers to establish rates and charges without regulatory approval and by allowing carriers to negotiate confidential contracts with their customers.\footnote{FREEDOM TO MOVE, supra note 70, at 6, col. 2. See also, National Transportation Act, 1987, supra note 4, at Part II, § 79 (1).} However, the Act requires that carriers have domestic tariffs (i.e., fares, rates, charges) available for inspection by any interested person.\footnote{National Transportation Act, 1987, supra note 4, at Part II, § 83(1)(2)(3).} Increases in fares on so-called "monopoly" air routes

Questions of law or jurisdiction may be appealed to Federal Court. FREEDOM TO MOVE, supra note 68 at 11, col. 2.
TABLE 2
SOUTHERN TRANSCONTINENTAL

<table>
<thead>
<tr>
<th>CITY PAIR</th>
<th>1983 FLIGHTS</th>
<th>1988 FLIGHTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Toronto To:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Vancouver</td>
<td>8</td>
<td>21</td>
</tr>
<tr>
<td>Calgary</td>
<td>10</td>
<td>16</td>
</tr>
<tr>
<td>Halifax</td>
<td>8</td>
<td>14</td>
</tr>
<tr>
<td>Edmonton</td>
<td>7</td>
<td>10</td>
</tr>
<tr>
<td>Winnipeg</td>
<td>10</td>
<td>15</td>
</tr>
</tbody>
</table>

REGIONAL ROUTES

<table>
<thead>
<tr>
<th>CITY PAIR</th>
<th>1983 FLIGHTS</th>
<th>1988 FLIGHTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vancouver-Victoria</td>
<td>24</td>
<td>86</td>
</tr>
<tr>
<td>Halifax-Moncton</td>
<td>2</td>
<td>10</td>
</tr>
<tr>
<td>London-Toronto</td>
<td>8</td>
<td>21</td>
</tr>
<tr>
<td>St. John's-Halifax</td>
<td>7</td>
<td>15</td>
</tr>
<tr>
<td>Quebec-Montreal</td>
<td>11</td>
<td>29</td>
</tr>
<tr>
<td>Toronto-Montreal</td>
<td>30</td>
<td>50</td>
</tr>
</tbody>
</table>


TABLE 3
THE NORTH

<table>
<thead>
<tr>
<th>CITY PAIR</th>
<th>1983 FLIGHTS</th>
<th>1988 FLIGHTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Whitehorse-Vancouver</td>
<td>1</td>
<td>3</td>
</tr>
<tr>
<td>Yellowknife-Edmonton</td>
<td>2</td>
<td>6</td>
</tr>
<tr>
<td>Resolute Bay-Yellowknife</td>
<td>2/WK</td>
<td>8/WK</td>
</tr>
</tbody>
</table>


can be appealed to the NTA, and if unreasonable, can be disallowed or reduced.\textsuperscript{126} Carriers in the North may be subject to review of both basic fare levels and increases, but only upon complaint.\textsuperscript{127} In sum, fair increases in the southern market will not be subject to review.

The Northern and remote Canadian communities have specialized transportation needs. Transportation is their lifeline and many communities depend upon the service of a relatively few transportation providers.\textsuperscript{128} In certain remote areas, air transportation is the only mode of travel. The Transportation Act, 1987 recognized these needs and made

\textsuperscript{126} Id. at Part II § 80(1).
\textsuperscript{127} Id. at Part II § 80(2).
\textsuperscript{128} FREEDOM TO MOVE, supra note 70, at 9, col. 1.
special provisions for northern air transportation. Although the removal of the restrictive economic controls is intended to increase domestic competition, the North will continue to be regulated. Carriers wanting to provide new air service in the North must meet the "fit, willing and able" test. However, this test is accompanied by a "reverse onus test" in which the burden is on the interested community or party to voice its concern and show it would significantly decrease the existing level of service or jeopardize the continuation of essential air service by the granting of a new license. The NTA will also continue to impose license conditions with respect to the type of service offered, the routes and destinations served, the size of the aircraft and exit from northern routes.

Mergers or acquisitions of any Canadian federally regulated mode of transport (e.g. airline) which has assets or annual income of $10 million or greater are subject to review by the Agency. However, the proposed acquisition must represent 10% or more of the issued and outstanding voting shares of the airline or mode of transportation. Notice of such a merger or acquisition must be given to the Agency, but review will only be granted upon objection to the proposed merger or acquisition. The Agency must then examine whether the proposed merger or acquisition would be adverse to the public interest as defined by the NTA.

Finally, the NTA provides for financial assistance to those domestic services designated by the Minister of Transport to be essential as of January 1, 1988. The legislation is unclear as to who determines which level of service is essential. The term essential air service is not defined in the legislation, nor are the terms and conditions of assistance.

3. IMPACT OF ECONOMIC REGULATORY REFORM ON THE CANADIAN AIRLINE INDUSTRY.

Unlike the United States experience with deregulation, there have been virtually no new entrants into the Canadian carrier market. However, two mergers and acquisitions have occurred in Canada. Prior to deregulation in Canada, the two transcontinental carriers, Air Canada and the then-CP Air, the four major regional carriers and Wardair (which was a

129. National Transportation Act, 1987, supra note 4 at Part II, § 67. The north is referred to as a "designated area" (See Table 4).
130. Id. at Part II, § 72(2).
131. FREEDOM TO MOVE, supra note 70, at 9, col. 2.
133. Id. at Part VII, § 253(3).
134. Id. at Part VII, §§ 252(1)(2), 255, 256.
136. Id. at Part I, § 85.
137. Phillips, supra note 1 at 63.
charter airline) were the main providers of air transport. Competition between the carrier levels was minimal. Since deregulation, the Canadian air transport industry has seen the rise of two large carrier families (Air Canada and Canadian Airlines International) operating fully competitive coast-to-coast networks. This duopoly of carriers came about as the regionals merged with or were acquired by these two large carriers. One of the regionals, Pacific Western Airlines (PWA) increased its share of the market by acquiring smaller regional carriers, third level carriers, and by signing cooperative marketing agreements to offer coordinated feed services and schedules. CP Air acquired several regional carriers and a commuter airline and was renamed Canadian Pacific Airlines, Ltd. (CPAL). PWA acquired 100% of CPAL for $300 million and renamed the carrier Canadian Airlines International. Canadian Airlines International also established a new regional airline providing fleet services to southern Ontario, particularly Toronto. Canadian Airlines International affiliates include TimeAir, CalmAir, AirAtlantic, Inter-Canadian and Ontario Express. Air Canada's affiliates include AirOntario, AirToronto, AirNova, AirAlliance, NWTAir and AirBC. The alliance with turbo prop carriers by both Canadian Airlines International and Air Canada provides local commuters with access to the major carriers and routes as well as joint fares. Thus in Canada, carriers have increased their market shares through mergers and acquisitions, rather than through the deep discount fares experienced by U.S. carriers at the onset of deregulation.

Canadian deregulation was intended to subject Canadian carriers to greater competition and market forces. Paradoxically the result of deregulation is less competition. By 1988, Air Canada and Canadian Airlines International plus Wardair handled about 95% of scheduled passengers and earned 97% of the operating revenues (See Table 6). In January of 1989, Canadian Airlines bought out the last competitor to the Big Two, Wardair, a charter carrier which had acquired some commuter and international routes. Wardair did not emerge as a serious competitor until 1996 when it launched its regularly scheduled domestic service. Wardair initiated dramatic fare wars, however, the Big Two were determined to undercut Wardair. The intense competition, continued operating losses,

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139. See generally, Phillips, supra note 1 at 64-65. PWA acquired 100% of CPAL in 1986.
140. 1988 ANNUAL REVIEW, supra note 138 at 53.
141. Id. at 52.
142. Phillips, supra note 1 at 66.
143. Id.
144. 1988 ANNUAL REVIEW, supra note 138 at 55.
### TABLE 4

**THE AIR CANADA FAMILY**

<table>
<thead>
<tr>
<th>CARRIER</th>
<th>NETWORK</th>
<th>FLEET</th>
</tr>
</thead>
<tbody>
<tr>
<td>Air Canada</td>
<td>points in all 10 provinces; the U.S., the Caribbean, Europe and Southeast Asia.</td>
<td>108 jets</td>
</tr>
<tr>
<td>Air Nova</td>
<td>points in Newfoundland, Nova Scotia; Prince Edward Island and New Brunswick; Montreal, Quebec City; Ottawa and Boston.</td>
<td>3 jets; 7 non-jets</td>
</tr>
<tr>
<td>(49% owned)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Air Alliance</td>
<td>points in Quebec; Ottawa and Boston.</td>
<td>3 non-jets</td>
</tr>
<tr>
<td>(75% owned)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Air Toronto</td>
<td>points in Ontario; Winnipeg, Montreal, Hartford, Minneapolis, Cleveland and Detroit.</td>
<td>1 jet; 42 non-jets</td>
</tr>
<tr>
<td>75% owned</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Air Toronto</td>
<td>service between Toronto and 7 northeast U.S. cities</td>
<td>7 non-jets</td>
</tr>
<tr>
<td>(commercial agreement)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>AirBC</td>
<td>points in B.C. and Alberta; Whitehorse and Seattle.</td>
<td>3 jets; 19 non-jets</td>
</tr>
<tr>
<td>(85% owned)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>NWT Air</td>
<td>points in the Northwest Territories; Edmonton and Winnipeg.</td>
<td>1 jet; 7 non-jets</td>
</tr>
<tr>
<td>(90% owned)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Source: NATIONAL TRANSPORT AGENCY CANADA, ANNUAL REVIEW 38 (1988) at 52.*

### TABLE 5

**THE CANADIAN AIRLINES INTERNATIONAL FAMILY**

<table>
<thead>
<tr>
<th>CARRIER</th>
<th>NETWORK</th>
<th>FLEET</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canadian Airlines</td>
<td>points in all 10 provinces and both territories; the U.S., Europe, Central and South America, the South Pacific and Asia.</td>
<td>84 jets; 3 non-jets</td>
</tr>
<tr>
<td>International (PWA Corp.)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Air Atlantic</td>
<td>points in Newfoundland, Nova Scotia, New Brunswick and Prince Edward Island; Montreal, Ottawa and Boston.</td>
<td>7 non-jets</td>
</tr>
<tr>
<td>(45% owned)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inter-Canadian</td>
<td>points in Quebec and New Brunswick; Charlottetown, Ottawa and Toronto.</td>
<td>5 jets; 11 non-jets</td>
</tr>
<tr>
<td>(35% owned)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ontario Express</td>
<td>points in Ontario; Brandon, Winnipeg and Pittsburgh.</td>
<td>14 non-jets</td>
</tr>
<tr>
<td>(49% owned)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Calm Air</td>
<td>points in Manitoba and the Northwest Territories.</td>
<td>15 non-jets</td>
</tr>
<tr>
<td>(45% owned)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Time Air</td>
<td>points in B.C., Alberta and Saskatchewan; Winnipeg and Minneapolis.</td>
<td>3 jets; 29 non-jets</td>
</tr>
<tr>
<td>(46% owned)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Source: NATIONAL TRANSPORT AGENCY CANADA, ANNUAL REVIEW 38 (1988) at 52.*
<table>
<thead>
<tr>
<th>Carrier</th>
<th>Domestic South</th>
<th>Domestic North</th>
<th>Transborder</th>
<th>International</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Air Canada</td>
<td>290,993</td>
<td>2.8%</td>
<td>1,000</td>
<td>0.0%</td>
<td>36,591</td>
</tr>
<tr>
<td>Affiliates</td>
<td>104,985</td>
<td>53.7%</td>
<td>22,603</td>
<td>72.8%</td>
<td>6,796</td>
</tr>
<tr>
<td>Total</td>
<td>395,978</td>
<td>12.7%</td>
<td>23,603</td>
<td>67.6%</td>
<td>43,387</td>
</tr>
<tr>
<td>Canadian</td>
<td>279,088</td>
<td>(7.8)%</td>
<td>33,160</td>
<td>(17.8)%</td>
<td>6,569</td>
</tr>
<tr>
<td>Affiliates</td>
<td>120,546</td>
<td>110.5%</td>
<td>30,820</td>
<td>94.8%</td>
<td>3,365</td>
</tr>
<tr>
<td>Total</td>
<td>399,634</td>
<td>11.1%</td>
<td>63,980</td>
<td>14.0%</td>
<td>9,934</td>
</tr>
<tr>
<td>Wardiar</td>
<td>53,445</td>
<td>189.4%</td>
<td>0</td>
<td>NA</td>
<td>471</td>
</tr>
<tr>
<td>Independents</td>
<td>43,919</td>
<td>(38.8)%</td>
<td>31,093</td>
<td>2.5%</td>
<td>2,475</td>
</tr>
<tr>
<td>Total</td>
<td>892,976</td>
<td>11.4%</td>
<td>118,676</td>
<td>18.0%</td>
<td>56,267</td>
</tr>
</tbody>
</table>

Note: () indicates negative figures
and ongoing equipment costs prompted Maxwell Ward, chairman of Wardair, to sell out.145

<table>
<thead>
<tr>
<th>PROVINCE</th>
<th>ABANDON</th>
<th>RETAIN (miles)</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>British Columbia</td>
<td>27</td>
<td>100</td>
<td>127</td>
</tr>
<tr>
<td>Alberta</td>
<td>15</td>
<td>0</td>
<td>15</td>
</tr>
<tr>
<td>Saskatchewan</td>
<td>48</td>
<td>0</td>
<td>48</td>
</tr>
<tr>
<td>Manitoba</td>
<td>71</td>
<td>0</td>
<td>71</td>
</tr>
<tr>
<td>Ontario</td>
<td>267</td>
<td>0</td>
<td>267</td>
</tr>
<tr>
<td>Quebec</td>
<td>38</td>
<td>69</td>
<td>107</td>
</tr>
<tr>
<td>New Brunswick</td>
<td>10</td>
<td>0</td>
<td>10</td>
</tr>
<tr>
<td>Prince Edward Island</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Nova Scotia</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Newfoundland</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td><strong>Total Miles</strong></td>
<td><strong>476</strong></td>
<td><strong>169</strong></td>
<td><strong>645</strong></td>
</tr>
<tr>
<td>(%)</td>
<td>(73.8%)</td>
<td>(26.2%)</td>
<td>(100.0%)</td>
</tr>
</tbody>
</table>

The ranks of independent carriers grew in 1988. Aside from Wardair, the largest are City Express and First Air.146 In the international charter markets, the established carriers (Nationair, Worldways, Air Transit and First Air) were joined by the new carriers147 of Vacationair, Odyssey International, Air 2000, Ports of Call, Minerve Canada and Holidaire.148 Also, the shift to hub-and-spoke route systems opened up opportunities for smaller commuter airlines to serve as feeder airlines for the megacarriers.149

With respect to air fares, the major Canadian airlines apparently have learned from observing their U.S. counterparts. Aside from the fare wars with Wardair, the major Canadian carriers did not have to offer the deep discount fares to increase their market share.150 Over all, discount fares in Canada are limited. Although there has been an increase in the number of passengers traveling on discount tickets, seating capacity is limited and various travel restrictions apply. The average level of fares has not declined, although the variety of fares has increased. The Na-

146. 1988 ANNUAL REVIEW, supra note 138, at 54. First Air upgraded its service to northern Canada during 1988 and continued to service Mirabel and Boston out of Ottawa. First Air also operated flights (passengers and cargo) to Florida, the Caribbean, Mexico and the Arctic. Id. City Express expanded its Toronto-Ottawa-Montreal route network in 1988. It also added a second U.S. destination. Id.
147. Id.
148. Id.
149. Id.
150. Phillips, supra note 1 at 99.
tional Transport Agency's 1988 annual review indicated that business and economy fares increased on most domestic routes. More and deeper discounts were available, however, on the highly competitive long-haul transcontinental routes such as Toronto-Vancouver, Calgary-Toronto, Edmonton-Toronto, Montreal-Vancouver and Ottawa-Vancouver.151

Deregulation has also brought about changes in the Canadian route structure system. Since Canadian Airlines International and Air Canada have entered into alliances and joint feed and scheduling agreements with many of the regional and local commuters, carrier route patterns have evolved into the hub-and-spoke systems. The traveling passenger is offered more destinations, ticket and baggage integration, and access to frequent flyer programs. The carriers benefit by being able to keep the passenger on line until final destination,152 however, there are disadvantages to the passenger. Fewer nonstop long-distance flights mean more connections, higher load factors and more delays. Jet service to low-traffic-density communities has been replaced by turboprop carriers which share the major carriers designator code.153

As have their American counterparts, Canadian airlines have cut their labor costs in order to compete more effectively in the deregulated market. All carriers have relatively stable overhead costs such as fuel, interest and liability insurance thus, labor costs become the target for cutbacks through layoffs, paycuts, greater use of part-time employees, more flexible work rules and profit sharing plans.154

The newly deregulated Canadian airline industry theoretically relies on competition and market forces to achieve an economic, efficient and adequate air transport system in Canada.155 In the U.S., eight megacarriers have emerged, controlling 94% of the passenger business, with one or two major carriers dominating gate and landing and takeoff slots at each of the major hub and spokes. Canada's two large carrier families dominate about 97% of its market. It is now important for Canada to address the emerging forms of anticompetitive conduct. Anticompetitive conduct results from mergers which limit competition, create opportunities for conspiracies of price-fixing and market sharing, predatory pricing or scheduling and manipulating the costs of competitors. Potential agreements by major carriers such as Air Canada and Canadian Airlines International regarding airfares, markets to be served and schedules, inhibit local carriers from entering the larger markets and preclude potential new

151. 1988 ANNUAL REVIEW, supra note 138 at 60-61.
152. Phillips, supra note 1 at 99.
153. id.
154. id. at 100.
155. id.
entrants. Hub domination by major carriers also affects competitive
to gates and landing and takeoff slots. Finally, anticompetitive
practices potentially surface through travel agents and computerized res-
ervation systems which generally favor the larger and established
carriers.

The NTA, 1987, frowns upon anticompetitive conduct in its declara-
tion of policy by stating that "... competition and market forces are, 
whenever possible, the prime agents in providing viable and effective 
transportation services..."157 The agency has the power to make ad-
ministrative decisions and order compliance with the Act, however, the 
sanctions for noncompliance are vague.158

The New Competition-Act159 in Canada, although not formulated 
specifically for the Canadian airline industry, penalizes criminal conduct 
such as price fixing and market sharing conspiracies. Whether the Com-
petition Act provides adequate protection against anticompetitive conduct 
by air carriers is yet to be determined. The Competition Act may be diffi-
cult to enforce with respect to the Canadian Airline Industry due to the 
vagueness of the statutory criteria involving the standards of proof and 
available defenses. The determination of anticompetitive conduct most 
likely will be left to the discretion of the courts and the Competition Tribu-
nal (the governing body established by the Competition Act) on a case-
by-case basis.160

The question arises as to whether the domination of the market by 
the two major carriers, Air Canada and Canadian Airlines International, is 
anticompetitive or in Canada's best interest. Maxwell Ward regretted 
having his airline (Wardair) swallowed up by Canadian Airlines Interna-
tional. However, Ward maintained that the Canadian airline industry must 
develop huge airlines that are large enough to compete with major inter-
national carriers including American Airlines (the largest U.S. carrier) and

156. Id.
158. See generally, Part I §§ 34-45. "Any decision or order of the Agency may be made on 
order of the Federal Court or any superior court and is enforceable in the same manner as an 
order thereof" Id. at § 42. But CF, Part II, of the Act dealing specifically with air transportation 
does provide punishment for willful contravention of licensing procedures. Punishment ranges 
from fines not exceeding $5,000 or imprisonment for a term not exceeding one year or both for 
individuals; corporations may be liable for fines of up to $25,000. Id. at 103, 104, 105.
159. Competition Act, [am. 1968, c. 26] [hereinafter Competition Act].
160. Phillips, supra note 1 at 88. The Competition Act provides for the establishment of a 
Competition Tribunal. This body will hear applications and issue orders with respect to Part VII of 
the NTA, 1987, dealing with acquisitions of Canadian transportation undertakings (i.e., any busi-
ness engaged in transportation under the legislative authority of Parliament). Id. at 88. See also, 
NTA, 1987, supra note 4 at Part VII § 251(1). Reviewable matters will include refusal to deal, 
exclusive dealing, market restriction, tied selling, abuse of dominant position, delivered pricing, 
specifications agreements and merger. Phillips, supra note 1 at 88.
British Airways, even if this means the smaller airlines will not be able to survive.\textsuperscript{161} Ward is of the opinion that domination of the Canadian market by the Big Two is positive for the industry. Canada has a problem sustaining smaller airlines. With a new 747 jumbo jet costing $125 million, "...there is only room for the largest."\textsuperscript{162}

Maxwell Ward's opinion is shared by others in the industry. August E. Pokotylo, Director General, Air Policy and Programs, Transport Canada, maintains that the restructuring of Canada's airline industry is emerging with positive signs.\textsuperscript{163} Despite increased concentration, there is more competition on a route-to-route basis between existing airlines. In sum, Pokotylo views airline management as innovative in offering discounted yet quality service to Canadians.\textsuperscript{164} Furthermore, as one member of Transport Canada expressed, Canada's airline industry does not function in a vacuum and must still compete on an international level.\textsuperscript{165}

Added to the list of potential anticompetitive practices is the phenomenon of "globalization." This term refers to mergers and agreements between foreign carriers.\textsuperscript{166} Globalization may have begun in December of 1987 when United Airlines announced a marketing agreement with British Airways.\textsuperscript{167} Scandinavian Airline System (SAS) has a 10% stake in Continental.\textsuperscript{168} Swissair and Singapore Airlines each own 5% of Delta. More recently the Netherland's KLM contributed $400 million to Alfred Checchi's buyout of NWA.\textsuperscript{169} With the advent of the European Economic Community in 1992, the arena of possible merger between foreign carriers widens.\textsuperscript{170}

If the skies should belong only to the megacarriers, what will protect the passengers and the shippers from potential anticompetitive effects of deregulation? Not all would agree with Maxwell Ward that domination of the Canadian market by the Big Two is desirable.\textsuperscript{171} While it may be more feasible for Canada to support only a duopoly, this system, without any type of regulation, invites potential abuse. Under deregulation, competitive market forces were predicted to effectively discipline the airline

\textsuperscript{161} \textit{MACLEAN'S}, January 30, 1989 at 35, col. 2.
\textsuperscript{162} \textit{id.}
\textsuperscript{163} \textit{14TH ANNUAL FAA CONFERENCE, supra note 5, at 113.}
\textsuperscript{164} \textit{id. at 113-14.}
\textsuperscript{165} Interview with Vale'rie Dufour, Director, Domestic Air Policy, Transport Canada, in Ottawa, Canada (Sept. 15, 1989) [hereinafter Interview].
\textsuperscript{166} \textit{14TH ANNUAL FAA CONFERENCE, supra note 5, at 21.}
\textsuperscript{167} \textit{id.}
\textsuperscript{168} \textit{U.S. NEWS & WORLD REPORT, Sept. 11, 1989, at 54, col. 1.}
\textsuperscript{169} \textit{id. at 55, col. 1.}
\textsuperscript{171} See generally, Phillips, \textit{supra note 1, at 101-02.}
industry. Without effective competition, market forces cannot operate as intended by the proponents of deregulation.

The Canadian Federal Government implemented economic regulatory reform of its airline industry closely following the model set by the United States. However, Canada still retains the National Transportation Agency to provide minimal regulation. It has been suggested that the Federal Government could have maintained the liberalization policy and still retained independent regulatory discretion. Like the CAB, the CTC, rather than being abolished, could have used its expertise to combat the potential anticompetitive practices using the existing regulatory framework.172

It is feared that the general market competition laws are not suitable to an essential infrastructure industry which is excessively concentrated.173 A highly concentrated airline industry may create uneconomic, inefficient, anti-competitive, expensive and inadequate transportation for Canadians.

One effective way of dealing with the anti-competitive effects of airline deregulation may be through the Competition Tribunal. This tribunal was established by the New Competition Act as a governing body authorized to hear applications and issue orders with respect to anti-competitive conduct such as market restrictions, abuse of dominant positions, exclusive dealing, and special agreements on mergers.174 The Tribunal's approach is civil rather than one based upon criminal law standards. If assisted by lay experts knowledgeable in the area of effective but fair competition, the Tribunal may be an appropriate mechanism to deal with the anti-competitive effects of airline deregulation. The Tribunal was recently called upon to determine whether the Gemini Merger, Canada's largest computer reservation system (CRS), was anticompetitive. (Air Canada and Canadian Airlines International merged their travel agency reservation systems under the Gemini Group Distributed Information Systems, Inc.). The Gemini Merger was approved. However, Transport Canada has been instructed to develop a code of conduct.175 Finally, if the courts are called upon to determine anti-competitive conduct by carriers, it is hoped that clearer, consistent guidelines will be developed to interpret these statutory tests as outlined in the Competition Act.

173. Id.
174. Id. at 88.
175. Interview, supra note 165.
III. THE NEW RAIL REGIME IN CANADA

A. DEREGULATION COMES TO CANADIAN RAILWAYS

Railroads in Canada have operated on a different basis from those south of the 49th parallel. The United States still has no true transcontinental railway (Robert R. Young used to argue that a hog could cross Chicago without changing trains — but you can’t), while Canada has two — the Canadian National [CN] and the Canadian Pacific [CP].

Moreover, these two railroads are essentially the only important railways in Canada. Canadian National Railways is a Crown Corporation — owned by the government, as was Air Canada and as is the Canadian Broadcasting Corporation. CN & CP at one time also competed in hotels, telecommunication and air carriers services.

Thus, deregulation would seem to have less appeal in a country where the market is already dominated by a duopoly. Nonetheless, the same National Transportation Act that brought deregulation to the skies and highways applies to Canada’s two transcontinentals and a few provincial railways as well.

Both Canada and the United States developed their framework of railroads under regulation by their Federal governments. The Constitution Act of 1867 gave the Federal parliament the right to legislate for a “work for the general good of Canada,” and development of the railroads has taken place under Federal regulation. The intent of regulation was to promote competition between the privately-owned CP and the publicly-owned CN.

The railway system in Canada operates in eight of the ten provinces, having just exited the island provinces of Prince Edward Island and Newfoundland in 1988-89. Canada is also one of the few countries in the world still adding to its railway network, building extensions to serve economic activity in the hinterland.

Both the United States and Canada have maintained continent-wide railroad systems with an extensive private component. In the United States, private ownership is the rule, while in Canada the privately owned Canadian Pacific is one of the largest railroads in the world. Both U.S.

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179. C. Phillips, Railways in Canada, Transport Canada Surface Administration, Railway and Grain Transportation Report at 2 (March 1986). The report mentions that B.C. Rail has just completed the first modern electrified line in Canada, the 69 mile Tumbler Ridge branch, and that CP is engaged in a $600 million project for tunnelling and line relocation in the Rockies.
180. Id. See also Ellison, supra note 176.
and Canadian railroads face competition from motor carriers, although long-distance trucking is less significant to Canada than to the United States. Both country's railroads have lost the bulk of their passenger business to airways and, to a lesser extent, to buses. 181 Both nations find that their rail systems are overbuilt for today's traffic needs.

Between 1976 and 1980 the United States substantially demolished the statutory system of economic regulation of trucking, buses, airlines and railroads. 182 Within the United States, rail passenger service was spun off to Amtrak in 1971; 183 commuter rail service was turned over to the states a decade later. 184 Unprofitable Eastern railways were lumped in together and turned over to Conrail in 1976, a federal entity. Conrail was later returned to the private sector.

The key point of rail deregulation in the United States was the Staggers Rail Act of 1980. 185 The Staggers Act was based upon a finding by Congress that modernization of regulation was essential, 186 and an intention to rely upon competition to the greatest extent possible. 187

Under Staggers, entry to the rail industry was relaxed, which facilitated the start-up of short line railroads. 188 Similarly, abandonment of rail lines was accelerated, and made much easier for railroads to accomplish. 189 The Staggers Act provided for less supervision of ratemaking, with no maximum rates unless the carrier has market dominance, and a great deal of ratemaking freedom. 190 Rates themselves may be virtually irrelevant, as the Staggers Act also allowed railroads and large shippers to contract for the shipment of goods without any recourse to regulatory approval. 191

Reliance on competition in the United States meant turning to intermodal competition, as few new railroads were coming onto the scene. In fact, railroads have now become even more of an oligopoly under de-

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187. Id.
188. The public convenience and necessity need only permit (not require) construction or acquisition and operation of a rail line. 49 U.S.C. § 10901 (d),(e) (1980).
189. Abandonment is now limited to a 330-day process. 49 U.S.C. § 10904 (1980).
regulation with seven major railroad systems dominating the U.S. industry ten years after the passage of Staggers, four west of the Mississippi, and three east.\textsuperscript{192} Canada, with two major railroad systems, nevertheless saw the need to meet the competition of the Yankee railroads, which were competing for coast-to-coast traffic with the CN and the CP. As with airlines, the Canadian government chose to follow the U.S. example and substantially deregulate the rails.

Passenger service had already been spun off from CN and CP by the establishment of VIA Rail Canada, Inc., a Crown Corporation, to take over intercity passenger service in a similar fashion to the establishment of Amtrak in the United States.\textsuperscript{193} Commuter service in the Toronto and Montreal areas had been lifted from the railways and placed under the operating authorities of Ontario and Quebec, respectively.\textsuperscript{194} The repeal of the Crow’s Nest Pass rates, which mandated uneconomic rates for movement of western grain, brought on a more realistic rate base for agricultural products and ended a cross-subsidization of freight traffic.\textsuperscript{195} Now it was Parliament’s turn to examine the regulation of the freight railroad industry in Canada.

\textbf{B. THE NATIONAL TRANSPORTATION ACT}

The National Transportation Act, of 1987 contains the most far-reaching changes in the regulation of railways since Confederation. Its aim is to strengthen the railway system by allowing it to better compete with other modes, and to allow the railways to modernize, even though such modernization might deprive many communities and shippers of freight service. In many ways, the partial deregulation experience in the U.S. by the Staggers Act is replicated north of the border.

Many of the Canadian deregulation features found in the National Transportation Act were found originally in the Staggers Rail Act in the U.S. For example, it is now easier for Canadian and U.S. Railroads to enter and leave markets. True, few new railroads are being built either in the U.S. or Canada, but the new law makes it easier for a Canadian short line to obtain Letters Patent to take over and operate an existing line that a major railroad no longer wants. (The Staggers Act makes this process easier for U.S. railroads.) With abandonments, the burden of proof has been shifted to shippers and passengers to prove that the line is still re-

\begin{itemize}
\item 192. The seven are: Santa Fe, Southern Pacific, Union Pacific, Conrail, Norfolk Southern, CSX and Burlington Northern.
\item 195. Ellison, \textit{The Formation and Dissolution of the Canadian Rail Cartel}, 15 TRANSP. L.J. 175, 197-201 (1986).
\end{itemize}
quired for the needs of the public.\textsuperscript{196}

The agency which has replaced the Canadian Transport Commission, the new NTA, is directed by the statute that states traditional regulation of railroads is to be used as a last resort.\textsuperscript{197} Such time-honored practices as collective ratemaking are no longer allowed, and railroads are allowed to enter into contracts with their shippers. Currently in the United States most freight moves by contract rather than tariff rates, and a shift to "confidential contracts" (as they are called in Canada) is occurring in Canada as well.\textsuperscript{198}

The philosophy of the National Transportation Act is found in the government's White Paper, "Freedom to Move." Following a study by the Canadian Transport Commission on railway problems, it endorsed the need for Canadian shippers to have confidential contracts, but moved away from the then-current policy of allowing the two railroads to exchange information on costs and to file joint and common rates.\textsuperscript{199} In an informative article published in the \textit{Transportation Law Journal}, Canadian economist Anthony P. Ellison writes:

> By removing the exchange of cost information and the setting of common rates, the ... National Transportation Act withdraws the legislative protection afforded the fifty year old rail cartel. The (National Transportation) Agency, with its proposed direction over running rights, joint-track usage and joint rates, empowered to facilitate rather than limit intramodal competition.\textsuperscript{200}

The Act's Section 3 clarifies Canada's National Transportation Policy, which includes safety as a key objective, but then relies upon competition and market forces as the prime agents in providing a transportation system. Competition is regarded as desirable both between modes and within each mode. Carriers are to set rates which do not discourage movement of commodities nor the development of primary and secondary industry or export trade.\textsuperscript{201}

The Act creates a National Transportation Agency, of not more than nine permanent members plus up to six temporary members, appointed by the Prime Minister and the Cabinet. The Governor in Council may revise or annul decisions of the Agency. The NTA requires a complaint or an application to trigger its jurisdiction except for matters relating to safety

\textsuperscript{197} National Transportation Act, 49 U.S.C. § 3 (1987).
\textsuperscript{198} Confidential contracts are allowed by Section 120 of the NTA. The parties may agree to a contract concerning rates, level of services, equipment and other conditions. Neither party may apply for final offer arbitration nor public interest appeal of that contract unless the other party concurs.
\textsuperscript{200} Ellison, supra note 195, at 216.
\textsuperscript{201} National Transportation Act, 49 U.S.C. § 3 (1987).
or licensing. In its independence from Cabinet, the NTA has some features of the Interstate Commerce Commission in the United States.

C. BRANCHLINE ABANDONMENTS

Abandonment proceedings have been streamlined: if a railroad applies to abandon a branchline and nobody objects, the railway is automatically permitted to close the line. If a party protests the application, then the NTA must determine if the line is profitable or has some prospect of becoming so. The NTA also has power to establish short lines or to subsidize operations over the branch for years. There is a cap on abandonments, as no railroad may abandon more than 4% of its system during each of the first five years of the Act. This 4% limit was at first objected to by the railways, but proposals for abandonment have in no instance come close to 4% of the total of either of the two transcontinental systems, nor of the smaller railways.

The rail abandonment process before the NTA works like this:

- A railway company must give the National Transportation Agency (the Agency) and the public in areas served by the rail line a Notice of Intent to apply for abandonment.
- Ninety days after the Notice of Intent the railway may apply to the Agency for abandonment authority.
- Within sixty days of the application, any party may oppose abandonment in writing to the Agency.
- If the application is not opposed within the sixty days, the Agency must order abandonment.
- If the application is opposed, the Agency investigates the present and future economics (costs and revenues) of the line.
- The Agency must decide within six months of the application whether or not to allow abandonment of the line, according to the following provisions in the National Transportation Act:
  (a) if the line is deemed to be uneconomic, with no reasonable probability of becoming economic, the Agency must order abandonment;
  (b) if the line is deemed to be economic (now or in the future), but is not required in the public interest, the Agency must order abandonment;
  (c) if the line is found to be uneconomic, but is deemed to have a reasonable probability of becoming economic and is required in the public interest, the Agency must order the line retained and reconsider the application within three years;
  (d) if the line is found to be economic (now and in the future) and required in the public interest, the Agency must dismiss the application for abandonment.

Public interest considerations are examined only if the line will be or has a reasonable probability of becoming economic in the future.

The Agency may hold public hearings if there is opposition to the application and it considers hearings necessary.

There is not opportunity for Ministerial intervention in the abandonment process once an application has been received.204

There are several limitations to the rail abandonment process:

- A railway company cannot abandon more than 4% of its total route mileage in any of the five years including 1992.
- The existence of passenger service on a line does not prevent the line from being ordered abandoned (for freight traffic).
- The effective date of an abandonment order would be set so that VIA Rail would have six months to decide if it wants the rail line for its passenger services and another six months to negotiate the terms of the line’s transfer.
- VIA Rail may abandon the rail line if subsequently it is no longer needed for passenger rail service.
- The Agency can order a line retained for as long a period of time as a province, municipality, or other interested person pays the actual losses of the line.205
- Once the agency has announced its decision, there are three mechanisms for appeal including rehearing by the Agency, appeal to the Federal Court of Canada, or appeal to the Governor in Council for a delay of up to five years if there are inadequate alternate facilities in the area.206

The largest abandonment of 1988 was concluded outside of the NTA’s abandonment processes. The narrow-gauge Newfoundland Railway had been transferred to the central government of Canada when that province entered Confederation in 1949. Under a deal worked out in June 1988 between the Newfoundland and federal governments, the Canadian National (the line’s operator) was allowed to abandon the entire railway. Included in the agreement was over $800 million in federal funding to improve highway and other transport facilities in the province (plus labor protection provisions for displaced railway employees, who will not be required to leave Newfoundland to obtain railway work elsewhere. Most are now engaged in the demolition of the railway).207 Under new legislation, once a railroad line is abandoned, disposition or reinstatement becomes a provincial responsibility. As the wreckers were tearing up the 42-inch gauge track, the province stepped in to save a few segments for tourist and historical purposes. Because an isolated railway is now a pro-

204. This outline is adapted from “Railway Branch Lines”, a memorandum Transport Canada, Surface Administration, Railway & Grain Transportation of 1989. The pertinent parts of the statute can be found in National Transportation Act 1989, §§ 157-177.
205. Id. at p. 2.
206. Id. The relevant sections are National Transportation Act 1987, § 41, § 45, and § 165(2).
province, and not a federal responsibility, Newfoundland is now in the railroad business, and is responsible for the upkeep of the remaining lines.

During 1989, the Canadian National also abandoned what little track-age remained on Prince Edward Island under the provisions of the National Transportation Act. The same year, Canadian Pacific reorganized its entire system in the Maritimes (which also passes through the State of Maine) as the Canadian Atlantic Railway. Some observers suggested that such a move was made to isolate the costs involved in operating in the Atlantic provinces as a separate profit centre, which could be abandoned if losses prove to be too onerous. This is apparently why Canadian National had set up its Newfoundland operations as Terra Transport in the years preceding abandonment.208

D. COMPETITIVE ACCESS

Most substantive changes under the Transportation Act of 1987 parallel the changes in the Staggers Act for U.S. railroads. The uniquely Canadian difference is competitive access for captive shippers. We have seen that in most cases there are only two Canadian railroads and not much opportunity for intramodal competition. To remedy this defect the new law establishes an "interswitching limit" of 30 kilometers. That means that if a factory is located on a CN siding and there is an interchange with the CP some 25 kilometers away, the shipper can choose CP service; the CN must then allow the CP switcher to use its tracks and haul the car away.209

A shipper which is served by only one railway at either origin or destination may request that railway to establish a competitive line rate to or from the nearest interchange with a competing railroad. The shipper may designate the route for the competitive line rate (for example, a Manitoba shipper might request a rate to Emerson from the CN and via the Soo Line or Burlington Northern beyond). If a cost-effective continuous route from origin to destination is available entirely in Canada, the shipper is precluded from selecting a route involving a U.S. carrier. If a carrier fails to establish a competitive line rate upon request, then the National Transportation Agency will do so. Competitive line rates are not available for containers or trailers on flat cars, unless the intermodal shipment is export or import traffic moving to or from a port. The percentage of the distance to or from the interchange point cannot be more than 50% of the total rail mileage or 750 miles, whichever is greater. Unless agreed upon otherwise between the carrier or shipper, a competitive line rate will remain in

force for one year.\textsuperscript{210}

One interesting feature of this competitive access provision is that it is not limited to CN, CP or the local Canadian railways (British Columbia, Algoma Central, Ontario Northland, Quebec North Shore & Labrador). Five U.S. railroads (Burlington Northern, Norfolk Southern, CSX, Conrail and Delaware & Hudson) also operate into Canada. If they come within the interswitching limit, Canadian shippers can take advantage of U.S. competitors as well. It is also easier for U.S. railroads to obtain trackage rights over Canadian lines, and possibly abandon their own Canadian track.\textsuperscript{211} CN and CP are both vulnerable to competition by Burlington Northern, Conrail and other northern U.S. lines.

\textbf{E. PROSPECTS FOR RAIL FREIGHT Deregulation}

Both national railways have made it clear that they would like to slim down their systems (in Saskatchewan in May 1988, CN and CP exchanged trackage rights so that each could serve certain points near their systems and abandon redundant lines). The 4% cap will limit the size and scope of the abandonments. But a quick look at the rail map of Canada will show a pre-auto-age map crisscrossing the country without the consolidations and rationalization of lines that characterizes American railways.

In 1988, the National Transportation Agency issued 20 decisions relating to the abandonment of 645 rail lines, with the following results:

\begin{tabular}{|l|c|c|c|}
\hline
\textbf{Province} & \textbf{Abandon} & \textbf{Retain} & \textbf{Total} \\
\hline
British Columbia & 27 & 100 & 127 \\
Alberta & 15 & 0 & 15 \\
Saskatchewan & 48 & 0 & 48 \\
Manitoba & 71 & 0 & 71 \\
Ontario & 267 & 0 & 267 \\
Quebec & 38 & 69 & 107 \\
New Brunswick & 10 & 0 & 10 \\
Prince Edward Island & 0 & 0 & 0 \\
Nova Scotia & 0 & 0 & 0 \\
Newfoundland & 0 & 0 & 0 \\
\hline
\textbf{Total Miles} & 476 & 169 & 645 \\
\hline
\textbf{Total} & (73.8\%) & (26.2\%) & (100.0\%) \\
\hline
\end{tabular}

In 1989, the railways submitted 65 applications for abandonment of

\textsuperscript{210} National Transportation Act 1987 §§ 148-149. In addition to the freight railroads, Amtrak has running rights over CN and CP into Montreal, and operates joint services with VIA Rail into Toronto.

\textsuperscript{211} Data from Rail Planner Hoisak, Transport Canada, and included in Transport Canada report "Railroad Branch Lines". Surface Administration, Railway and Grain Transportation, August 17, 1989, p. 5.
1,306 miles. As a result, all lines on Prince Edward Island were abandoned. In addition, the Agency has twenty-three applications for 1,008 miles carried over from 1988, including reconsideration of previous decisions on lines that were ordered retained and were due for review in 1989. Short of amending the National Transportation Act, there is no mechanism for the Minister or Governor in Council to override the abandonment process currently set out in the NTA.212

During the last decade, large U.S. railroads have been turning over tremendous segments of routes to short lines or regional railroads. Locally operated with lower labor costs, and a friendly connection to the parent railroad, they are providing service to communities that might otherwise be bypassed. But such an easy turnover has not been possible in Canada. The Canada Labor Code provides that a successor employer inherits not only the same union, but the same collective bargaining agreement as it predecessor. This means that the same work-rules that hampered economical operation of the major railroad will still prevail. It may also mean that there might be no takers for these castoff lines.213

One important role for the NTA is the mediation of disputes between a shipper and a carrier or between two railways. A dispute may be referred to the NTA for mediation, which must be completed within thirty days. The mediation process is nonbinding and confidential, unless the parties agree to disclosure, and is available for all traffic except for grain movements and rail-water intermodal traffic.214

A shipper may apply to the Agency for final offer arbitration when dissatisfied with a railroad rate. Unlike traditional arbitration, the NTA is obliged merely to select from the final offer of the shipper and the final offer of the railroad. The Agency may pick the arbitrator if the parties cannot select one, and both parties share in the cost of arbitration, which must be completed with 90 days.215

Not only shippers, but the public in general may request the NTA to investigate any rate, act or omission of a carrier believed to be prejudicial to the public interest. The proceedings are informal, with no requirement for the appellant to prove a prima facie case, but in any case they must be completed within 120 days.216 In all matters affecting rail transportation,

212. See Thoms, How Long is the Short Line?, TRAINS, October 1986, p. 37; Thoms, Dereg Comes to Canada, TRAINS, Dec. 1988, p. 26. Presently there is only one spinoff short line in Canada, Alberta’s Central Western Railway. The CWR claims, as an intraprovincial railway, the federal government cannot legislate for it. Most observers believe that legislation is necessary to allow local contract negotiation and settlement for shortline railroads.


these procedural provisions may be suspended by the NTA if they have an unfavorable impact on the viability of Canadian railways.

Liberalization of railway regulation has not meant an end to rate regulation. The statute still requires that rates be compensatory (cover the variable cost of the particular movement of traffic).\(^{217}\) A noncompensatory rate must be disallowed unless it is proved by the carrier that the rate was not designed to be anti-competitive and does not, in fact, lessen competition.\(^{218}\) But a railroad need only publish tariffs on a request of a shipper.\(^{219}\) There are four types of rates allowed: agreed charges, published tariffs, confidential contracts and statutory rates.\(^{220}\) Published tariffs must not contain secret rebates, discounts or allowances. Even though confidential contracts are expected to move most bulk traffic in Canada by the end of the century, even these may be appealable if they are not compensatory.\(^{221}\)

The common carrier obligations traditional in Canada have been reiterated by the National Transportation Act: a railway must provide cars, deliver traffic offered to it and maintain facilities for receiving rates. It must interchange with connecting railroads and handle their cars. The NTA will police violation of common carrier obligations, but shippers and railways may agree to modify these obligations.\(^{222}\)

The NTA also may approve running rights and joint track usage, and determine whether railroads should build connections between the two of them. The Agency can also order one railroad to operate over the tracks of another. The aim of these new powers is to produce a more streamlined and efficient railway system for Canada.\(^{223}\)

\section*{F. Rail Passenger Service}

Until recently, Canada relied upon passenger trains connecting its large cities with virtually every hamlet of the Dominion. For the last dozen years, Canada has followed a regime similar to that of the United States: long-haul passenger service was made a responsibility on the central government (Amtrak in the U.S.; VIA Rail in Canada), while commuter service is the responsibility of state or provincial governments. (In Canada, extensive commuter operations in both Montreal and Toronto are supported by the Quebec and Ontario governments.) There is also a

\begin{itemize}
  \item \(^{217}\) id.
  \item \(^{218}\) id.
  \item \(^{219}\) National Transportation Act 1987 §§ 129-133.
  \item \(^{220}\) National Transportation Act 1987 § 120.
  \item \(^{221}\) National Transportation Act 1987 §§ 144-147.
  \item \(^{222}\) National Transportation Act 1987 §§ 148-152.
\end{itemize}
modicum of passenger service by the provincially-owned railways (British Columbia and Ontario Northland) and some privately-owned trains hang on so long as the Algoma Central and Quebec North Shore & Labrador keep going.

VIA Rail is a relatively new Canadian institution, limited to providing intercity rail service. In the mid-1970's, the Canadian rail transport system was an anomaly. Other nations had converted their rail networks to public ownership. The United States Congress had passed the Rail Passenger Service Act of 1970, which had established the National Railroad Passenger Corporation - Amtrak. Amtrak is not a public entity, but a private corporation owned by four participating railroads - but it has continued to exist by virtue of Congressional funding and government support. In contrast to this, Canada persisted in its competition between the public and private sector. The privately-owned Canadian Pacific was decidedly unhappy about continuing to foot the passenger burden, and was taking steps to reduce its passenger deficit by replacing conventional trains with rail diesel cars, and discontinuing secondary and branchline runs, as well as some intercity service. Even the publicly-owned Canadian National was chafing under its mandate to provide essential passenger services. Its experiments with innovative fare pricing policies had not stemmed the rising tide of red ink, and by 1975 the CN was in the process of studying the best way to use its passenger fleet effectively.

In October, 1976, the first joint timetable was issued by Canadian National and Canadian Pacific. The latter railroad also announced it was adopting the VIA logo for its equipment, with an eye to coordinating service, a necessary first step before a government-sponsored revitalization of that service could occur. Via Rail Canada, Inc., was incorporated in January, 1977, under the Business Corporation Act, and approved by the Parliament of Canada in March of that year. Originally, VIA was a subsidiary of the Canadian National and was charged only with the planning and marketing of services. Equipment, stations and employees would continue to be provided by CN and CP. VIA was to collect all the revenues and would pay the carriers 100% of the costs incurred in providing the service, as opposed to 80% under the 1967 National Transportation Act.

VIA found it difficult, however, to conduct negotiations with a railroad of which it was a subsidiary. In order to maximize the efficiency of VIA and make it more even-handed in its dealings with both the CN and CP, it was made a Crown Corporation on April 1, 1978. It operates basically

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224. Id. A Crown corporation is established for some public or quasi-public purpose. VIA Rail's sole responsibility is the carriage of intercity passengers. See T. Nelligan, VIA RAIL CANADA: THE FIRST FIVE YEARS (1982).
as a private corporation, but is subsidized by the Federal government and
must submit an annual report and request for funding to the Canadian
government. The new corporation now has the powers of a railway com­
pany and is regulated by the CTC. The company was not to be responsi­
ble for any rail service until the CTC completed its rationalization process
for that particular service. Then, the government would enter into a con­
tract with VIA for that particular route. VIA would contract with CN or CP
to provide locomotives and crews. VIA acquired CN and CP intercity
equipment, after selecting the best of the aged fleet for its purposes. It
has since ordered rail equipment of its own.

Like Amtrak, VIA is set up as an independent, ostensibly "for-profit"
corporation dedicated to providing improved intercity passenger service
by rail. Neither country is yet ready to declare outright nationalization of
their railroads, or even of their passenger function. However, VIA is
owned, as is Canadian National, by the Crown, whereas Amtrak was le­
gally the property of four cooperating railroads. Also similar to Amtrak’s
legislation is the limiting of VIA's service to intercity passenger trains. VIA
does not run commuter or urban transfer routes.

The main thrust of VIA was to reduce the deficit of rail passenger
operations in Canada. While VIA is labeled a "for-profit" corporation, it
was never expected to be a money-making venture. It has, however,
slowed down the increase in losses.

The rationalization and emergence of VIA was the end product of a
CTC study on the implications of Amtrak for Canada. One of the implica­
tions was that by 1978, the U.S. would have a better rail passenger sys­
tem than that of Canada. Furthermore, if Amtrak’s estimate of its FY1978 deficit is at all accurate and,
if Canada’s passenger train subsidies continue to increase at about the
same rate as they have in the past, it is likely that Canada will pay more for its
80% subsidy program than the United States will be paying for Amtrak.
Another implication has to do with the roadbed problem. Are passenger and
freight systems just as incompatible in Canada as they apparently are in the
United States? Not enough is known to provide a definitive answer to the
questions. A great deal of additional research needs to be done to reveal the
system-wide effects of “efficient” 250 car freight trains.

Finally, the findings and conclusions of this study do not seem to indicate that
Amtrak, in its present form, is an appropriate model for Canada. Amtrak
was, and is, a pragmatic compromise developed within the larger United
States context of bankrupt railroads owned by successful holding compa­
nies. Canada, with a program of 80% subsidy and a Crown Corporation in
railroading, has an institutional context quite different from the United States
— and perhaps even more complex. Certainly, further study of institutional
arrangements for providing future rail passenger service in Canada is
All Fool’s Day, 1978, brought VIA into the rail business directly. Up until that date, the corporation had been proceeding on a step-by-step, route-by-route basis. But observers felt that basis was too complicated and inefficient. Thus, April 1, 1978, was set for VIA’s takeover of every CN or CP train not rationalized out of existence by that time. VIA is organized into four regions: Atlantic, Quebec, Ontario and West. At its genesis, it acquired at its start approximately 2,800 unionized employees and 500 non-scheduled management and professional employees. Approximately 2,300 additional employees were later transferred from CN and another 500 from CP.

Labor negotiations between the parties were governed from the outset by Federal government legislation enacted in October 1977. The parties were unable to agree, and a special mediator was called in to help the parties reach a settlement, with one issue - separation from service - submitted to binding arbitration. As a result, the unionized employees did not come under the VIA plan until July of 1978.

Since April 1, 1978, CN and CP have sent the bills for their passenger service to VIA — 100% of the avoidable costs. Ministry of Transport officials were expected to keep a close check on the fledgling carrier’s finances since the Ministry is VIA’s banker. The relationship of the Ministry to its creature, VIA, is very much like that between the government and Air Canada, until 1989 a Crown corporation. The government does not run the corporation; it arranged that the corporation is well run. A Ministry spokesman described the role of the government as giving the general direction, providing management and verifying that management is working in the direction outlined. The corporation should handle the specifics. The first combined tariff was filed for VIA trains, effective June 15, 1978. (Unlike Amtrak, the corporation must have regulatory approval of rates and fares.)

From the start, VIA Rail’s costs relative to the size of the population to be served proved to be a problem. David P. Morgan, the respected rail journalist and editor of Trains, wrote in 1978:

Those inexorable economics show no respect for national boundaries. Or to quote Canadian National President Robert A. Bandeen, “Passenger services cannot be provided on a profit-making basis under North American conditions.” To which, we think, VIA’s (Garth) Campbell would add, any passenger service: rail, road, or air. The trains’ losses are visible, he argues, while the deficits of the competition are hidden in publicly provided airways and roadways.

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227. PASSENGER TRAIN JOURNAL, June 1978, p. 35.
Be that as it may, the VIA system is going to cost 23 million Canadians more than the Amtrak network costs 216 million Americans:

<table>
<thead>
<tr>
<th></th>
<th>VIA</th>
<th>ATK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Route-Miles</td>
<td>14,000</td>
<td>26,000</td>
</tr>
<tr>
<td>Passengers (millions)</td>
<td>7</td>
<td>19.2</td>
</tr>
<tr>
<td>Revenues (millions)</td>
<td>$120</td>
<td>$311.2</td>
</tr>
<tr>
<td>Loss (millions)</td>
<td>$300</td>
<td>$536.6</td>
</tr>
</tbody>
</table>

The assumption is that parliament will be more benign about these statistics than is Congress. However, thinly populated, Canada’s land mass is larger than that of the U.S., thus eight times as many passenger route-miles per capita may be justified. Item: There’s no U.S. equivalent for CN’s line up to Hudson Bay, with a terminus at Longitude 94 and Latitude 59 (on a parallel with Juneau, Alas.), and in consequence no Amtrak counterpart for the triweekly passenger train that goes there.

There are many similarities between Amtrak and VIA which show a basic affinity in the statutory schemes. Both are independent corporations with government guidance. Both are nationwide in scope and intend to effect savings by combining formerly separate systems. Both involve marketing schemes to increase patronage and reduce deficits, and both replace railroad-operated passenger services which the railroads involved wanted to dump. Both are concerned only with intercity, long-distance passenger services. VIA and Amtrak do not operate commuter trains, which are a local responsibility.

In the last decade, VIA Rail has compiled a worse track record than Amtrak. It was too late in refurbishing its equipment as a tenant of the railroads, and has had trouble keeping a handle on costs or scheduling reliability. Part of the problem is that the VIA rail system, almost the length of Amtrak’s with a similar deficit ($600 million a year) is being supported by one-tenth the population. Whereas Amtrak’s deficits cost every American $3, the equivalent deficit costs each Canadian $30 to support VIA. It is like trying to run the Trans-Siberian Railway with the population of New York State.

VIA was left out of much of the planning that resulted in the Transportation Act. Furthermore, the government planned a VIA Rail Act to complement the other transport legislation, but none was forthcoming. The Mulroney government viewed rail passenger and freight services as discrete problems.

In contrast to the plans for other Canadian transport modes, VIA is deregulated but publicly owned. The main issue concerning VIA is cost limitations and government subsidies.

In April 1989, a trial balloon was leaked from the Mulroney government, suggesting the end of the line for VIA. The budget for Fiscal Year

1990 calls for just enough to keep VIA's major services running, and after that it is anyone's guess.

As of this writing, changes have been proposed affecting the future of VIA Rail without any legislation being enacted in Parliament. The entire effort to cut back on VIA subsidies has been run by the Cabinet through ministerial order; the point man for the campaign in 1989 was the Conservative Minister of Transport, Benoit Bouchard. Ronald Lawless, already chief executive officer of Canadian National, was appointed president of VIA as well in the Spring of 1989, and apparently will preside over the shrinkage of the system.  

Government funding of VIA operations will be reduced as follows:

- 1989-90: $541 million
- 1990-91: $435 million
- 1991-92: $394 million
- 1992-93: $275 million
- 1993-94: $250 million

VIA is instructed to submit a new business plan to the government for the years 1990-94, which would include prospective operations of passenger service throughout that date. Another expenditure will be lifetime job protection for VIA employees with more than four years' seniority; under that dispensation, it might be cheaper in the short run to operate VIA than to shut it down, as is the case with Amtrak.

In Canada, passenger trains often serve isolated communities with neither airports nor highways. Because of this phenomenon, the transport minister declared that services are to be protected on the following remote routes:

- Edmonton, Alberta - Prince Rupert, British Columbia
- The Pas, Manitoba - Churchill, Manitoba
- Winnipeg, Manitoba - Capreol, Ontario
- Montreal, Quebec - Senneterre, Quebec
- Montreal, Quebec - Jonquiere, Quebec
- Senneterre, Quebec - Cochrane, Ontario

Provision of these remote services would leave scant funding for the rest of the system. It appears that the reduction in VIA subsidies was decided not on the basis of transportation criteria, but in response to the Mulroney government’s need to cut its horrendous fiscal deficits. VIA Rail was a service that the government decided Canada could do without.

The cuts in VIA service were announced on October 5, 1989, with the Transport Minister stating that Canada could no longer afford the level of service provided by VIA Rail. As part of a diminished budget strategy for VIA, the cuts may not be the last word; but under Canada’s parliamentary
system where the government gets its way until there is a vote of no confidence, few expect the discontinued trains to make a comeback.

The effect of the cuts is effectively to take the Canadian Pacific out of the passenger business (except for a triweekly Sudbury-White River RDC, the Atlantic across Maine and a Calgary-Vancouver weekly stub). Transcontinental service will now be an all-CN routing.

Canadian National's route was favored because it incorporates some "remote services" stipulated in the earlier (May 3) report which stated that the government "ensures that rail passenger service will be maintained to remote localities which have no other year-round means of transportation." One of these routes is Winnipeg-Capreol, which now will be included in a triweekly Super Continental route. In addition, Edmonton-Prince Rupert (route of the Skeena) is a remote service deserving of protection, which can connect with the Super Con at Jasper.

Other services to be protected as to "truly isolated communities" include the Winnipeg-Churchill Hudson Bay, that Wabowden-Churchill mixed and the mixed train serving The Pas and Lynn Lake, Manitoba. Service out of Montreal to Senneterre and Jonquiere, Quebec, and between Senneterre and Cochrane, Ontario, is to be preserved as well. Finally, the Canadian may be gone, but the "remote services" provision will ensure that the RDCs operating between Sudbury and White River, Ont. along the CP will be saved as well. Still other features of the trimmed rail service include the following:

—Daily service in Canada is restricted to the provinces of Ontario and Quebec. Everything outside the Quebec-Windsor corridor is now triweekly.

—The Maritime is the area most hard-hit by the Bouchard axe. It is also the most vocal; an earlier plan to restrict service to a triweekly Ocean was replaced by the current scheme of service six days per week, thrice weekly on each route (CN and CP).

—Joint services with Amtrak are unaffected. Joint trains will still run out of Toronto to New York and Chicago. New York-Montreal service via the Adirondack and the newly-reinstituted Montrealer are totally Amtrak concerns and thus unaffected.

—The "Canadian Rockies by Daylight" service has been renamed the "Rocky Mountaineer" and remains in the timetable. The train will leave Vancouver each Sunday and proceed to Kamloops, where passengers will stay overnight and reboard the train the next day, divided into Jasper and Calgary sections. The daylight train will return to Kamloops on Thursday and Vancouver on Friday.

—Hudson Bay service remains unaffected, even to the mixed train

between Wabowden and Churchill. Minister Bouchard has said, however, that such protected remote services will be reexamined after a year, in a continuing search for transport alternatives. 233

—With everything west of Windsor on a triweekly basis, Amtrak’s Empire Builder (with connecting buses) is now234 the only daily service to Winnipeg and Vancouver.

—VIA made no attempt to cushion the blows with alternative services. However, Canada’s intercity bus companies have stepped up plans to offer increased service on January 8, one week before VIA’s cuts take effect. Bus fares are also expected to rise with the withdrawal of subsidized rail competitors.

Not only trains will disappear, 2,761 of VIA’s 7,300 employees are scheduled to be furloughed on January 15. Although VIA’s contract contains generous labor-protective provisions (lifetime guarantees after four years with the corporation), VIA spokesmen insist that such benefits are only due those who exhaust all railroad and non-railroad opportunities to mitigate their losses first. 235

The new VIA system of 191 weekly trains will require $350 million (Canadian) in annual subsidies, compared with the $641 million (roughly equivalent to Amtrak’s annual subsidy) presently needed to keep the 405 VIA trains in operation.

The selection of CN routes throughout may have been based on other than transportation criteria. Several influential Tory parliamentarians live on the retained routes. (When the Liberals were in power, it was the CP, not the CN, that was retained for transcontinental services.) CN routes are further north with fewer transportation alternatives. Although a smaller population base may threaten revenues, the trains perform a greater social need in the northland. Finally, VIA operates over the CN with its own crews and own labor agreement. Its CP trains operate with CP engine and train crews, and a more expensive labor package.

Gone from the timetable for good are the following routes:

Halifax-Yarmouth
Halifax-Sydney
Moncton-Edmundston
Montréal-Québec (via CP and Trois-Rivières)

233. Amtrak’s Empire Builder serves Grand Forks, N.D. and Everett, Washington. Amtrak has made arrangements with connecting bus lines to bring passengers to Winnipeg and Vancouver. In November there was a brief flurry of excitement in Manitoba, as local politicians accused Amtrak of a power grab to lure passengers south of the border. (The Empire Builder operates on a daily basis, while VIA will only run thrice weekly on the transcontinental route.) See Huck, Sabotaging VIA Rail, Winnipeg Free Press, Nov. 28, 1989.

234. Interview with Jane Dick, Public Affairs Representative, VIA-WEST, Winnipeg, October 18, 1989. See Bergman, supra note 231.

Toronto-Havelock
Toronto-North Bay
Cochrane-Kapuskasing
White River-Winnipeg
Winnipeg-Calgary
Victoria-Courtenay

(See Table 7)

All non-corridor service operates thrice weekly, except the weekly Rocky Mountaineer and the once-a-week Wabowden-Churchill mixed train. With the demise of the overnight Montreal-Toronto Cavalier, sleeping cars will now only operate on the transcontinental and Maritime trains, as well as on the Hudson Bay to Churchill.

Within the Corridor, frequencies will be reduced as well. Montreal-Quebec (now limited to the CN route, plus the Ocean, which stops at Levis across the river) is down to three trains a day. Toronto-Sarnia is cut from four times a day to twice daily (including the International), and there are reductions to Niagara Falls and London as well.236

As for the future, the Tory motto is still "use it or lose it." Meanwhile, Prime Minister Mulroney has promised a Royal Commission to investigate the future of Canadian surface transportation for the 1990s and develop legislative policy. Royal Commissions in the past have been graveyards for political concepts, but this time the Government states that it will be bringing out a VIA Rail Act in the Spring of 1990. Currently, there is no Canadian legislation comparable to the Rail Passenger Service Act of 1970, which governs Amtrak. The lack of a statutory basis is one of the handicaps VIA has had to face in this troubled decade.

The vagaries of VIA are similar to the continuing melodrama of Amtrak appropriations during the 1980s. Amtrak has both expanded and contracted along with the political winds, but its system remains more or less intact and service is gradually improving. During the Reagan administration, successive Republican secretaries of transportation proposed budgets with zero funding for the passenger rail corporation. However, in the United States, unlike Canada, the head of government does not control the budget’s fate in Congress. For eight years, a Democratic house and a Senate which changed from Republican to Democratic leadership successfully rebuffed the Reaganite efforts to eliminate the intercity passenger train from the United States. An uneasy truce prevails during the Bush administration, and Amtrak has been able to trim its own costs by operating new equipment and establishing new labor contracts with its operating unions. Also, Amtrak has its own enabling legislation (the Rail

Table 7
VIA Network -- 1990
Old and New Routes of the Canadian

[Map showing routes in Canada and the United States, with different line styles indicating current, former, and daily routes.]

- Current route of the Canadian
- Former route of the Canadian
- Corrida (Daily)
- Tri-weekly Routes
Passenger Service Act of 1970), while VIA has been around for a dozen years without any organic act of Parliament establishing its functions.

Neither VIA nor Amtrak are technically part of the deregulation story. But the corollary of allowing freight railroads to compete effectively with truckers for the shipper’s dollar has been relieving them of public service burdens by setting up entities to operate both commuter and intercity passenger service.

Deregulation in Canada goes hand in hand with talk of privatization — of VIA Rail, of the Canadian National Railways, and even of Air Canada. Whether or not privatization is a way to phase out the Crown Corporations, or merely a smokescreen for abandonment of services remains to be seen.

With regard to privatization of passenger railroads, there is one prospective buyer at this writing. Sam Blyth, president of the Toronto-based travel agency Blyth & Co., is negotiating a $10 million bid to buy the Canadian linking Montreal and Vancouver. Blyth intends to convert the train into a luxury cruise train, similar to the Orient-Express operation in Europe. The price of a first-class one-way ticket between East and West would be $2,500 — five times the current price. If the deal is consummated, Blyth would operate twice weekly during the summer, and in the winter, merely operate Toronto-Montreal and Calgary-Vancouver luxury service. In response to charges of elitism, Blyth said his luxury express would stop at the smaller cities currently served along the CP route, and have a few coach seats for one-way fares as low at $230.237

In addition, on November 30, 1989, VIA advertised nationally throughout Canada that it was initiating discussions with parties who have expressed an interest in private operation of the seasonal “Rocky Mountaineer,” complete with a fax number for interested parties to state their qualifications. The Mulroney government is at least giving lip service to privatization. In addition, Ontario’s GO Transit commuter agency has taken over VIA’s Toronto-Peterborough route.238

Railroad deregulation began in the system of competing private rail-

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237. VIA advertisement appeared in Winnipeg Free Press, Nov. 30, 1989. It states that “Others with an interest are invited to make this interest known, in writing or by Fax, no later than 12 noon, December 15, 1989.” Sources at the Free Press stated that Amtrak may be one of the interested parties in this tourist operation. As far as GO Transit, see PASSENGER TRAINS JOURNAL, NOV. 1989, p. 37.

238. De facto deregulation of the motor carrier industry began with the liberalized approach of the Interstate Commerce Commission in 1977 and 1978, when the ICC began issuing operating authority more broadly defined, from a commodity and territorial perspective, than ever before. The nation’s economic recession did not begin until 1979, yet every leading economic indicator shows that the industry has progressively suffered virtually every year since 1977. P. DEMPSEY, THE SOCIAL AND ECONOMIC CONSEQUENCES OF DEREGULATION 40 (1989) [hereinafter P. DEMPSEY].
roads in the United States. To see if deregulation is exportable, the next market test seems to be our closest neighbor, which has relied on duopoly — the Crown corporation to keep the private sector honest; the private company to keep the Crown efficient. In embracing deregulation, Canada is taking as historic a step in changing policy as it has in free trade. Both are leaps of faith. Let us hope Canada can profit from our mistakes.

IV. CANADIAN MOTOR CARRIER Deregulation

A. MOTOR VEHICLE TRANSPORT ACT, 1987

This section assesses the legal, social, and economic dimensions of motor carrier deregulation in Canada. In some respects it may be too early to draw definitive conclusions about transport liberalization in Canada, because Canada has only recently passed federal legislation liberalizing interprovincial traffic. However, one can, by looking at the decade of experience under motor carrier deregulation south of the border, make some projections as to how deregulation will manifest itself in Canada, for the United States effectively deregulated its motor carrier industry a decade before.

In the United States, Congress deregulated motor carriers with the promulgation of the Motor Carrier Act of 1980. It provided for rate flexibility, and on entry, shifted the burden of proving that granting an application for operating authority would be inconsistent with the "public convenience and necessity" to protestants, while applicants continued to bear the legal obligation of proving that they were "fit, willing and able" to perform the proposed operations. But de facto deregulation preceded de jure deregulation in the United States by about two years, tracing its origins to decisions of the U.S. Interstate Commerce Commission in 1977 and 1978.239

Canada promulgated the Canadian Motor Vehicle Transport Act, 1987 [MVTA]240 about a decade after the United States launched its experiment in deregulation. Many Canadian Provinces, too, launched their experiment in de facto liberalization in the early 1980s, following the American lead; the new federal legislation is designed to provide uniformity for the acquisition of intra-provincial authority in all provinces.

The 1987 legislation replaced the Motor Vehicle Transport Act of 1954, under which provincial transport boards defined criteria for extra-provincial authority. Under the 1954 legislation, each province was free to define its own criteria for motor carrier entry across its borders. Pursuant thereto, there was a wide spectrum of approaches to regulation, some

provinces adopting virtually de facto deregulation while others remaining rather tightly regulated. The 1987 legislation was designed to eliminate those discrepancies between provinces, and to provide uniformity among the provinces in terms of the acquisition of extra-provincial operating authority.

The new legislation is the product of a 1985 Memorandum of Understanding between the federal and provincial governments. The 1987 legislation calls for a five-year, phase-in period of deregulation. As of January 1, 1988, the acquisition of operating authority is a three-step process. In the first, an applicant's fitness is determined, no longer by the provincial motor carrier boards, but now by an independent functionary. Second, once notice is published, if no objection has been filed, the application is automatically granted to those carriers deemed fit in stage one. If an objection is filed, the provincial motor carrier board determines whether a hearing shall be set. Third, the board determines whether issuance of the requested authority is likely to be "detrimental to the public interest." Here, the burden of proof has been shifted to protestants. This places a reverse onus upon interveners. If the protestants establish a prima facie case, the applicant may submit rebuttal evidence. In deciding whether new entry will be allowed, the Board must give "primary emphasis to the interests of users of transportation services."

The MVT A eliminates interprovincial rate regulation as of January 1, 1988, although rates have never been as strictly regulated in Canada as they once were in the United States. It also creates a mechanism for establishing more stringent safety regulation of motor carriers, that is being implemented in phases.

As of January 1, 1993, the MVT A provides for elimination of the "public interest" test; hence, "fitness" will become the sole criterion for extra-provincial entry. Moreover, commodity and route limitations will then be eliminated. However, the "reverse onus" procedure will be reviewed by the Minister of Transport to determine whether an extension of the transition period will be desirable.

241. MVTA, supra note 239, Part II, art. 8(2).
242. MVTA, supra note 239, Part II, art. 8(3).
243. Id.
244. MVTA, supra note 239, Part II, art. 8(5)(a).
245. Extra-provincial rates in Canada were only nominally regulated prior to 1985 when rate regulation was limited to a filing requirement in certain provinces. 1988 ANNUAL REVIEW, supra note 240, at 45.
246. MVTA, supra note 239, art. 3(1).
247. 1988 ANNUAL REVIEW, supra note 240, at 38.
The MTVA left interprovincial bus transport much as it found it. Entry in the bus industry will continue to be governed by the "public convenience and necessity," and the Provinces may regulate bus tariffs and tolls.249 It also leaves intraprovincial discretion on motor carrier regulation to the Provinces, much as the U.S. Motor Carrier Act left intrastate regulation unmolested.250

B. PROVINCIAL IMPLEMENTATION OF THE MVTA

The new federal legislation appears to have opened wide the floodgates on entry in motor carriage. Tremendous interest has been generated on behalf of motor carriers in seeking new operating authority. For example, in 1988, there were more than one thousand applications pending in Ontario alone.

On the whole, the approach of the provincial licensing boards appears to be extremely liberal. At this writing, Quebec and Alberta appear to be the most liberal, while Manitoba and New Brunswick appear to be the most conservative.251

Moving from west to east across Canada, in one case, the British Columbia motor carrier provincial board denied operating authority to a new applicant, concluding that the hauling of automobiles from docks to interior points was a natural monopoly. In a more recent decision in British Columbia, and one which has received considerable attention, it granted extra-provincial operating authority to United Parcel Service. In Alberta, applications appear to be generally unopposed. Being unopposed, of course, requires that the applications be granted under the new legislation. The Saskatchewan Board has required certificates of support for new applications. Manitoba appears to have adopted a "go-slow" approach to new entry, preferring to use the transition period as a true transition, as the federal legislation suggests. More about Manitoba's independent approach below. For some time, Ontario appeared to be paralyzed because of a jurisdictional dispute between two regulatory bodies, the Provincial Transportation Ministry and the Ontario Highway Transport Board. In Quebec, the motor carrier board appears to be granting all applications. In Nova Scotia, transport authorities apparently are taking a conservative approach to less-than-truckload (LTL) entry.252 In New Brunswick, a number of cases have been set for hearing. In Newfound-

249. MVTA, supra note 239, Part III, art. 11-15.
250. 1988 ANNUAL REVIEW, supra note 240, at 38.
251. Smith, supra note 248.
land, the motor carrier board has made it clear that the intervenor would have to meet a very heavy burden in order to prevail.

In most Provinces, it appears that existing incumbents are finding that opposing motor carrier applications for extra-provincial authority is wasteful of time and resources. The futility of opposition is causing more and more applications to go unopposed, leading to a flood of new entry. Although the federal legislation called for a five-year transitional period toward deregulation in 1992, in most provinces the period has been collapsed to one or two years. The net effect is that de facto deregulation of extra-provincial operating authority is pretty much here today. That, in itself, creates a number of concerns for the economic well-being of the industry and its stability to adhere to the highest level of safety, in light of the fact that the national safety code in Canada is only gradually being implemented.

C. MANITOBA’S INDEPENDENT COURSE

The Manitoba Motor Transport Board has taken an independent approach to implementing the MVTA, one which insists on not capitulating immediately to deregulation as have virtually all the other Provinces, and which intends to utilize the statute’s full five-year transition as a legitimate transition period. Early in the process, Mr. Donald S. Norquay, Chairman of the Manitoba board, recognized that the “reverse onus” of the federal legislation would be an impossible burden for intervenors to sustain, and that unless a more conservative approach to licensing were taken, the floodgates to entry would be opened creating much unnecessary turmoil in the industry. The “reverse onus” started was proposed by the Council of Ministers on May 31, 1984. Mr. Norquay immediately had reservations about the viability of such a standard. In the 1985 proposal he prepared for the Manitoba Transport Minister, he perceptively observed:

After a very short period, it is probable respondents will find they are losing all their cases because they cannot prove, beyond speculation, any detriment [to the public], and will give up on filing oppositions. As a result, the system will be effectively deregulated in an insidious manner, without adequate preparation for the consequences of doing so.253

Indeed, what Mr. Norquay accurately predicted would happen has happened in virtually all the Provinces. As in the United States, Canadian protestants eventually give up protesting applications they cannot defeat. Mr. Norquay expanded his thoughts in a speech delivered before implementation of the MVTA:

[R]eform economic regulation is a slippery slope. When entry is eased, beyond some point entry control will be effectively eliminated for all practical

purposes. Cognizant of this, the Board has been cautious in its reform. Rather than a full "reverse onus," which is feared may be tantamount to complete deregulation, the Board has adopted a "shared onus" entry standard. . . [N]ext January 1st, the Board will be compelled by federal law to implement a full "reverse onus" entry standard, despite our concern that such a standard has the potential to cause the system to quickly slide down the slippery slope of regulatory reform to the bottom of the valley of deregulation; and at the risk of carrying the metaphor too far, with this occurring before we have a national safety code in place that valley could literally be akin to the valley of the shadow of death. In this context, I pledge to you that the Board will do everything within its legal power to ensure the continuance of a meaningful entry standard for extra-provincial trucking, after January 1st, 1988. 254

Unfortunately, Mr. Norquay had the Curse of Cassandra: the ability to predict the future coupled with the inability to have anyone believe him. Here is the fundamental difficulty posed by the MVTA’s imposition of a "reverse onus" upon intervenors, again, as described by the eloquent Mr. Norquay, after implementation of the federal legislation:

Quite frankly, in my heart I still believe that you either regulate entry or you do not. In principle, there can be no "easing" of entry control through reversing the burden of proof without assuming entry control should be virtually eliminated. . .

The essential reason for this is that by shifting the burden of proof to respondents, Parliament is saying to the respondents in each and every case, it is up to you the carriers, to provide a theoretical and empirical basis to support a system of economic regulation. You must prove the negative that unfettered competition will not best serve the public interest. And of course, if any carrier could do this, then we should not be deregulating at all. . . .

A system that assumes competition is best, but gives respondents a chance to prove otherwise, makes no sense: if a respondent can do this, then the basic assumption of the system is wrong. It is entirely unreasonable to expect respondents to prove the theories of destructive competition, network economics, economies of scale and scope, oligopoly pricing, price and service discrimination, cross-subsidization and so on. Economists have spent decades studying these issues without definitive answers. 255

The Manitoba Motor Transport Board responded to the dilemma posed by the MVTA by finding that a significant influx of new entrants would increase the likelihood that "a significant component of the existing Manitoba trucking industry will not survive the transition to deregulation." 256 It believed that "there is a significant risk of a substantial adverse effect on the economic development of the Province which could be

256. Id.
avoided if deregulation is appropriately phased-in."\textsuperscript{257} In order to avoid these potential adverse effects, the Manitoba Board adopted a "cumulative effects" test — applicants would effectively bear the burden of proving that the public interest would not be adversely affected if all other pending applications are granted as well. Said the Board:

Although there may be no demonstrable detriment to the public interest from the granting of a single application, where there is no evidence to distinguish the applicants' operations from one another, the Board must, in order to properly assess whether detriment to the public interest is likely, assume in each application the granting of all others pending, and assess the cumulative effect on the public interest of doing so.\textsuperscript{258}

The number of applications for extra-Provincial applications pending before the Manitoba Board was vast:

\begin{table}[h]
\centering
\begin{tabular}{lcc}
\hline
\textbf{EXTRA-PROVINCIAL APPLICATIONS FILED WITH THE MANITOBA MOTOR TRANSPORT BOARD} & 1988 & 1989 (to Sept. 30) \\
\hline
Applications filed & 393 & 291 \\
Pending & 214 & 188 \\
Granted in full & 218 & 173 \\
Granted in part & 218 & 43 \\
Denied & 1 & 2 \\
\hline
\end{tabular}
\caption{Extra-Provincial Applications Filed with the Manitoba Motor Transport Board}
\end{table}

Obviously, the granting of each of the hundreds of applications filed would flood the market with capacity and destabilize the trucking industry, potentially causing the bankruptcy even of efficient and well-managed carriers. The Manitoba Board was convinced that a more conservative approach to gradual entry would cause less economic turmoil and fewer safety problems, and was therefore determined to use the five-year transition period contemplated under the MVTA to avoid deleterious consequences.

But the Manitoba Court of Appeals struck down the Motor Transport Board's application of the cumulative effects test on grounds that in denying operating authority to new applications, the Board had not considered the evidence in the other pending applications proceeding upon which it relied to deny operating authority.\textsuperscript{259} The solution of this problem is, of course, to consolidate a large number of pending applications, and consider the evidence as to the cumulative effects of

\textsuperscript{257} Id. at 5.
\textsuperscript{258} Robert Lindsay v. Motor Transport Board of Manitoba, Manitoba Court of Appeal, slip. op. (Sept. 8, 1989).
granting them all. This indeed, appears to be the direction in which the Manitoba Board is heading.

D. THE IMPACT OF UNCONSTRAINED ENTRY

In its economic impact study, the Canadian federal government predicted that the new legislation would create a large number of entrants and a large number of motor carrier failures. That indeed, was the experience in the United States when it opened the floodgates of entry and deregulated rates. The empirical evidence of motor carrier deregulation in the United States reveals that a large number of new carriers entered the industry during the initial years of deregulation. Excessive capacity caused the proportion of empty trailers and the number of empty miles to increase and load factors to suffer. The immediate response to declining rates was one of great public applause. This appeared to be a development of great benefit for consumers. However, the United States experience reveals that in the longer run, there are some distressing trends. Among them is some measure of declining productivity because more entry creates more capacity without stimulating additional freight, and that simply leaves trucks emptier over more miles. In the

260. Between 1980 and 1983, 49,726 new certificates for motor carrier operating authority had been granted by the ICC; this included certification of 13,806 new carriers. Rosenak, address before the Motor Carrier Lawyers Ass'n., (Washington, D.C., Jan. 8, 1983); ICC Chairman Tells Senate Panel He Favors Early Sunset of Agency, TRAFFIC WORLD (Dec. 20, 1982), at 27, 64. The ICC has also largely expanded the ability of private carriers to engage in common carriage. See e.g., Leasing Rules Modifications, 132 M.C.C. 927 (1982); Lease of Equipment and Drivers to Private Carriers, 132 M.C.C. 956 (1982). See Faris & Southern, Federal Regulatory Policy Affecting Private Carrier Trucking, 49 ICC PRAC. J. 503 (1982); Borghesani, Motor Carrier Regulatory Reform and its Impact on Private Carriers, 10 TRANSP. L.J. 398, (1978). As of June 1, 1983, the ICC had certificated 25,342 carriers. This represents a 43% increase in the number of carriers holding operating authority since promulgation of the Motor Carrier Act of 1980. The Commission gave some 870 carriers nationwide authority, effectively deregulating them from an entry standpoint until the end of time. See Statement of George Ziglich before the U.S. Senate Surface Transportation Subcommittee of the Committee on Commerce, Science and Transportation (Sept. 21, 1983).

261. P. DEMPSEY, supra note 238, at 79.

262. Id. at 100.

263. Productivity for general freight carriers grew by an average of 0.29% annually after 1969, it has declined by 0.21% per year since 1978. In contrast, productivity levels of all manufacturers have increased an average of 2.4% per year since 1975. Panelists Deplore Truck Regulation; Rate Discrimination at NARUC Confab, TRUCK WORLD, Dec. 1, 1986, at 68-69.

264. Professor Grant Davis has observed that the nation's largest shippers exert monopsony of the economic leverage they wield by conferring or withholding their vast volumes of freight. The Fortune 500 can unilaterally dictate rates at (and for cash-starved carriers, below) the marginal costs of trucking companies. Oversight of the Motor Carrier Act of 1980: Hearings before the Subcommittee of Surface Transportation of the Senate Committee on Commerce, Science and Transportation 99th Cong., 1st Sess., 234 (statement of Prof. Grant M. Davis).
short run, wealth is transferred first from investors, and then from labor, to shippers, particularly large shippers.

**E. PRICING**

Under deregulation, the United States experienced a phenomenon that was largely unanticipated, that of a monopsony power creating highly discriminatory pricing. Very large shippers enjoy monopsony power because of their enormous volumes of freight, which enables them unilaterally to dictate rates. To give an example, in the United States, upwards of 50% in general revenue price increases have been authorized by the U.S. Interstate Commerce Commission since 1983. Discounts off the published rates are running up to 75%, but the steep discounts are enjoyed exclusively by large-volume shippers. Smaller shippers either pay the full rate or enjoy rather more modest discounts of, say, 5-15%. While all shippers perceive that they are getting a bargain, in fact, smaller shippers are paying more for transportation today than they did prior to deregulation. Moreover, this distortion in transport pricing distorts the broader market for the sale of commodities. Pricing discrimination may cause serious injury to those enterprises or geographic regions disfavored by the pricing scheme. The U.S. Supreme Court in *Munn v. Illinois* recognized that transportation firms are the gatekeepers of the larger market for the sale of commodities; therefore their price and service offerings must be nondiscriminatory.

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266. P. Dempsey, supra note 238, at 100.
267. A small shipper recently summarized the impact of transportation deregulation upon smaller enterprises in testimony before the U.S. House of Representatives: "the benefits promised by the Motor Carrier Act of 1980 have not reached the medium and small shipper. Small shippers are receiving discounts substantially below what the large shippers enjoy. Our markets are shrinking." Coalition For Second General Freight Trucking, The Rationale For Trucking Regulation: Exposing The Myths Of Deregulation (1986).
268. Pricing discrimination may cause serious injury to those enterprises or geographic regions disfavored by the pricing scheme. The U.S. Supreme Court has observed that "discriminatory rates . . . may affect the prosperity and welfare of a State. . . . They may stifle, impede, or cripple old industries and prevent the establishment of new ones." Georgia v. Pennsylvania R.R., 324 U.S. 439, 450 (1945).
269. 94 U.S. 113 (1876).
270. P. Dempsey, supra note 238.
torted, the market for the sale of commodities will be distorted as well.\textsuperscript{271} A significant advantage that Fortune 500 companies enjoy under deregulation \textit{vis a vis} their smaller rivals is of particular concern,\textsuperscript{272} unless one concludes that domination by huge corporations is not an undesirable phenomenon.

Two other products of the monopsony power of large shippers have manifested themselves in the United States. One is the ability of large shippers with market power unilaterally to dictate excessively low rates, insufficient to allow trucking companies to cover their full costs of operation. This has a fatal economic impact on unsophisticated carriers with inadequate understanding of costs and without the ability to counterbalance the monopsony power of large shippers which unilaterally dictate noncompensatory rates.\textsuperscript{273} This causes carriers to underprice their services, which gives them insufficient resources to maintain safe operations. By underpricing their services, they also drag down efficient firms with them into the Darwinian abyss of bankruptcy.

A second phenomenon which appears to be growing more widespread is the practice by large shippers of sending commodities "freight collect," whereby the consignee pays the full, published rate for transportation. The large shipper then forces the carrier to rebate to the consignee the difference between the full, published rate and significant discount of up to 75\% off the published rate.\textsuperscript{274} Thus fraud is being practiced on unwary consignees.

If Canada has the same experience, it will see an immediate fall in transport prices in the short run, followed by a longer-term increase in discrimination between large \textit{vis a vis} shippers, in which larger corporations enjoy a significant advantage over their smaller competitors. This will distort the broader market for the sale of commodities, giving larger firms a decided advantage, and cause many motor carrier failures. With the consummation of the Canadian-United States Free Trade Agreement (FTA) in 1988, opening the border between the United States and Canada for the sale of commodities, that broader market could come to be dominated by larger corporations headquartered south of our common border.

\textsuperscript{271} The ten most profitable carriers in 1984 accounted for over 80\% of all general freight carriers profits.
\textsuperscript{272} Between 1979 and 1983 the 75 largest general freight carriers increased their share of Class I less-than-truckload revenues from 79.2\% to 88.2\%.
\textsuperscript{273} During this same period, the four largest carriers increased their market share from 26.4\% to 30.6\%, with the largest carrier increasing its share from 9.1\% to 10.1\%.
\textsuperscript{272} Dempsey, \textit{Punishing Smallness}, Cleveland Plain Dealer, Dec. 12, 1987, at 15A.
F. INDUSTRY ECONOMIC ANEMIA: FAILURES, MERGERS AND CONCENTRATION

In addition to the discriminatory pricing that has occurred in the longer term under deregulation, declining productivity engendered by excessive capacity appears also to have caused destructive and predatory competition between the motor carriers themselves. It must be remembered that transportation firms sell what is, in essence, an instantly perishable commodity. Once the truck leaves its terminal, any unused space is lost forever. It cannot be warehoused and sold another day as could, say canned beans. It is as if a grocer were selling commodities which had the propensities of open jars of unrefrigerated mayonnaise. He would be forced to have a "fire sale" every afternoon in order to rid himself of unsold inventory, for it could not be warehoused and sold another day. So it is with transportation capacity. Unlimited entry creates excessive capacity which, in turn, creates destructive competition and economic anemia.

In the United States, the profitability of the motor carrier industry has been inadequate. Motor carrier profit margins have fallen significantly under deregulation. The U.S. trucking industry has suffered the worst economic losses and the highest failure rate since the Great Depression. In the United States, more than one thousand trucking companies have gone bankrupt each and every year since 1983. In the less-than-truckload (LTL) section of the United States industry, more than 50% of the firms which existed before deregulation have failed. There is also evidence that larger firms have engaged in predatory behavior in order to drive their smaller motor carrier rivals out of the market. Often we see the phenomenon of pricing at or below short-term marginal costs. In part, this is inspired by the instantly perishable nature of the service being sold and the monopsony power of large shippers, and in other instances, it appears to be inspired by the desire of large trucking companies to domi-
nate the market by engaging in predatory behavior.279

As a direct consequence of the ruthlessly competitive environment unleashed by deregulation, the transportation industry in the United States is more highly concentrated than it has ever been.280 This high level of concentration has manifested itself not only in the motor carrier industry, but also in airlines, in railroads, and in the bus industry.281 The eight largest U.S. airlines accounted for 81% in 1987; the eight largest motor carriers accounts for 20% of industry revenue in 1978, and 37% in 1987; and the bus duopoly of Greyhound and Trailways which preceded deregulation became a monopoly with their merger after deregulation.282 Because of the scale and network economies existing in these industries, the long-term trend of deregulation appears to be oligopoly of megacarriers. As noted above, while the less-than-truckload sector of the motor carrier industry has experienced a shakeout of more than half of the firms which previously existed, there have been no new, major entrants into that section of the industry since deregulation began.283

The immediate results of Canadian liberalization appear to parallel those of the United States. Canada has already experienced significant new entry into the truckload arena, although entry into LTL trucking has not been significant.284 Such entry appears to have created significant overcapacity in trucking.285 This squeezed the profit margins of many firms, sharply increasing industry operating ratios to 0.98 in 1988 from 0.96 in 1987.286 Mergers and acquisitions intensified in 1987 and 1988.287 What is even more significant is that bankruptcies of Canadian motor carriers rose sharply to 394 in 1988, a year in which the Real Gross Domestic Product increased by 4.5%, a higher rate than anticipated.288 This parallels the U.S. experience, in which bankruptcies continued at a robust rate even after the recession abated and fuel prices fell.

Unlimited entry and rate deregulation in the United States have, as noted above, created excessive capacity, declining productivity, and

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280. P. DEMPSEY, supra note 238, at 91-92.
281. P. DEMPSEY, supra note 238, at 83-93, 129-93.
284. See Id. at 42.
285. Id. at 47-48.
286. Id. at 38. The most prominent acquisition was of CF Kingsway of Toronto be Federal Industries of Winnipeg, a company which already controlled Motorways Inc. Id. at 38.
287. Id. at 17, 40-41. The largest Canadian bankruptcy in 1988 was that of Transport Route Canada. Id. at 37. Although the number of bankruptcies for 1988 is lower than that experienced in 1982-1984, North America was then reeling from the impact of the deepest recession since the Great Depression.
288. P. DEMPSEY, supra note 238, at 120-125.
therefore destructive competition which, in turn, has created economic anemia and inadequate returns on investment. This economic anemia has had other adverse consequences in addition to the high failure rate among trucking firms. It has caused a significant deterioration in safety and had an adverse impact on labor-management relations and wages.

G. SAFETY

Under deregulation, motor carriage in the United States is an anemic industry with a high turnover rate among firms running aging and poorly maintained equipment and employing overworked and underpaid drivers.289 A recent study by the U.S. Office of Technology Assessment reveals that heavy-truck accidents have increased significantly under deregulation, and at a rate higher than the increased in truck miles travelled.290 Professor Nicholas Glaskowsky points out that deregulation has produced aging equipment, deferred maintenance, and an increasing accident rate. The American Insurance Association performed a study in which it found that the accident rate per million miles has increased under deregulation.291 The American Automobile Association concluded that, under deregulation, motor carriers in the United States run older equipment, pay less in wages, work drivers longer, and skip on maintenance.292

Under the severe rate competition engendered by excessive capacity, carriers cut costs wherever they can.293 The alternative, as noted above, is bankruptcy. For that reason, they have reduced wages for drivers and mechanics.294 Between 1979 and 1985, trucking wages fell 30% in California. At the same time, factory wages increased more than 15%. By reducing pay, the job becomes less attractive, causing the industry to hire unskilled and untrained drivers.

The industry also appears to be deferring new vehicle purchases.295

289. OFFICE OF TECHNOLOGY ASSESSMENT, GEARING UP FOR SAFETY; MOTOR CARRIER SAFETY IN A COMPETITIVE ENVIRONMENT (1988) [hereinafter OFFICE OF TECHNOLOGY ASSESSMENT].
290. N. GLASKOWSKY, EFFECTS OF DEREGULATION ON MOTOR CARRIERS 32 (1986).
291. F. BAKER, SAFETY IMPLICATIONS OF STRUCTURAL CHANGES OCCURRING IN THE MOTOR CARRIER INDUSTRY 15 (1985) [hereinafter cites as AAA SAFETY STUDY].
293. AAA Safety Study concludes that because there are few other areas in which to cut costs, motor carriers whose profit margins are squeezed have less alternative but to "run older equipment, pay less in wages, work drivers longer, and/or skip on maintenance." AAA SAFETY STUDY, supra note 291, at 15.
294. AAA SAFETY STUDY, supra note 291, at 17. N. GLASKOWSKY, supra note 282, at 32.
Carriers also have cut maintenance expenditures up to 3.6% annually. This means that carriers are not buying spare parts when they need them and they are not taking vehicles off the highway when they ought to be. Carriers have also cut training and forced drivers to work longer hours. Corsi and Fanara found that the new entrants had an accident rate up to 27% higher than that of existing motor carriers. The Motor Carrier Act of 1980 exacerbated this problem by increasing the number of new entrants. Daust and Cobb found that fatigue and unqualified drivers were responsible for a disproportionate number of trucking accidents. The American Automobile Association study found that driver fatigue was responsible for 41% of motor carrier accidents on the highway. Under the National Accident Sampling System, the three largest causes of accidents were (1) speeding, (2) the level of training, and (3) the age of the vehicle. All of these factors seem to have worsened under deregulation. Professor Garland Chow found that the carrier which eventually goes bankrupt spends less on maintenance and new equipment; he runs older equipment and uses more owner-operators. Professor Corsi found a correlation between owner-operator use and a higher accident rate.

The average age of trucks on the highway has risen significantly under deregulation from 6.9 years in 1978 to 8 years in 1987. According to Professor Evans, the number of trucks twelve years or older on the highway have more than doubled under deregulation. In 1985, checks of vehicles on the highway under the Federal Motor Carrier Safety Assistance program revealed that 29% of large trucks were insufficiently safe to be on the highway. In some states, the figures have been even higher. In 1986, studies in New York and Connecticut revealed that 60% of trucks were insufficiently safe to be on the highway. The U.S. Office of Technology Assistance reveals that the number of accidents between 1981 and 1989 increased 15%, more than the increase in truck-miles

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297. AAA FOUNDATION FOR TRAFFIC SAFETY, A REPORT ON THE DETERMINATION AND EVALUATION OF THE ROLE OF FATIGUE IN HEAVY TRUCK ACCIDENTS (1985). For purposes of this study, fatigue was defined as more than 15 consecutive hours of on-duty or defined activity time. Id. at 2.


300. Dolan, supra note 273, at 274.

301. Id. at 273-274.

302. P. DEMPSEY, supra note 238, at 122.


304. OFFICE OF TECHNOLOGY ASSESSMENT, supra note 289. See also, N. GLASKOWSKY, EFFECTS OF DEREGULATION ON MOTOR CARRIERS 33 (1986).
traveled during that period.305

The Canadian MVTA implicitly admits that deregulation will likely have a deleterious effect on safety. First, it includes specific recommendations that the Minister of Transport create a safety program.306 Second, the Minister must report to the Canadian Parliament statistical information regarding highway accidents.307 Hopefully, the results will not be as bleak as those experienced south of our common border.

H. SMALL COMMUNITIES

Another adverse effect of deregulation is its impact upon small community service and pricing.308 Approximately 90% of all Canadians live within one hundred miles of the United States border. If small community service should deteriorate or grow more expensive, the vast northern reaches of the continent will be adversely affected. In motor carriage, we have not yet seen the full impact of deregulation, because there has been no federal preemption in the United States of intrastate trucking. Therefore, the deleterious consequences have been somewhat blunted. The overwhelming majority of states in the United States continue to regulate motor carrier entry and pricing.309

However, in those transport sectors where the federal government has preempted the states, the adverse impact upon small community service has been quite profound.310 For example, four years after promulgation of the Bus Regulatory Reform Act of 1982, more than 4,500 communities have lost service, while fewer than 900 had gained it.311 Since enactment of the Staggers Rail Act of 1980, more than 1,200 small communities have lost all of their rail service.312 And, since promulgation of the Airline Deregulation Act of 1978, more than 100 communities have lost all air service.313 More than 150 now receive air service under Section 419 of the Federal Aviation Act, which provides essential air services to eligible points.314 Should the federal subsidies for such service dry up,
a significant number of them — perhaps most — would lose all air transport service. That is of significant concern when one realized that 80% of the Fortune 500 executive officers revealed that they would not locate a facility in a community which did not have reasonable adequate air service.\footnote{Thomas Gale Moore, a nationally recognized proponent of deregulation, admits that 40% of small communities have suffered a loss of air service since deregulation began, while ticket prices have increased disproportionately for them. \textit{Moore, U.S. Airline Deregulation: Its Effects on Passengers, Capital, and Labor}, 24 \textit{J.L. & Econ.}, 1, 15, 16, 28 (1986).}

The loss of transport services creates an outmigration of investment, jobs and population to crowded urban areas, a social consequence which may not be desirable. As noted above, in the United States, we have not witnessed severe disruptions of motor carrier service to small communities under deregulation; however, pricing appears to have increased significantly.\footnote{See supra text accompanying notes 265-74.} Many communities are only served by United Parcel Service (UPS), which sets a price somewhat lower than the United Postal Service for small parcels, but which enjoys profit margins well above those of other industries, suggesting a pricing structure reflecting their monopoly position in the market. Since deregulation, many trucking companies have exited rural markets, leaving the void to be filled by UPS. This means that small communities are paying monopoly prices for transport services.

Moreover, many large carriers are refusing to provide discounts on interline movements.\footnote{G. BLANCHARD \& L. CLAVEL, TRANSBORDER TRUCKING BETWEEN CANADA AND THE UNITED STATES 11 (1988) [hereinafter G. BLANCHARD \& L. CLAVEL].} Hence, the local regional carriers are unable to provide the small communities they serve with the discounts enjoyed in the national pricing structure elsewhere. This means that pricing to and from small communities is higher, on average, than competitive rates in larger markets.

Oddly, while Canadian airline deregulation retains regulatory control and subsidies over entry in the northern tier of Canada so as to protect aviation access to small communities, Canadian motor carrier deregulation has no similar provision to protect rural areas.

\section{Transborder Trucking}

\addcontentsline{toc}{section}{1. Transborder Trucking}

In the early 1980s, the United States government became concerned about the potential advantages Canadian trucking firms enjoyed because of the deregulation of interstate trucking. Canadian-based firms could apply to the ICC for U.S. operating authority and receive rather liberal and
expeditious application approval. In contrast, U.S.-based firms would apply to the Canadian provincial motor carrier commissions for authority; while some were as liberal as the ICC several were not. This created an appearance of discriminatory treatment.

In 1982, the ICC began an investigation of the question, freezing 340 pending applications filed by Canadian carriers for U.S. operating authority.318 The ICC found that Canadian motor carrier regulation was applied to both the U.S. and Canadian carriers in an even handed and nondiscriminatory fashion, although Canadian restrictions were tighter than those in the United States. In September of that year, Congress passed the Bus Regulatory Reform Act of 1982, Article 6 of which authorized a two year moratorium on the issuance of operating authority to carriers domiciled, owned or controlled in Canada or Mexico. Under the legislation, the President could lift the moratorium if he deemed it in the national interest to do so. In November 1982, letters of understanding were signed between the Canadian ambassador to the United States and the U.S. Trade Representative which established economic and administrative guidelines for jointly resolving problems which have or will arise in transborder trucking. On November 12, 1982, President Reagan lifted the moratorium on Canadian entry in the U.S., and the ICC began processing some 400 pending applications.319 A bilateral consultative mechanism was established which has met annually since, alternatively in Ottawa and Washington, D.C.

In the wake of this confrontation, and taking a philosophical lead from their neighbors to the south, many of the Provinces began to liberalize entry in the early 1980s. A number of U.S. carriers seized this opportunity to expand operations in Canada, both by filing applications with the Provincial boards for new operating authority, and by purchasing Canadian truck lines. Since 1980, almost 3,000 motor carrier operating permits have been issued to U.S. carriers.320 By the time the MVTA has been promulgated in 1987, a number of large U.S. motor carriers were already established in Canada.

By 1988, two thirds of Canadian carriers operating across the common border reported that they faced more competition by U.S. carriers in this market.321 Domestically, one in five Canadian carriers had experienced more competition from U.S. carriers, particularly in Ontario, Quebec and Manitoba.322 In its 1988 report, Transport Canada noted:

Canadian carriers are concerned about sustained price competition from

318. id. at 13.
319. id. at 27.
320. 1988 ANNUAL REVIEW, supra note 240, at 42.
321. id.
322. id. at 43.
large scale U.S. carriers (especially in respect to volume discounts). . .

Because U.S. carriers do not have to penetrate deeply into Canada to access the major markets, they can draw on domestic U.S. traffic to balance headhaul/backhaul loads. In reaction, a number of Canadian firms have made greater use of U.S. based operations and have set up operations in the United States to serve the transborder market.\footnote{323}

With 90% of Canadians living within 100 miles of the United States, LTL terminals in the U.S. can easily expand to serve Canadian points.

Tariff and investment barriers for most economic sectors were eliminated by the Canada-United States Free Trade Agreement, signed on August 1, 1988.\footnote{324} Transport services were omitted from the FTA because of the concern of the U.S. maritime industry with Jones Act protections afforded labor. But with promulgation of the U.S. Motor Carrier Act of 1980 and the Canadian MVT A in 1987, the net effect is deregulation on both sides of the common border — relatively open entry by Canadian firms into U.S. markets, and by U.S. firms into Canadian markets (although immigration laws restrict labor somewhat).

With the conclusion of the new Canadian-United States Free Trade Agreement, traffic patterns which have traditionally been east-to-west and west-to-east will shift and be dominated in the long run by traffic patterns which are north-to-south and south-to-north. In 1989, the two nations exchanged $180 billion in goods.\footnote{325} We are each others largest trading partners. Trade with Canada accounted for 22% of the United States' exports and 19% of its imports.\footnote{326} In contrast, trade with the United States accounted for 72% of Canada's exports and 66% of its imports.\footnote{327} For Canada, with one-tenth the population of the United States, the FTA will have a more profound impact. It is anticipated that the FTA will increase U.S. GNP by one-half a percentage point and create 750,000 jobs, while it will increase Canadian GNP by 2.5% and add 250,000 jobs.\footnote{328}

If the largest firms are ultimately to dominate North American transport on both sides of our common border — and they likely will — one must fear that Canadian transportation in the motor carrier sector, now dominated by Federal Industries Transport Group, CP Trucks Group and TNT Canada,\footnote{329} may ultimately come to be dominated by firms headquar-

\footnote{323. G. BLANCHARD & L. CLAVEL, supra note 317, at 100.}
\footnote{324. Feder, Unfinished Business with Canada, N.Y. Times, Oct. 8, 1989, at 4F.}
\footnote{325. Id.}
\footnote{326. Id.}
\footnote{327. Id.}
\footnote{328. Lockwood & Howarth, The Top 100, TODAY'S TRUCKING, Sept. 1989, at 19, 20.}
\footnote{329. EXTERNAL AFFAIRS CANADA, CANADA-USA THE RELATIONSHIP (1989). Although the U.S. is the single most important destination for Canadian foreign investment, Canada is the fourth largest investor in the United States.}
tered in the United States — United Parcel Service, Yellow, Consolidated Freightways and Roadway. Canada is the nation which accounts for the single most significant target of U.S. investment abroad, or one-fifth of all U.S. foreign direct investment. While the FTA does not liberalize free trade in transportation, the net effect of deregulation in the United States in the 1977-80 period, and in Canada under the 1987 federal legislation, is the same.

An interesting dimension of this problem involves national security. If one looks at the major infrastructure industries, one sees a long history in more nations, including the United States, of prohibiting foreign ownership. This is true in communications and energy; cabotage legislation has also prohibited dominant foreign ownership in the major transportation industries of airlines and ocean shipping. Imagine what problems might have existed in 1938 if Lufthansa and Japan Airlines had been the dominant air carriers in the United States. The United States has never promulgated cabotage legislation in the surface transport modes, presumably because foreign ownership has never been a significant potential problem. However, one wonders whether the United States would tolerate foreign ownership of its domestic transport industry. That is a question that Canada must now confront. And it will undoubtedly be a difficult one between friends as strong as these.

J. SUMMARY AND CONCLUSIONS

In the United States, unlimited entry and rate deregulation has created excessive capacity, declining productivity, destructive competition, discriminatory pricing, predatory behavior, inadequate returns on investment, a deterioration in safety, a decline in wages, a deterioration in labor-management relations, an enhanced number of bankruptcies, mergers, and acquisitions, and, in the long term, unprecedented concentration. The motor carrier industry in the United States is becoming dominated by a very small number of extremely large firms. Today, much of North America is dominated by its four largest trucking companies — United Parcel Service, Yellow, Consolidated Freightways, and Roadway. In the long-term, deregulation appears to have created an oligopoly of megacarriers providing highly discriminatory pricing, as smaller firms fall into the social Darwinist abyss of bankruptcy. In the interim, the smaller firms endanger the safety of those with whom they share the highways.

Why has deregulation failed to achieve much of what it has promised? Deregulation's proponents assured us that, if we were to free the transport market of the dead hand of regulation and replace it by Adam

330. P. DEMPSEY, supra note 238, at 129-69.
Smith's invisible hand, we would enjoy marginal cost pricing and near-perfect competition in a healthy, competitive environment.

Deregulation failed because it was a theory based on false assumptions. In theory, regulation distorted efficiency. The transportation industry was thought to be naturally competitive. It was thought to have no economies of scale or scope of consequence. It was believed that there were no economic barriers to entry of significance except by regulatory authorities. It was thought that, if incumbent firms enjoyed market power and raised prices to supra-competitive levels, new entrants would be attracted to these markets like sharks to the smell of blood. This was, in essence, the theory of contestable markets which was premised on the notion that the presence or threat of new entry would restore the competitive equilibrium. It was also predicted that destructive competition would not occur. But what we have seen under deregulation is unprecedented losses, a high number of bankruptcies, a shakeout of many small producers, an industry which is highly concentrated, and one in which there has not been significant new entry.

The theory of contestable markets has not been sustained by the empirical evidence. Leaseway was the only major carrier to enter the less-than-truckload sector of the industry in the United States, and it exited after several years of significant losses.\(^{332}\) There appeared to be significant economies of scale, scope, and density in the trucking industry. The LTL section requires a significant multi-million-dollar investment in a network of terminals, a large number of employees, and skilled management.\(^{333}\) Therefore, barriers to entry in the less-than-truckload sector are very high. Economies of scale exist in terms of the terminal networks which are required by these very large firms.

Deregulation's proponents also did not foresee the monopsony power of large shippers and the high level of discrimination it creates. This overwhelming strength of large carriers and large shippers had distorted the market for the sale of transportation services in a way which is antithetical to notions of achieving allocative efficiency.

Only prudently administered economic regulation can accomplish both economic and social goals deemed to be in the highest public interest. Among the economic goals are the prevention of the distortions created by imperfect competition. Regulation can avoid the regressive wealth transfers created by market power, including large shipper's monopsony power to unilaterally dictate rates which are noncompensatory. Additionally, regulation can ameliorate the market power of large carriers, preventing them from charging excessively high rates to small shippers.

\(^{333}\) MVTA, *supra* note 240, Part V, art. 35.
and engaging in predatory practices against competing carriers. Regulation can also avoid the problem of externalities, which manifests itself in transportation by the impact of inadequate profits upon highway safety, and the discriminatory pricing and service provided to small communities.

In addition, regulation can accomplish a number of important social goals. It can engender a regime of cross-subsidization providing for equality of access to all shippers and to all communities, large and small. Regulation can create a geographic distribution of opportunity for economic growth spread over a larger and more diverse group of participants, thereby enhancing pluralism. It can ensure that small and remote users enjoy the same access to the broader market for the sale of goods as do large firms, thereby enhancing competition in that broader market for the sale of goods.

Transportation is part of the broader infrastructure which is the foundation for economic growth. In most nations, that infrastructure (communications, energy, and transportation) is owned, subsidized, or regulated by government. Only in North America have we entered the Brave New World of deregulation and the highly imperfect economic environment that it creates. Most nations view the infrastructure as an essential foundation for economic growth, and therefore, distortions in it cannot be tolerated. It is for that reason that these industries are treated differently from other sectors of the economy. There is also a strong public interest in motor carriage because these firms are users of a public resource — highways — which are shared by nearly all citizens. If carriers are to use this scarce public resource, they have traditionally been required to do so in a way that achieves broader social goals.

The net impact of deregulation is that the social objectives for which regulation has traditionally been a catalyst have been abandoned. We have left the industry and the public it serves to a highly imperfect market which has created gross distortions between large and small firms. The result is that the larger users of the system (the large shippers) in the short run, and the larger providers of the service (the large carriers) in the longer run, are its principal beneficiaries. Small shippers, small communities, and small transportation firms are clearly disadvantaged in an unregulated environment.

The same problems which exist today in a deregulated trucking environment are those which existed in the 1930s prior to regulation and differ only in magnitude. In the 1930s, the world was ravaged by the worst economic depression of this century; during the early 1980s, the economy was struggling. After the recession, the economy has much improved. Yet, the same parallels exist between destructive competition in the 1930s preceding regulation and the destructive competition in the 1980s following deregulation. A nation that does not learn from its history
is doomed to repeat it. The United States has an extremely short memory, and is prone to reliving its past. Canada can learn from the mistakes we make south of our common border, if only it will see them.

The MVTA calls for the Minister of Transport to undertake a comprehensive review of the impact of the reverse-onus entry test in 1991. Transport Canada has already begun to prepare the data necessary to sustain the success of the government's policy. Officials in Transport Canada were quite candid in interviews with the authors, foreseeing major Canadian motor carrier bankruptcies and searching for rationales (such as "bad management") to blunt criticism that deregulation was to blame. They were envious of the ability of the U.S. Department of Transportation (DOT) to lay the blame of widespread U.S. motor carrier bankruptcies on the recession of the early 1980s. One fears that Transport Canada will prepare the same kind of whitewash reports and studies of Canadian deregulation that the DOT prepared of the impacts of U.S. deregulation during the last decade. Political ideology too often prevails over truth.

Although the five-year transition period contemplated by the MVTA has been collapsed into one, the impact of Canadian deregulation is not likely to be felt sharply in the next year or two, for many Provinces began to liberalize entry early in the 1980s, and rates in Canada have never been as tightly regulated as in the United States. Thus, the impact of deregulation in Canada must be viewed as a phenomenon which in some Provinces is well advanced, with lots of entry, acquisitions and mergers already having occurred. Some U.S. carriers have been present and growing in Canada for years.

Of course, if U.S. carriers should come to dominate Canadian trucking, Canada could always shut the door, for transportation was intentionally excluded from the Canada-United States Free Trade Agreement. In the last analysis, that is Canada's trump card should this grand experiment in free market ideology turn out not to be as lovely as that depicted in economics textbooks.

V. DEREGULATION AND THE BUS INDUSTRY

In the United States, the rate wars, bankruptcies, a deteriorating margin of safety, and consumer exploitation coalesced in the mid-1930s to prompt federal regulation of the bus industry. In promulgating the Motor Carrier Act of 1935, Congress added trucking and bus companies to the jurisdiction of the Interstate Commerce Commission (ICC). Destructive

335. 49 U.S.C. § 10922 et seq.
competition abated, and for the half century which followed, bus service was ubiquitously available throughout the nation at a price which was "just and reasonable." Service was safe and dependable to large and small communities throughout the nation.

As in telephone regulation, there was some measure of "cross subsidization" performed under the regulatory umbrella of the U.S. Interstate Commerce Commission (in interstate transport) and the State Public Utility Commissions (PUCs) (in intrastate transport), with more lucrative, denser traffic lanes paying a premium above marginal costs to subsidize rural and small community service. With the disintegration of the passenger railroad system, buses became the only public means of transport to or from tens of thousands of communities across the nation.

With the laissez faire crusade sweeping railroads (with promulgation of the 4-R Act of 1976 and the Staggers Rail Act of 1980), airlines (with the enactment of the Air Cargo Deregulation Act of 1977 and the Airline Deregulation Act of 1978), and trucking (following a biased construction of the Motor Carrier Act of 1980), the buses became the latest casualty of free market theory.

The Bus Regulatory Reform Act of 1982 (BRRA) significantly liberalized entry, exit and pricing of the U.S. bus industry, and largely preempted the states.\textsuperscript{336} Paradoxically, while the BRRA was premised on the notion that deregulation would enhance competition, the result has been a higher level of concentration than has ever existed in the industry, poorer returns than have ever been realized, and a large and growing number of small community abandonments.

The BRRA liberalized entry by removing the requirement that applicants prove "public convenience and necessity," leaving them with the obligation to establish only that they are "fit, willing and able" to provide the proposed operations. A protester must then prove that issuance of the authority sought will not be in the public interest.\textsuperscript{337} Abandonments became easier too. Moreover, industry proposed intrastate abandonments and price increases denied by the State Public Utility Commissions could now be appealed to the Interstate Commerce Commission, where they were almost always reversed.

In the first year under the BRRA, the bus industry announced termination or reductions of service at 2,154 communities.\textsuperscript{338} The ICC estimated that 1,045 communities that lost service in the first year of deregulation had no alternative intercity transportation.\textsuperscript{339} By late 1986, 4,514 com-

\textsuperscript{337} U.S. DEPT. OF AGRICULTURE, RECONNECTING RURAL AMERICA 20 (1989) [hereinafter RECONNECTING RURAL AMERICA].
\textsuperscript{338} Id.
\textsuperscript{339} Letter from ICC Chairman Heather Gradison to Senator Larry Pressler (Sept. 8, 1986).
munities had lost bus service, while only 896 had gained it. The big losers were small communities—3,432 of the small towns which lost service had a population of 10,000 or less.\textsuperscript{340} This loss of service falls particularly hard on nonmetropolitan and rural populations, which have a higher percentage of children and elderly who need access to public intercity transport, than do urban areas.\textsuperscript{341}

Who suffers when bus service deteriorates or becomes more expensive? Individuals in the lowest income groups, people living in rural areas, and the young and elderly rely disproportionately upon buses than any other mode of transportation.

During 1977, the last year the U.S. Department of Commerce performed a travel survey, 30\% of all intercity bus passenger miles were traveled by individuals living in rural areas, compared to trains (20\%) and airlines (15\%); families earning less than $10,000 a year accounted for 45\% of intercity bus passenger miles, compared to trains (25\%), automobiles (18\%), and airlines (15\%);\textsuperscript{342} people under the age of 18 or over the age of 64 accounted for half of intercity bus passengers, compared to automobiles (33\%), railroads (25\%), and airlines (17\%).\textsuperscript{343}

The isolation of rural America has had a pernicious social and economic impact.\textsuperscript{344} The U.S. Department of Agriculture recently summarized the impact of deregulation upon small towns and rural communities:

Many rural residents no longer have intercity public transportation available to them. It is no longer possible "to get from here to there." The combined effect of rail, air, and bus deregulation has simply removed many rural areas from the intercity transportation network. In those small communities where some form of intercity transportation is still available, the cost of travel has risen, sometimes dramatically. . . .

The net result for many rural residents is increased isolation from society at large, as linking with other communities becomes more and more difficult. An alternative for some elderly people is to move away from their homes in rural areas to an urban area—where they no longer have the support of their local community network and where they may require the support of human services agencies to remain independent. . . .

\[\text{There may be an incremental addition to a larger trend toward increased isolation and rising costs for rural communities. As costs rise, businesses close, thereby reducing the number of services available locally.}\]

\textsuperscript{340} See \textit{Reconnecting Rural America}, \textit{supra} note 337, at 8.

\textsuperscript{341} The trend continues. A 1988 survey by Greyhound Lines, Inc. revealed that 44.8\% of its passengers were from families which earned less than $15,000 a year. R. Nathan, Federal Subsidies for Passenger Transportation, 1960-1988: Winners, Losers, and Implications for the Future 17 (1989) [hereinafter R. Nathan].

\textsuperscript{342} Id. at 17-20.

\textsuperscript{343} See Dempsey, Rate Regulation and Antitrust Immunity in Transportation: The Genesis and Evolution of This Endangered Species, 32 Am. U.L. Rev. 335, 343-44 (1983).

\textsuperscript{344} \textit{Reconnecting Rural America}, \textit{supra} note 337, at 26-27.
And as the number of services decline, residents are forced to travel farther to access medical care, shopping, employment opportunities, and social and recreational outlets. As people travel to meet basic needs, the cycle of decline is reinforced as individuals combine their trips to the larger community to include the doctor, the shopping center, and the theater—and bypass the local business as an additional, unnecessary stop. Eventually, population declines as access to basic services becomes too difficult or too costly for rural residents to sustain.\(^{345}\)

The U.S. intercity bus network is shrinking under deregulation. Peaking at 27.7 billion intercity passenger miles traveled in 1979, it has fallen steadily each year since to 23 billion passenger miles in 1987.\(^{346}\)

Prior to its deregulation, industry officials predicted that deregulation would result in drastic service reductions to small communities. Harry Lesko, President of Greyhound of Arizona, said that "Eighty-nine percent of our routes are subsidized by the bread-and-butter primary routes... \([I]\)f we are to keep our lines running and the scheduled miles operating on the primary routes to satisfy the high-density population factors, the rural areas are going to have to suffer because they're straining the main line system."\(^{347}\) Similarly Charles Webb, President of the National Association of Motor Bus Owners, insisted that "[t]he one conclusive argument against removal of controls on entry by motor carriers of passengers stems from their obligation to provide service to thousands of small cities and towns and to vast rural areas without profit or at a loss, and from the fact that it would be unconscionable either to permit new entrants to skim the cream of traffic or to authorize existing carriers to discontinue bus service to thousands of communities having no other form of public transportation."\(^{348}\)

Moreover, the loss of bus service means the loss of the most fuel efficient and least pollutive mode of transport.\(^{349}\) In 1985, the various modes consumed the following amounts of fuel per passenger mile:

\[^{345}\text{R. Nathan, supra note 341, at Appendix B, Table B-1.}\]
\[^{346}\text{Senate Comm. on Commerce, Science and Transportation, 95th Cong., 2d Sess., Intercity Bus Service in Small Communities 17 (1978).}\]
\[^{348}\text{R. Nathan, supra note 341, at 20-24.}\]
\[^{349}\text{Id. at 20.}\]
FUEL CONSUMPTION BY MODE

<table>
<thead>
<tr>
<th>Mode</th>
<th>Btus per passenger mile</th>
</tr>
</thead>
<tbody>
<tr>
<td>Buses</td>
<td>1,323</td>
</tr>
<tr>
<td>Trains</td>
<td>2,800</td>
</tr>
<tr>
<td>Automobiles</td>
<td>4,040</td>
</tr>
<tr>
<td>Commercial Aviation</td>
<td>4,376</td>
</tr>
<tr>
<td>General Aviation</td>
<td>11,339</td>
</tr>
</tbody>
</table>

Despite the freedom to raise prices and leave unprofitable markets created by deregulation, the bus industry suffered unprecedented losses under deregulation. Industry operating ratios exceeded 96.9 every year between 1982 and 1986.\(^{350}\) Part of this was due to "cream skimming" by new entrants which focused their operations on the denser, higher revenue traffic lanes. Excessive capacity in dense markets deprived carriers of the revenue needed to cross-subsidize weaker markets. Another part still was prompted by the impact of the airline rate wars of the early 1980s, created by the destructive competition unleashed by the Airline Deregulation Act of 1978. Supersaver air fares were luring passengers away from the bus stations and into airports.\(^{351}\) Even charter and tour deregulation had a deleterious effect upon carrier profitability. Jeremy Kahn painted the following portrait of the empirical results of deregulation:

\[^{350}\]R. Nathan, supra note 341, at Appendix C, Table C.

\[^{351}\]Reconnecting Rural America, supra note 337, at 21.

Regardless of the number of efficient management programs which are instituted, regardless of the modernization of maintenance facilities and customer service facilities, and regardless of computerization of record keeping and billing, many carriers are faced with a close-to-being unbearable squeeze on their profits. . . .

Many carriers are today operating aging fleets of equipment, with models costing the then significant amount of $155,000 now replaceable only with comparable models which cost twice as much.

In many instances, only new entrants, highly leveraged, and barely able to make lease payments on these expensive coaches, enter the charter market and provide fierce price competition, anxious only in the short run to
meet their leasing obligations, thereby further exasperating this problem.\textsuperscript{352}

Between 1981 and 1986, Greyhound in the United States experienced severe losses;\textsuperscript{353} because of its anemic performance and labor difficulties, it was placed on Standard & Poor’s “watch list” in 1983.\textsuperscript{354} In 1986, Greyhound of Arizona sold its domestic operations to an investment group led by Fred Curry, a former officer, for $350 million.\textsuperscript{355} The following year, Greyhound acquired its rival Trailways, for $80 million, and the U.S. bus duopoly became a monopoly.\textsuperscript{356} Recognizing that Trailways was on its death bed, the U.S. Department of Justice acquiesced and withheld antitrust opposition under the “failing company” doctrine.\textsuperscript{357} That single firm today accounts for more than 85% of the operating revenues of the ten largest carriers.\textsuperscript{358}

While deregulation initially increased price competition by flooding the market with excess capacity, it caused the industry’s profit margin to plummet, a large number of carriers to fail, or merge, thereby creating unprecedented levels of concentration. During that time, small and rural communities lost bus service or faced extreme price discrimination.\textsuperscript{359}

Thus, deregulation of the U.S. intercity bus industry has created an anemic monopoly providing poorer service than before deregulation. Even Alfred Kahn, the guru of deregulation, has acknowledged that bus deregulation was a threat to small communities, whose lifeline is the intercity operator. Therefore, had he been at the helm of government, he probably would not have deregulated the bus industry.\textsuperscript{360}

The public has suffered unduly in the United States as free market economists played havoc with national transportation policy. Laissez faire has made impossible the achievement of the broader social and equity objectives of ubiquitous intercity passenger transportation linking all to the infrastructure, even those living in remote communities, for it has

\textsuperscript{352} J. Kahn, The U.S. Bus Industry Seven Years After Deregulation 16-17 (address before the Canadian Transport Lawyers Ass’n, Nov. 18, 1989) [hereinafter J. Kahn].

\textsuperscript{353} GREYHOUND CORP., ANNUAL REPORT 2 (1982); GREYHOUND CORP., ANNUAL REPORT 1 (1986).


\textsuperscript{358} J. Kahn, supra note 352, at 14.


obliterated the delicate balance of cross-subsidies which only responsibly administered economic regulation can provide.

In Canada, the Motor Vehicle Transport Act of 1954 essentially granted the provincial highway transport boards the authority to regulate extra-provincial bus transport in accordance with provincial laws and regulations. Although the Motor Vehicle Transport Act, 1987, significantly liberalizes extra-provincial and international trucking regulation, it leaves companion bus regulation as it was under the 1954 Act, with one addition: the Governor in Council may, upon the recommendation of the Federal Minister of Transport after consultation with the provincial governments, promulgate safety regulations. Thus inter-provincial and extra-provincial regulation remains under the jurisdiction of the Provincial motor carrier transport boards, and most continue to require that new applicants demonstrate that new operations would be consistent with the "public convenience and necessity."

Canada thus can avoid the serious problems of deregulation caused by unlimited entry. Its provinces can take a more moderate, balanced approach, one which recognizes that the U.S. experiment with transport deregulation has created significant problems antithetical to the public interest.

VI. CONCLUSIONS

"Trans-Canada Air Lines was established to carry the mail . . . there were still plenty of people around in 1937 who would no more have set foot on an aeroplane than they would willingly have stepped into a bear trap. And there were those on both sides of the Atlantic who felt that no matter how intrepid the potential airline passenger might be, he had no place aboard a machine designed to speed the mail. 'Mails may be lost but never be delayed. . . . and passengers may be delayed but must never be lost.'"


"By the time we're ready to celebrate the bicentennial of passenger rail in 2036, much will have changed in our world. The steel wheel on the steel rail may well be a thing of the past. But the pioneering vision that built our first railways against incredible odds will service well in the 21st century and beyond."

—VIA Rail Canada, Rails Across Canada, 127 (1986).

Transportation systems in Canada grew under conditions of benevolent protection and sponsorship by a development-minded government in Ottawa. While the United States opted for private operation of its railroads, airlines and motor carriers, most other nations opted for nationali-
zation of these modes. Canada has relied for most of the twentieth century on competition between a major Crown and a large-scale private carrier. Canada was content to let this duopoly serve most of its transportation needs, and extend this competition to hotels and telegraph services.

The 1970s brought about a greater coordination of Canadian transport facilities. It also began the unloading of social services from the carriers upon the government. VIA Rail was implemented to take the passenger burden away from Canadian National and Canadian Pacific. Canadian National, in turn, was restructured to operate more like a conventional railroad, while local commuter services were turned over to the provinces. Air Canada was relieved of many obligations to serve northern communities, and Canadian Pacific Airlines was permitted more competitive service on the transcontinental run. Regional airlines emerged to handle local traffic, connecting with Air Canada and CP Air at major hubs. Bus service took the form of Greyhound of Canada as the principal east-west carrier, with other regional carriers operating in the various provinces. (Buses are the one form of transport whose regulatory regime has not been changed.)

The 1980s was the decade wherein the United States attempted a massive experiment in deregulation of transportation as well as other regulated industries. Later, two administrations in Canada decided that the deregulation route was the way for Canada to go as well. Deregulation in the United States was intended to bring more competition, but in many cases it ended in oligopoly. Much of the same process occurred in Canada, particularly in aviation. The principal Canadian private airlines were all merged into Canadian Airlines International. Air Canada has now been privatized. VIA Rail has been downsized, and the government is looking for private buyers to take over the pieces as an alternative to abandonment. The two major freight railroads are now being rationalized. Canadian Pacific has taken its trackage in the Maritimes and placed it with a subsidiary; Canadian National has abandoned its trackage in Prince Edward Island and Newfoundland. Motor carriers are facing increased competition from large U.S. carriers and oligopolistic trends are being seen in the Canadian trucking industry. After a five-year shakeout period, provincial control of extraprovincial trucking will be a nullity. With the implementation of the Canada-U.S. Free Trade Agreement, traffic patterns will increasingly shift from east-west to north-south. Ultimately, that may lead to growth of a handful of dominant North American motor megacarriers.

The twin themes of deregulation and privatization have changed the face of Canadian transport and its regulatory and statutory controls. Enactment of the Transportation Act, 1987 was the culmination of the drive
to replace the Canadian regulated duopoly with a freewheeling system modeled after that south of the 49th parallel. It represents a faith that a system which developed in a far more densely populated nation will suffice for a Canada of vast expanses and few alternative transportation facilities. The long history of multimodal transportation systems owned by the railways represents a different face of transportation development in Canada; presumable that history is set aside in hope that new carriers will come to take their place. Cross-subsidization, a necessity for developing transport facilities in the remote portions of the country, is now a thing of the past.\(^{362}\) As in the United States, concern with government inefficiency may also have been a motivating factor, and certainly was a factor in the radical restructuring of VIA Rail.\(^{363}\)

The 1990s will be a period wherein a largely deregulated Canadian transportation system faces a similarly deregulated system in the United States. During this decade, the Free Trade Agreement between the two countries will be phased in, gradually eliminating all tariffs, easing non-tariff trade barriers and encouraging the integrations of markets on the North American continent. At the same time, both Canadian and American rail, air and truck regulations have been greatly eased. Is the next logical step the blending of the two nation’s transport networks with complete continental deregulation?

As it happens, transportation services are not included in the Free Trade Agreement. Pressured in part by U.S. maritime interests and border state congressmen, Canada agreed in 1987 to drop the transportation annex proposed to be appended to the Fair Trade Agreement. American sailors feared repeal of the Jones Act, which limited coastwide trade to U.S. bottoms, and American airlines, reeling from deregulation, feared the easing of cabotage restrictions. Under pressure from his negotiators, Prime Minister Mulroney agreed to drop transportation from the free trade legislation, and the Canadian Parliament complied.\(^{364}\)

But mutual deregulation has brought many of the economic effects of


\(^{363}\) See Gormick, VIA’s Cuts Stun Canada, RAILWAY AGE, Nov. 1989, at p. 46. (The author points out that for roughly the same subsidy, Amtrak operates twice as many trains and carries three times VIA’s ridership of 6.8 million passengers. Amtrak has re-equipped its system, while VIA has only purchased some LRC trains for corridor service and 59 new locomotives, the latter in the last three years. Furthermore, VIA is top-heavy, with one manager for every 3.5 employees.)

\(^{364}\) Solomon, Canada Seen Anxious To Re-Insert Transportation Annex in Trade Pact, TRAFFIC WORLD, November 6, 1989, at 32.
free trade to Canada’s transportation community anyway. U.S. carriers now have a better chance at operating within Canadian provinces. Since some states (New York, Michigan and Ohio, for example) still have strict standards about entry into intrastate trucking, Canadian members of Parliament are now wondering if the U.S. got the better of the deal, and are openly campaigning for an annex to the Free Trade Agreement which would give them transportation access to the greater U.S. market.

Perhaps, a limited amount of cabotage in aviation would give competition to what appears now to be an airborne oligopoly. Currently, there are routes in Canada which are served by only Air Canada or Canadian Airlines. Much of the upper Great Plains is only served by Northwest Airlines. (Aspen Airways, operating as United Express under a special bilateral arrangement between the Canadian and U.S. governments, cancelled its service between Denver, Grand Forks and Winnipeg in December 1989. Northwest is now the only carrier offering transborder service out of Winnipeg). Such a move, even one which merely allowed a carrier to fill in empty seats on the other side of the border, would be a positive move toward bringing competition to the skies — the stated purpose of deregulation. The last decade of the twentieth century will bring either a sober second look at what transport deregulation has wrought, or the liberalization of Canadian transport to participate in a continent-wide common market with U.S. carriers.365

365. The authors would particularly like to thank the Government of Canada, the Department of External Affairs, for an Institutional Research Grant which enabled them to travel to Canada to cover late-breaking legislative and regulatory developments in the preparation of this article.
Airline Globalization: A Canadian Perspective

CAROLYN HADROVIC*

I. INTRODUCTION

Today, code-sharing arrangements between Canadian airlines are commonplace in domestic and transborder markets. In the 1990s and beyond, code-sharing will play a role in the competitive strategies of international airlines, unless the world community adopts a code of conduct on computer reservation systems. Since traffic can be diverted from a flag carrier, these arrangements will likely be a contentious issue in bilateral negotiations, particularly where one nation fears “globalization”. But, what is code-sharing? Code-sharing is a marketing arrangement whereby one airline’s designator code is shown on flights operated by another airline. Two-letter designator codes are provided by the International Civil Aviation Organization to identify the world’s airlines on passenger tickets, airport information boards, computer reservation systems and airline guides.

The purpose of this paper is two-fold. First, it provides an understanding of code-sharing. Second, it provides a general analysis of the opportunities and challenges for Canadian carriers in the international market.

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The paper is organized as follows: Section 2 outlines the policy position of the Canadian and the U.S. government as well as the European Economic Community, while section 3 discusses the ways in which an international code of conduct could become legally binding. Section 4 then describes existing code-sharing operations. Sections 5 and 6 discuss the advantages and disadvantages for airlines respectively, while section 7 discusses the disadvantages for consumers. Finally, sections 8 and 9 analyze opportunities and challenges for Canadian carriers in the international market respectively.

II. GOVERNMENT POLICY

A. CANADA

In 1984, Canadian Pacific Air Lines1 (CP) and AirBC established the first domestic code-sharing arrangement whereby the "CP" code was shown on AirBC's flights between Vancouver and other British Columbian points. Since that time, code-sharing has become an essential element of marketing alliances between regional and large carriers in the Canadian airline industry.2

Quite surprisingly, the Canadian government has yet to issue a policy direction with respect to the use of shared airline designator codes. The policy branch of Transport Canada, however, is currently formulating a proposal which should be released by the summer of 1990. If the proposal is adopted, a Ministerial direction would then be referred to a House of Commons Standing Committee. Although subsection 23(2) of the National Transportation Act, 19873 (NTA) is vague, the Committee would likely hear submissions from interest groups and make recommendations to the Cabinet.

In the interim, the National Transportation Agency (Agency)4 intends to scrutinize code-sharing operations pursuant to section 18 of the Air Transportation Regulations which impose the following licensing conditions:

(a) the licensee shall, on reasonable request therefor, provide transportation in accordance with the terms and conditions of the license and shall furnish such service, equipment and facilities as are necessary for the purposes of that transportation;

(b) the licensee shall not make publicly any statement that is false or mis-

1. In December 1986, PWA Corporation purchased Canadian Pacific Air Lines, who now carry on business as Canadian Airlines International.
2. Canadian Partners are Air Atlantic, CalmAir, Ontario Express and TimeAir, while Air Canada Connectors include Air Alliance, AirBC, Air Nova, Air Ontario, Air Toronto and NWT Air.
3. On January 1, 1988, the National Transportation Agency replaced the Canadian Transport Commission.
leading with respect to the licensee's air service or any service incidental thereto; and

(c) the licensee shall not operate a domestic service or an international service or represent, by advertisement or otherwise, the licensee as operating such a service under a name and style other than that specified in the license.

While no guidelines have been issued, the NTA appears to follow those proposed by its predecessor, the Air Transport Committee (ATC), in March of 1987. The purpose of the guidelines was to make the public aware of air carriers providing transportation services under a shared code.

Under section 1 of part IV of the guidelines, a Canadian and foreign air carrier could share designator codes only if the arrangement was first approved in writing by the ATC. Similarly, today, international, and not domestic, code-sharing operations require prior governmental approval. The reason behind prior governmental approval lies in protection of the interests of the public. This is accomplished through administrative means established by the ATC including, for example, "underlying route authority". The NTA may, however, grant an exemption from the statutory requirement to hold a license if route authority is provided by the Minister of Transport. In March 1990, an application by City Express for approval of a code-sharing operation with Continental Airlines, (originally denied in January), was granted by the NTA on the basis that the Minister of Transport had provided the necessary authority to the U.S. air carrier to operate air service between Toronto and Newark including connecting services via Toronto, from Ottawa and Montreal.

With respect to disclosure requirements, the operating carrier has to be identified in computer reservation systems and elsewhere. In particular, section 2 states that the identity of the air carrier actually performing the service should be disclosed: (a) prior to reservations and ticketing; (b) on passenger tickets; (c) on timetables, industry guides, electronic or manual information boards, reservation systems, and other information devices used by carriers; and (d) in media advertising.

Even though disclosure regulations have not been prescribed, both Canadian Airlines International (CAI) and Air Canada comply with these initial ATC proposals. First, all code-sharing flights are identified with an

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6. Underlying route authority means the flag carrier holds an operating license on the international route. A proposed operation will be deemed in the public interest where both applicants hold underlying route authority, and the government of the foreign applicant deals with Canada on a reciprocal basis.
8. Id.
asterisk or a circle in the airlines' timetables (eg. CP* 123). Second, a list of code-sharing flights is submitted, upon request, to the Official Airline Guide (OAG) and the ABC World Airways Guide (ABC), which also use an asterisk to identify these flights.\textsuperscript{9} Third, in both Pegasus (CAI) and Reservec (Air Canada), the flight availability screen identifies code-sharing partners of the host airline, while the direct link between the two computer reservation systems (CRSs) displays the competitor's code-sharing partners. And fourth, the identity of the operating carrier is disclosed in media advertising. However, no Canadian carrier provides disclosure on airport information boards and passenger tickets, although boarding passes identify the Canadian partner or Air Canada connector in the space reserved for class of service. In addition, airline reservation agents are not instructed to inform consumers in reservation transactions.\textsuperscript{10}

\section*{B. United States}

While a relatively new concept in Canada, code-sharing arrangements in the U.S. domestic airline industry date back to 1967. Since the move to jet aircraft was uneconomical on low-density routes, Allegheny Airlines (now USAir) turned over these routes to commuter carriers who agreed to use the "AL" code. Unlike today, the primary object was not to gain market access, but to provide replacement service. Under Civil Aeronautics Board Regulations,\textsuperscript{11} the airline retained responsibility to ensure that service was maintained on former routes. Since that time, however, deregulation coupled with technological innovations have forced airlines to seek allies. In fact, between 1984 and 1989, the number of U.S. domestic code-sharing partnerships increased from only a few\textsuperscript{12} to fifty-seven.\textsuperscript{13}

\begin{thebibliography}{99}
\bibitem{9} OAG and ABC are situated in Illinois and England respectively.
\bibitem{10} It is interesting to note that airline reservation agents tend to disclose the identity of the operating carrier when turboprop aircraft are used and the passenger is elderly. Air Canada Reservation Agent.
\bibitem{11} On January 1, 1985, the CAB was dissolved and its remaining functions were absorbed by the Departments of Transportation and Justice.
\bibitem{13} As of December 1989, U.S. code-sharing partnerships included: Aloha and Aloha Islandair; Alaska and Bering Air, ERA Aviation, Horizon, LAB, Markair, Temsco; American and Command, Executive Air, Metroflight, Nashville Eagle, Simmons, Wings West; Continental and Bar Harbour, Britt, Colorado Mountain, Resort Express, Rocky Mountain, Southern Jersey; Delta and Atlantic Southeast, Business Express, Comair, Sky West; Eastern and Bar Harbour, Metro Express; Frontier and Tatouduk; Midway and Iowa Airways, Midway Commuter; Midwest Express and Skyway; Northwest and Big Sky, Express, Horizon, Mesaba, Precision, USAir; Pan Am and Pan Am Express; TWA and Air Midwest, Jet Express, Pocono, Metro Northwest, Trans State, USAir; United and Air Wisconsin, Aspen, NPA, Presidential, Westair Commuter; USAir and Chautaugua, Commutair, Crown, Henson, Jetstream, Pennsylvania, Suburban. OFFICIAL AIRLINE GUIDE, (North American ed. December 1989).
\end{thebibliography}
Consequently, in 1985, the U.S. Department of Transportation (DOT) adopted a policy position with respect to two code-sharing issues. First, code-sharing arrangements between U.S. air carriers will not require prior governmental approval. According to DOT officials, these arrangements are "private marketing deals".14 Second, in order to protect the traveling public against deception, air carriers will have to comply with disclosure requirements set forth in section 399.88 of the Department's regulations.15 For example, code-sharing flights shall be identified with an asterisk in airline schedules, and the public shall be notified about these flights in advertising and reservation transactions. Unlike ATC proposals, disclosure on passenger tickets is not required.

With respect to international code-sharing arrangements, the DOT also indicated in 1985 that prior governmental approval will not be required so long as both the U.S. and the foreign carrier have underlying route authority.16 Soon after, U.S. Secretary of Transportation Elizabeth Dole, appeared willing to allow an arrangement wherein a foreign carrier lacked route authority. Here, Florida Express would have used KLM's code on flights between six U.S. cities and Orlando, a proposed KLM gateway. But, due to opposition from elected officials, this arrangement was not approved.17

In December 1987, the DOT changed its earlier policy position in response to a proposed code-sharing arrangement between British Airways and United Air Lines.18 The DOT's General Counsel advised the airlines that a statement of authorization was required pursuant to section 207.10 of the Regulations.19 Apparently, this decision was based on the view that code-sharing should be scrutinized separately from underlying route authority.20 United Air Lines, in turn, applied for exemption under section 416(b) of the Federal Aviation Act21 which states that an application may be approved where the DOT finds "the exemption...consistent with the public interest".

In an order dated March 15, 1988, the application for exemption was allowed because in December 1987, regulatory requirements were not

17. AVIATION DAILY, May 1, 1987, at 178.
18. British Airways proposed to code-share with United Air Lines on United's flights between Seattle and Chicago connecting with British Airways' flights between Chicago and London. British Airways has London-Chicago-Seattle permit authority, and United has domestic certificate authority for its Seattle-Chicago flights.
20. DEPT. OF TRANS., supra note 16.
clearly established, and the proposed arrangement was in the public interest. The Order further stated:

As a general policy we will require subsequent code-sharing arrangements to be filed as applications for statements of authorization for prior approval under Parts 207 or 212 of the Department Regulations.

Parts 207 and 212, which concern domestic and foreign carrier lessors respectively, authorize the DOT to issue statements of authorization if the proposed operation is in the public interest. To make that determination, the following factors are weighed and balanced:

1. The extent to which the authority sought is covered by and consistent with bilateral agreements to which the United States is a party, or should be covered;
2. The extent to which the foreign country involved deals with the United States carriers on the basis of substantial reciprocity; and
3. Whether the applicant has previously violated the provisions of this part.

Hence, in addition to disclosure and route authority, public interest factors now include the reciprocity for code-sharing operations, the overall balance of benefits, and the applicant’s prior conduct. These regulations will not apply, however, where the governing bilateral agreement provides for automatic authorization of code-sharing operations. At the present time, no such provision exists in any agreement between the U.S. and a foreign country.

It should be noted, however, that a bill entitled the Airline Enhancement Competition Act was introduced in the U.S. Senate in late 1989. As part of an attempt to reimpose elements of regulation, the Act would eliminate code-sharing and require the divesture of airline-owned CRSs. Not surprisingly, it has encountered strong opposition from industry leaders.

C. EUROPEAN ECONOMIC COMMUNITY

The European Economic Community (EEC), which is composed of

23. Id. The proposed arrangement was in the public interest for two reasons. First, the British Government had no general policy against international code-sharing operations involving points in the United Kingdom. In fact, it allowed Air Florida and British Island Airways to conduct similar services between Miami and points in Europe via London, as well as allowed a number of U.S. carriers, including American Airlines, to conduct code-sharing operations serving British points in the Caribbean. And second, since U.S. carriers would benefit significantly from arrangements involving British points, there would be a positive impact on the overall balance of benefits.
24. 14 C.F.R. §§ 207.10(g) and 212.6(b).
25. DEPT. OF TRANS. order, supra note 22.
twelve western European nations, has agreed to establish a common market for air transport by December 31, 1992. Member states have not, however, adopted an unified policy with respect to code-sharing operations. Since the outset, the United Kingdom and the Netherlands have not objected to the use of shared codes. Both countries claim that it is a private marketing right rather than a traffic right. In fact, until the fall of 1989, the only EEC air carriers conducting these operations were British and Dutch nationals; namely, Air UK, British Airways, KLM and Transavia Airlines. Other member states, in contrast, have placed restrictions on certain types of code-sharing operations. Italy, for example, prohibits code-sharing on fifth freedom routes unless the bilateral agreement provides for change of gauge rights.

Nonetheless, in June 1989, the EEC's Council of Ministers approved a code of conduct on CRSs which was drafted by the Commission, a non-partisan advisory body. It is closely modelled on the CRS code proposed by the European Civil Aviation Conference. Article 1 states that the purpose of the Code is to ensure that CRSs "are used in a fair, non-discriminatory and transparent way so avoiding their misuse and aiding fair competition between air carriers and protecting the interest of the consumers of air transport services.”

According to paragraph 2(a) of Article 5, primary display data shall not be inaccurate, misleading or based on any factor directly or indirectly related to air carrier identity. All code-sharing flights will be identified. In addition, subparagraph 2(b)(iii) states that connecting flights shall be displayed in order of minimum elapsed travel time. Hence, the rules will preclude any advantage of code-sharing, at least in the European common market.

When the Code is implemented, EEC and U.S. CRS rules will be in

27. Member States include Belgium, Denmark, France, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, United Kingdom, and West Germany.
29. The fifth freedom is the right to carry traffic from the home country to a foreign country, pick up traffic in the foreign country, and carry it to another foreign country.
30. Change of gauge rights allow an airline to use aircraft on one sector of the route which is different in capacity form that used on another sector of the route.
31. EEC COMMISSION, DRAFT COMMUNITY CODE OF CONDUCT ON CRSs (May 1988).
33. The European Civil Aviation Conference is composed of director generals from all EEC member states as well as twelve other European nations. This conference makes recommendations and resolutions which are considered by its members and often implemented as regulations. The proposed code would give priority to direct non-stop services, followed by direct stopping services and then connecting services. The last two would be displayed in order of minimum elapsed travel time.
conflict. Since U.S. carriers will not benefit significantly from code-sharing
operations involving EEC points, the DOT could prohibit EEC carriers
from conducting similar operations in the U.S. Consequently, change of
gauge or cabotage would be the only means by which EEC air carriers
could operate profitable services on low density, co-terminal routes. De­
spite the latter’s prohibition under current U.S. law, member states could,
in response, threaten to revoke U.S. fifth freedom rights on intra-EEC sec­
tors, claiming that these U.S. fifth freedom rights would amount to cabo­
tage in the common market. If the U.S. submits to EEC demands, it would
open a proverbial pandora’s box since other trading partners like Canada
would at the very least, demand similar cabotage rights on U.S. co-termi­
nal routes.

III. INTERNATIONAL CODE OF CONDUCT

Notwithstanding potentially diverse State practices, an international
code of conduct could be adopted which precludes the CRS advantage
of code-sharing. In other words, primary display data would not be based
on any factor related to carrier identity. Instead, connecting flights would
be ranked in order of minimum elapsed travel time. There are three ways
in which this code could become legally binding. Each one is discussed
in turn below.

First, the code could be adopted by an international organization
which has authority to make binding decisions. While its objects are to
foster the planning and development of international air transport, the In­
ternational Civil Aviation Organization (ICAO) is not expressly empowered
to make binding decisions. However, this authority could be inferred from

\[34\text{. For example, if an EEC carrier feeds traffic to a U.S. carrier at an EEC point, the use of
dual designator codes on the transatlantic route would no longer increase the number of EEC
originating passengers being flown by the U.S. carrier. But, the carrier could still carry more U.S.
originating passengers on domestic flights or transatlantic flights where dual designator codes
are shown on transatlantic flights or intra-EEC flights operated by the EEC carrier, respectively.}

\[35\text{. Cabotage, the eighth freedom, is the right to pick up traffic in a foreign country, and
carry it to another point in the same country.}

\[36\text{. Article 7 of the Convention on International Civil Aviation (the “Chicago Convention”) reads in part as follows: “Each contracting State undertakes not to enter into any arrangements which specifically grant...[cabotage] on an exclusive basis to any other State or an airline of any other State, and not to obtain any such exclusive privilege from any other State.” 1944 Can.
T.S. No. 36. While at least two interpretations exist, Gertler suggests that “[o]nly a deliberate
policy of a group of states to grant mutually for their airlines domestic cabotage rights and to
specifically exclude all other airlines, would not be compatible with Article 7 and would likely
create serious irritants.” See Towards a New, Rational and Fair Exchange of Opportunities for
Airlines (Montreal: Conference on EEC Air Transport Policy and Regulation and Their Implications

\[37\text{. Schwartz, Are the OECD and UNCTAD Codes Legally Binding?, 11 INT’L LAW. 529
(1988).}
other provisions of the Chicago Convention. Article 49(c) states that the Assembly, which is composed of all contracting States, has the power to "examine and take appropriate action on the reports of the Council". These decisions require a majority of the votes cast. According to Article 55(c), the reports may concern "all aspects of air transport... which are of international importance". Even if ICAO or any other organization does have such authority, the code would be unenforceable in a municipal system until the State complied with the requirements of its constitutional procedures. In Canada, for example, a declaration embodied in either a federal statute or regulation would be required because treaty obligations are not recognized as self-executing.

Second, a multilateral legal instrument on CRSs could be adopted. The instrument would be binding on the signatories as conventional international law. Again, it would be unenforceable in a municipal system until the contracting State complied with the requirements of its constitutional procedures.

Finally, the multilateral instrument could become binding on a third State as customary international law if it is comprised of settled State practice and opinio juris. In the North Sea Continental Shelf Case, the International Court of Justice held that a settled practice exists when the following three elements are present:

1. The provision concerned [is]. . . of a fundamentally norm-creating character;
2. A very widespread and representative participation. . . include[s] that of States whose interests [are] specially affected; and
3. Within the period, State practice, including that of States whose interests are specially affected, . . . [has] been both extensive and virtually uniform.

At a minimum, the signatories should include all major aviation players. If only the U.S. abstains but subsequently adopts the practice, the code would likely become binding as customary international law. However, if a different practice is followed, the code would be unenforceable against States not parties to the multilateral instrument.

39. Id. art. 48(c).
40. For a discussion on the doctrine of transformation, see H.L. KINDRED, INTERNATIONAL LAW AS CHIEFLY INTERPRETED AND APPLIED IN CANADA (1987).
42. Opinio juris means a belief that the practice is obligatory.
IV. CODE-SHARING OPERATIONS

A. TRANSBORDER ROUTES

Today, Canadian and U.S. code-sharing operations are commonplace in the transborder market. A typical arrangement involves a regional air carrier using the designator code of a major air carrier, and the two air carriers coordinating schedules to facilitate connections at a hub close to the border. In late 1988, at least twenty-seven transborder routes were operated on a shared code basis.44

Except for six routes,45 operating air carriers received automatic or discretionary approval under the Regional, Local and Commuter Air Services Agreement.46 Code-sharing air carriers, in contrast, only had permit authority on the Vancouver-Seattle route.47

Besides national alliances, in April 1990, City Express and Continental Airlines commenced a code-sharing operation on the Toronto (Island

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44. As of November 1988, the Canadian code-sharing operations were: Vancouver-Seattle, Victoria-Seattle (Air Canada and Air BC); Halifax-Boston, Yarmouth-Boston (Air Canada and Air Nova); London-Detroit, Thunder Bay-Minneapolis, Toronto-Hartford, Toronto-Cleveland (Air Canada and Air Ontario); Toronto-Allentown, Toronto-Columbus/Dayton, Toronto-Harrisburg, Toronto-Indianapolis, Toronto-Saginaw/Grand Rapids (Air Canada and Air Toronto); Halifax/Saint John-Boston (CAI and Air Atlantic); Toronto-Pittsburgh (CAI and Ontario Express); and Regina-Minneapolis, Vancouver-Seattle (CAI and TimeAir).

The U.S. code-sharing operations were: Boston-Montreal, New York-Montreal, Washington D.C.-Montreal (Delta and Business Express); Cincinnati-Toronto, Louisville-Toronto (Delta and Comair); Cleveland-London (Continental and Britt-North); New York-Hamilton (Pan Am and Pan Am Express); Seattle-Vancouver, Seattle-Victoria (United and San Juan); and Pittsburgh-Hamilton (USAir and Allegheny Commuter). OFFICIAL AIRLINE GUIDE, (North American ed. November 1988).


46. For automatic approval, five criteria must be satisfied. First, the aircraft capacity is no more than sixty passengers, and the payload capacity is no more than 18,000 pounds. Second, the city-pair is not named in the 1966 Agreement. However, the city-pair may be served if the airline operates at a secondary airport in either country. Third, at least one city has a metropolitan population of less than 500,000 in Canada, or 1,000,000 in the U.S. Fourth, the stage length does not exceed 400 statute miles to and from points in central Canada and 600 statute miles to and from all other points in Canada. And fifth, the proposed service is not already authorized to an airline of the same country. Exchange of Notes Between the Government of Canada and the Government of the United States of America Concerning Regional, Local and Commuter Air Services, 1984 Can. T.S.

47. Under section 416(b) of the Federal Aviation Act, a carrier may be exempt from the licensing requirements of § 401. Codified at 49 U.S.C. §§ 1386(b), 1371 (1988). See Eastern Air Lines' Application for Exemption to enable Bar Harbour to use the "EA" designator on services to Saint John and Halifax DEPT OF TRANS Docket No. 44052. In Canada, the Agency may order an exemption, or the Minister of Transport may issue a direction to make such an order pursuant to subsections 70(1) and 86(1) of the NTA, respectively.
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Airport)-Newark route. The regional air carrier obtained discretionary approval, while the major air carrier was granted an exemption from the requirement to hold a license.\footnote{48} To date, this is the only code-sharing arrangement between a Canadian and a U.S. air carrier. In 1986, however, Continental Airlines and CAI established a blocked space arrangement on the Canadian segment of the Houston/Dallas/Ft. Worth-Calgary/Edmonton route. This route has since been transferred to American Airlines.

B. CARIBBEAN ROUTES

Since 1985, U.S. air carriers have also conducted code-sharing operations in the Caribbean.\footnote{49} Usually, a regional and major air carrier mutually feed traffic at a U.S. point in either Florida or Puerto Rico. Subsequently, only the major air carrier’s code is shown on flights operated by the regional air carrier. While some flights originate in Puerto Rico and the U.S. Virgin Islands, a majority are from the Bahamas, the British Virgin Islands, the Dominican Republic, Guadeloupe and Martinique. For example, American Airlines has a hub in San Juan where Executive Air feeds traffic from Mayaguez, Ponce, St. Croix and St. Thomas, as well as Anguilla, Fort de France, La Romana, Point a Pitre, Punta Cana, St. Kitts, St. Maarten, Santo Domingo, Tortola and Virgin Gorda. In most cases, the major air carriers do not have certificate authority to serve the Caribbean points, but have been granted exemption authority.\footnote{50} Unlike several foreign competitors, it appears that no Caribbean government has strongly objected to these code-sharing operations.\footnote{51}

C. INTERNATIONAL ROUTES

In the international market, code-sharing is a relatively new element of foreign alliances. Although British Island Airways and Air Florida established the first arrangement in 1986,\footnote{52} only six existed at the end of 1988.\footnote{53} But, by late 1989, at least fifty-four international routes were op-

\footnote{48} Supra note 7.
\footnote{49} As of November 1988, there were six U.S. code-sharing partnerships in the Caribbean, namely, American Airlines and Executive Air, Delta Air Lines and Comair, Eastern Air Lines and Bar Harbour, Eastern Air Lines and Metro Express, Piedmont and Henson Airlines, and Trans World Airlines and Virgin Islands Seaplane. OFFICIAL AIRLINE GUIDE, supra note 44.
\footnote{51} For example, Air BVI opposed the Eastern Air Lines and Metro Express code-sharing operation, but neither the British Virgin Islands nor the British government objected to the exemption application. DEPT OF TRANS. order 86-3-44 (1986).
\footnote{52} Under this arrangement, Air Florida fed U.S. originating traffic to British Island Airways at London, and dual designator codes were shown on British Island Airways’ flights between London and Amsterdam.
\footnote{53} The international operations were: Montreal-Amman, Montreal-Jeddah (Air Canada and
erated on a shared code basis. So far, these operations have been conducted on two types of routes.

First, the code-sharing operation is conducted on the domestic sector of third and fourth freedom routes. Here, a foreign air carrier feeds traffic to a domestic air carrier at its first point of entry in the foreign country, and dual designator codes are shown on the domestic air carrier’s flights between co-terminal points. In some cases, the foreign air carrier also blocks space on domestic flights. For example, Qantas Airways purchases a minimum of ten first class seats and twenty-five coach seats on each of three specified American flights between Los Angeles and San Francisco and also Los Angeles and New York. As shown in Table 1, this type of operation has been conducted solely in the U.S. and it is likely that foreign carriers will also attempt to establish similar arrangements on the domestic sector of fifth freedom routes. In this regard, it is interesting to note that Delta Air Lines has applied for authorization to sell blocked space to Singapore Airlines on the domestic sector of the Singapore-Tokyo-Los Angeles/Dallas/Ft. Worth and Singapore-Tokyo-Los Angeles/Newark routes.

### Table 1

<table>
<thead>
<tr>
<th>Code-Sharing Carrier</th>
<th>Operating Carrier</th>
<th>Domestic Sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>British Airways</td>
<td>Enterprise Airlines</td>
<td>London-New York/Boston</td>
</tr>
<tr>
<td></td>
<td>United Air Lines</td>
<td>London-Chicago/Denver</td>
</tr>
<tr>
<td>Cathay Pacific</td>
<td>American Airlines</td>
<td>Hong Kong-Los Angeles/</td>
</tr>
<tr>
<td></td>
<td></td>
<td>San Francisco(^1)</td>
</tr>
<tr>
<td>Qantas Airways</td>
<td>American Airlines</td>
<td>Sydney-Los Angeles/San</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Francisco/New York</td>
</tr>
</tbody>
</table>


**NOTE:** (1) Proposed. AIR TRANSPORT WORLD, (October 1989), at 148.

Royal Jordanian); London-Chicago/Seattle (British Airways and United); Newark-London-Amsterdam (Continental and Transavia); New York-Budapest (Pan Am and Malev Hungarian); Sydney-Los Angeles/San Francisco/New York (Qantas Airways and American). OFFICIAL AIRLINE GUIDE, (Worldwide ed. November 1988).

54. The third freedom is the right to carry traffic from the home country to a foreign country, while the fourth freedom is the right to carry traffic from a foreign country to the home country.


Second, the code-sharing operation is conducted on the foreign sector of third and fourth freedom routes. Here, a foreign air carrier feeds traffic to a domestic air carrier at its first point of entry in the foreign country, and dual designator codes are shown on flights operated by the foreign air carrier. Both air carriers have underlying route authority, and in some cases, each air carrier operates the route under the designator code of the other air carrier. For example, CAI and Lufthansa have a blocked space arrangement on the Vancouver-Frankfurt route, and dual designator codes are shown on flights operated by both airlines. As shown in Table 2, this type of operation is conducted on at least forty-nine routes, and is not limited to any particular geographic region. The reader should be cautious, however, when referring to this table. The OAG supposedly identifies all code-sharing flights with an asterisk, and lists the flight numbers in the Abbreviations and Reference Marks section. Yet, in a number of cases, these flights are only identified by one of the following notes: leased passenger space, operated by 'X', or in co-operation with 'X'. Consequently, a number of code-sharing operations could have been overlooked.

### Table 2
**International Code-Sharing Operations Foreign Sector of Third and Fourth Freedom Routes**

<table>
<thead>
<tr>
<th>Code-Sharing Carrier</th>
<th>Operating Carrier</th>
<th>Foreign Sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>Air Canada</td>
<td>Royal Jordanian</td>
<td>Montreal-Amman</td>
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<tr>
<td></td>
<td></td>
<td>Montreal-Jeddah</td>
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<tr>
<td>Air Jamaica</td>
<td>Air Canada</td>
<td>Kingston-Toronto¹</td>
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<tr>
<td></td>
<td></td>
<td>Montego Bay-Toronto¹</td>
</tr>
<tr>
<td>Air New Zealand</td>
<td>Cathay Pacific</td>
<td>Auckland-Hong Kong</td>
</tr>
<tr>
<td></td>
<td>Qantas Airways²</td>
<td>Auckland-Adelaide</td>
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<tr>
<td></td>
<td></td>
<td>Auckland-Brisbane</td>
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<tr>
<td></td>
<td></td>
<td>Auckland-Perth</td>
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<td></td>
<td></td>
<td>Auckland-Melbourne</td>
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<tr>
<td></td>
<td></td>
<td>Auckland-Sydney</td>
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<tr>
<td></td>
<td></td>
<td>Auckland-Townsend</td>
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<tr>
<td></td>
<td></td>
<td>Christchurch-Brisbane</td>
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<tr>
<td></td>
<td></td>
<td>Christchurch-Hobart</td>
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<tr>
<td></td>
<td></td>
<td>Christchurch-Melbourne</td>
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<td></td>
<td>Christchurch-Sydney</td>
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<tr>
<td></td>
<td></td>
<td>Wellington-Brisbane</td>
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<td></td>
<td>Wellington-Hobart</td>
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<td></td>
<td>Wellington-Melbourne</td>
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<tr>
<td></td>
<td></td>
<td>Wellington-Sydney</td>
</tr>
<tr>
<td>All Nippon Airways</td>
<td>SAS</td>
<td>Tokyo-Stockholm¹</td>
</tr>
<tr>
<td>CAI</td>
<td>Japan Air Lines</td>
<td>Toronto-Hong Kong</td>
</tr>
<tr>
<td></td>
<td>Lufthansa</td>
<td>Toronto-Tokyo</td>
</tr>
<tr>
<td></td>
<td>SAS</td>
<td>Vancouver-Frankfurt</td>
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<tr>
<td></td>
<td></td>
<td>Toronto-Copenhagen¹</td>
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<td></td>
<td></td>
<td>Toronto-Stockholm¹</td>
</tr>
</tbody>
</table>
Table 2 (cont.)

<table>
<thead>
<tr>
<th>Code-Sharing Carrier</th>
<th>Operating Carrier</th>
<th>Foreign Sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cathay Pacific</td>
<td>Air Mauritius</td>
<td>Hong Kong-Mauritius</td>
</tr>
<tr>
<td></td>
<td>Air Niugini</td>
<td>Hong Kong-Port Moresby</td>
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<tr>
<td></td>
<td>Air New Zealand</td>
<td>Hong Kong-Auckland</td>
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<tr>
<td></td>
<td>Garuda Indonesia</td>
<td>Hong Kong-Denpessar</td>
</tr>
<tr>
<td>Continental Airlines</td>
<td>SAS⁵</td>
<td>Newark-Copenhagen</td>
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<tr>
<td></td>
<td>Transavia Airlines</td>
<td>Newark-Oslo</td>
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<td></td>
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<td>Newark-Stockholm</td>
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<tr>
<td></td>
<td></td>
<td>Newark-Amsterdam⁴</td>
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<tr>
<td>Japan Air Lines</td>
<td>Air France</td>
<td>Tokyo-Papeete</td>
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<tr>
<td></td>
<td>Air New Zealand⁶</td>
<td>Tokyo-Auckland</td>
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<td></td>
<td>Allitalia</td>
<td>Tokyo-Christchurch</td>
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<tr>
<td></td>
<td>CAI</td>
<td>Tokyo-Milan</td>
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<tr>
<td></td>
<td>Qantas Airways</td>
<td>Tokyo-Rome</td>
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<td></td>
<td></td>
<td>Tokyo-Toronto</td>
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<tr>
<td></td>
<td>Swissair</td>
<td>Tokyo-Zurich</td>
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<tr>
<td></td>
<td>Thai Airways Intl.</td>
<td>Nagoya-Bangkok</td>
</tr>
<tr>
<td>KLM</td>
<td>Air UK⁶</td>
<td>Amsterdam-Glasgow</td>
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<tr>
<td></td>
<td></td>
<td>Amsterdam-Newcastle</td>
</tr>
<tr>
<td>Lufthansa</td>
<td>CAI</td>
<td>Frankfurt-Calgary</td>
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<tr>
<td></td>
<td></td>
<td>Frankfurt-Vancouver</td>
</tr>
<tr>
<td>Pan American World</td>
<td>Adria Airways</td>
<td>New York-Ljubljana¹</td>
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<tr>
<td></td>
<td>Malev Hungarian</td>
<td>New York-Budapest</td>
</tr>
<tr>
<td>SAS</td>
<td>All Nippon Airways</td>
<td>Stockholm-Tokyo¹</td>
</tr>
</tbody>
</table>


NOTES: (1) Proposed. AIR TRANSPORT WORLD, various issues, (July 1989-April 1990). (2) Qantas Airways owns 19.9% of Air New Zealand. (3) SAS owns 9.9% of Texas Air, the parent company of Continental Airlines. (4) Continental’s code is shown on Transavia flights between London and Amsterdam. (5) Japan Air Lines owns 7.5% of Air New Zealand. (6) KLM owns 14.9% of Air UK.

V. ADVANTAGES FOR AIRLINES

A. COMPUTER RESERVATION SYSTEMS

In addition to product attributes, price and promotion, distribution plays an important role in any firm’s marketing strategy. In the airline industry, the product is an airline’s schedule, and the primary means by
which this product is distributed are CRSs in travel agents' locations.\textsuperscript{57} U.S. systems, for example, handle at least sixty and seventy percent of domestic and international passenger business respectively.\textsuperscript{58} An airline has two distribution objectives. The first objective is to ensure that its schedule is displayed in CRSs, even in those countries which the airline does not serve. The second objective is to obtain the most advantageous position on the CRS terminal screen, since fifty percent of all flights are booked from the first flight itinerary displayed. Furthermore, between seventy and ninety percent of all flights are booked from the first CRS screen.\textsuperscript{59} Before the role of code-sharing is discussed, an understanding of how flights are ranked in CRSs is provided.

All airlines submit schedules to OAG and ABC which enter direct flights (i.e. same-plane service) and paid connections onto magnetic tapes. System vendors, in turn, purchase these tapes and transfer the data to their own CRS. Each system vendor develops algorithms, which rank flights by the number of stops, elapsed travel time and/or the time differential between actual and preferred departure. In addition, if at all possible, algorithms tend to be structured in such a way as to provide superior display of the system vendor’s flights.

Despite a potential bias, ranking priority is commonly given to direct flights, followed by online connections,\textsuperscript{60} and then interline connections.\textsuperscript{61} Generally speaking, consumers prefer online connections over interline connections because the distance between gates is usually shorter, baggage transfer is more easily made when time is short, and an airline would be more willing to hold the outbound flight in the event of a delay caused by the incoming flight. To reflect this preference, interline connections are assessed a "penalty". American’s Sabre, for example, adds forty-five minutes to an interline connection flight departure time.\textsuperscript{62} However, there are two situations in which an interline connection could receive an equally prominent display position. First, the interline connecting service is significantly better in terms of travel time and/or departure con-

\begin{itemize}
\item \textsuperscript{57} Other means include airline guides used in unautomated travel agencies, and CRSs in airline ticketing and reservation offices.
\item \textsuperscript{58} In 1984, U.S. travel agents sold sixty-five percent of domestic tickets and over eighty percent of international tickets. Travel agents using CRSs sold ninety percent of these tickets. British Airways' Computer Reservations System Investigation, DEPT. OF TRANS. Docket No. 45389.
\item \textsuperscript{59} Osterr Jr., supra note 12, at 376.
\item \textsuperscript{60} Online connecting service means all flight segments are operated by the same airline.
\item \textsuperscript{61} Interline connecting service means at least one flight segment is operated by a different airline.
\item \textsuperscript{62} Feldman, supra note 14, at 375. Until the summer of 1987, elapsed travel time was also a ranking factor in Sabre, but it was eliminated to discourage the practice of publishing unrealistic short flight schedules.
\end{itemize}
venience. Second, the same code is shown on both flights, thereby elevating the interline connecting service to online status.

Table 3 shows the display position of the British Airways and United Air Lines code-sharing operation in Apollo (United), Sabre (American) and SystemOne (Continental, Eastern). A flight departing Seattle for London on June 10, 1988 at 11:15 a.m. was requested. On that particular day, United Air Lines operated two code-sharing flights, BA 8142 and BA 8150, from Seattle to Chicago, where London-bound traffic was fed to British Airways flight 296.

Both Apollo and SystemOne displayed the second code-sharing flight alternative on an earlier screen than interline connections. But, the first code-sharing flight alternative was not shown in either Sabre or SystemOne, while both alternatives received a more prominent display position in Apollo. This difference could have been due to different ranking factors and priority levels, as well as a structural bias in favor of the system vendor or a participant.

Assuming biased displays are not prohibited by law (or the policing machinery is otherwise ineffectual), a more prominent display position would likely be obtained where the code-sharing air carrier is a system vendor or participant. In addition, the probability that the code-sharing flight alternative is selected would increase proportionately with the size of the CRS network. In the U.S., Sabre and Apollo control about forty-one and twenty-eight percent of the market respectively. In Canada, Sabre is used by 1,100 to 1,200 travel agencies and commercial enterprises, while Reservec and Pegasus have a travel agency network of at least 3,000 and 775 agencies respectively. However, by the summer of 1990, the Gemini system will replace the two Canadian-owned CRSs.

It is predicted that, in the 1990s, at least three mega-computer reservation systems could control ninety percent of the free world’s one billion annual bookings. As shown in Table 4, most CRSs would be owned by a consortium of airlines and be linked to systems located in other regions. While market domination is a substantial concern, vendors of Amadeus and Abacus have already indicated that their systems would provide unbiased displays. This would not, however, eliminate the CRS advantage

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64. TRAVEL WEEK BULLETIN, November 30, 1989, at 1.
of code-sharing.

### TABLE 4

**MEGA-COMPUTER RESERVATION SYSTEMS**

<table>
<thead>
<tr>
<th>CRS</th>
<th>Region</th>
<th>Partners</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) Abacus</td>
<td>Asia</td>
<td>Cathay Pacific, China, Malaysia, Philippine, Royal Brunei, Singapore</td>
</tr>
<tr>
<td>Amadeus</td>
<td>Europe</td>
<td>Adria, Air France, Air Inter, Braathens, Emirates, Finnair, Iberia, Icelandair, JAT, KLM, Linjeflyg, Lufthansa, Royal Air Maroc, SAS</td>
</tr>
<tr>
<td>SystemOne</td>
<td>U.S.</td>
<td>Continental, Eastern</td>
</tr>
<tr>
<td>2) Abacus</td>
<td>Asia</td>
<td>Cathay Pacific, China, Malaysia, Philippine, Royal Brunei, Singapore</td>
</tr>
<tr>
<td>Worldspan¹</td>
<td>U.S.</td>
<td>Delta, TWA, Northwest</td>
</tr>
<tr>
<td>3) Apollo²</td>
<td>U.S./Asia</td>
<td>Alitalia, British Airway, KLM, Swissair, United, USAir</td>
</tr>
<tr>
<td>Galileo</td>
<td>Europe/Australia³</td>
<td>Aer Lingus, Alitalia, Austrian, British Airways, KLM, Olympic Airways, Sabena, Swissair, TAP Air, United</td>
</tr>
<tr>
<td>Gemini</td>
<td>Canada</td>
<td>Air Canada, CAI, Covia</td>
</tr>
<tr>
<td>4) Sabre</td>
<td>Worldwide⁴</td>
<td>American</td>
</tr>
</tbody>
</table>

**SOURCE:** Air Transport World, various issues, (July 1989 to April 1990).

**NOTES:**
1. Worldspan will combine the Datas II and Pars CRSs.
2. Apollo is marketed under the Covia Partnership.
3. Ansett and Australian Airlines have agreed to distribute Galileo in Australia.
4. Since Fantasia failed to attract investors, Qantas Airways has agreed to distribute Sabre in Australia and New Zealand.

### B. MARKET ACCESS AND PRESENCE

Without actually operating a route, the code-sharing air carrier could gain access to new markets. Here, either the air carrier has no route rights, aircraft are unavailable, or service would be unprofitable. Although market access could be obtained through interline arrangements, a code-sharing flight alternative would more likely be selected since CRSs assess penalties to interline connecting services. In addition, should the air carrier commence operations, its identity would already be established in the market. For example, Air Canada does not have aircraft to provide service to Amman and Jeddah, but its code is shown on Royal

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68. However, if underlying route authority is required, dual designator codes could not be used on the route.
69. Since wide body jets are commonly used on international routes, it would be unprofitable to provide service when passenger load factors are low, unless the airline has change of gauge or cabotage rights in the foreign country.
Jordanian's flights between Montreal and these points. As a result, the airline has gained access to, and established its identity in, at least two Middle East markets.

An air carrier could also establish a presence in existing markets. The additional code-sharing flights would superficially increase its flight frequency on the terminal screen. Besides the CRS advantage, the air carrier could advertise that it offers a variety of flights. For example, British Airways could advertise that it has three daily flights between Seattle and London, since the airline actually operates one direct evening flight and its code is shown on two United flights between Seattle and Chicago.

C. OPERATING PROFITS

Given the higher ranking priority of online connections, the use of shared airline designator codes would likely result in higher passenger load factors on both flight segments. For example, Continental Airlines and SAS mutually feed traffic at Newark, and dual designator codes are shown on SAS's flights between Newark and three Scandinavian points. In the summer of 1989, the code-sharing flights had an average load factor of ninety percent, and about forty percent of the transatlantic traffic was transfer business, sixty-six percent of which was carried by Continental Airlines.70

Higher passenger load factors could make a disproportionate difference in the profits earned. Additional passengers flying in otherwise empty seats would increase operating costs by no more than the cost of food and beverage service, while revenue would increase by the amount of the air fare. If the average load factor is sixty-five and the break-even load factor is sixty-one, this four percent difference would translate to five passengers on a B737-300 aircraft having a seat capacity of 118. Hence, a code-sharing arrangement which results in one more passenger could increase operating profits by as much as twenty percent.

Furthermore, if the code-sharing air carrier is required to purchase blocked space on specified flights, this gain could be increased by the difference between the fare and cost of each sold seat, and/or reduced by the cost of each unsold seat. Alternatively, if revenues and expenses are shared, the air carrier would assume a greater financial risk, but could potentially earn more profits from a joint operation.

VI. DISADVANTAGES FOR AIRLINES

A. DIVERSION OF INTERNATIONAL TRAFFIC

Code-sharing arrangements between foreign competitors would likely divert international traffic from other carriers. First of all, an air carrier could lose traffic on domestic routes. Prior to the code-sharing operation, the air carrier would have provided interline connecting service between the foreign air carrier’s point of entry and other domestic points. Subsequently, the foreign air carrier and another air carrier mutually feed traffic at the domestic point, and dual designator codes are used on the foreign sector. Not only would the competitive threat be reduced, it not eliminated, but the two air carriers could dominate the market. For example, until early 1989, Air Canada and Japan Air Lines had an interline arrangement at Vancouver. Today, CAI and Japan Air Lines operate joint services on the Toronto-Hong Kong and Toronto-Tokyo routes. Consequently, Air Canada carries less Pacific Rim traffic on domestic routes, while CAI and Japan Air Lines dominate the Canadian-Japanese market.

An air carrier could also lose traffic on foreign routes. Here, the air carrier would provide direct service in competition with the flag air carrier.

71. For U.S. major carriers, food expense averages about 3.55 percent of total operating cost. Henderson, Upgrades Send Costs Soaring Again, AIR TRANSPORT WORLD, April 1990, at 97.

72. It is noteworthy that the Canadian and Japanese governments are considering the designation of additional carriers. Air Canada Public Relations Office, Vancouver, December 1989.
of the foreign country, as well as other foreign air carriers who provide online connecting service via their home country. If the other air carriers operate code-sharing flights on either sector, a variety of flight options could be offered since the flight frequency of the code-sharing air carrier would be higher. For example, both Air Canada and Olympic Airways provide direct service between Toronto and Montreal, and Athens, while Lufthansa provides connecting service via Frankfurt. Since Lufthansa's code is used on CAI's Calgary-Frankfurt and Vancouver-Frankfurt routes, the foreign airline can offer more flights between Canada and Greece. As a result, the designated air carriers have likely lost some traffic on the foreign route. In addition, Air Canada probably carries fewer Athens-bound passengers on flights between Western Canada, and Toronto and Montreal.

B. CARRIER LIABILITY

The International Air Transport Association provides a standard form passenger ticket, and section 5 of its conditions of contract states that "[a]n air carrier issuing a ticket for carriage over the lines of another air carrier does so only as its agent." Accordingly, the contracting parties are the person named on the passenger ticket and the air carrier whose designator code is listed in the Carrier-Transport section.

It follows that the code-sharing air carrier is a party to the contract of carriage and liable to passengers for any breach thereof.73 Even though it has no contractual obligation to these passengers, the operating air carrier usually agrees to "indemnify and hold harmless" the code-sharing air carrier from all liabilities arising out of the marketing of the flights, regardless of negligence on the part of that air carrier.74 Since March 1988, however, code-sharing arrangements between U.S. and foreign air carriers have been authorized only on the condition that:

the foreign air transportation in question be sold in the name of the carrier holding out such service in computer reservation systems and elsewhere, and the carrier selling such transportation accept all obligations established in its contract of carriage with the passenger.75

Similarly, in Canada, the code sharing air carrier is required to accept all obligations established in its contract of carriage with the passenger.76 Thus, it appears that indemnity clauses would be of no force and effect, at least in the U.S. and Canada.

73. For example, denied boarding due to overbooking is a contractual breach.
75. DEP'T OF TRANS. order, supra note 22.
76. Orders supra note 7.
VII. DISADVANTAGES FOR CONSUMERS

A. POORER OPTIONS

Consumers are not usually informed of code-sharing flights in reservation transactions. Even though U.S. airline reservation agents are required to disclose the identity of the operating air carrier, over eighty percent of international tickets are sold by travel agents. Since CRSs only provide descriptive information on a system vendor's flights, the travel agent could not identify other code-sharing operations, unless the CRS has a direct link to the code-sharing air carrier's internal reservation system. Even after ticketing, a consumer would still be unaware that a different air carrier actually performs the service because its identity is not disclosed on passenger tickets. Apparently, dual information would cause confusion at airport check-in counters and baggage carousels. While airline timetables identify code-sharing flights, it is reasonable to assume that most consumers do not consult them before travel arrangements are made. Consequently, the identity of the operating air carrier would not likely be known until the consumer arrived at the check-in counter or departure gate.

Since the identity of the operating air carrier is not usually disclosed, consumers could accept poorer options. The travel agent could book a code-sharing flight alternative because it received a prominent display position on the CRS terminal screen, or an online connecting service was requested. Yet, an interline connection could have been better in terms of travel time and/or departure convenience. Alternatively, the consumer could prefer the services offered by a particular airline, but unknowingly choose a different airline. It is interesting to note, however, that the DOT has had only a minuscule number of complaints.

B. HIGHER AIR FARES

Code-sharing arrangements between foreign competitors could result in higher air fares on single designated routes. But, any proposed fare would require prior governmental approval. Under a double-disapproval pricing regime, only the aeronautical authority of one country has to approve the fare. In any other case, proposed fares have to be approved by the aeronautical authority of each country. Transborder fares, for example, are subject to the latter regime.

77. DEP'T OF TRANS. Docket No. 45389, supra note 58.  
VIII. CODE-SHARING OPPORTUNITIES

A. AIR CANADA AND CAI

The Canadian government has essentially divided the globe between its two flag air carriers, Air Canada and CAI. Air Canada provides service to the U.S., the Caribbean, Europe, and two South American and Asian points, while CAI serves Asia, the South Pacific, South America, and fewer U.S. and European points. Both airlines currently offer service to Frankfurt, London, Manchester and Paris.\(^{80}\)

Air Canada and CAI could conduct code-sharing operations on single and multiple designated routes. Here, the two air carriers would mutually feed traffic at Canadian points, and dual designator codes would be used on foreign sectors. For example, Air Canada could feed Pacific Rim traffic to CAI rather than its interline partner, Cathay Pacific. This arrangement would increase the number of Canadian-originating passengers on international flights operated by the designated air carrier. But, the air carrier could lose some traffic on domestic flights since its code-sharing partner would also be offering online service to the foreign destinations. However, if underlying route authority is required, code-sharing operations would be limited to multiple designated routes.\(^{81}\)

B. CANADIAN AND FOREIGN CARRIERS

Seven types of code-sharing arrangements between Canadian and foreign air carriers could be established in the international market. First, a Canadian air carrier could code-share on domestic sectors of third and fourth freedom routes. Here, the air carrier would feed traffic to a foreign air carrier at its first point of entry, and dual designator codes would be shown on the foreign air carrier's flights between co-terminal points. This operation would be advantageous where the flight terminates at the foreign gateway, or few passengers travel to the second point. For example, on CAI's Toronto-Rio de Janeiro/Sao Paulo route, its code could be shown on Varig's flights between the two Brazilian points. In addition, if underlying route authority is not required, Canadian air carriers could develop hubs and establish code-sharing arrangements on other routes in the foreign country. CAI already has a hub at Amsterdam and Tokyo, while Air Canada's hubs include Frankfurt, London and Paris. In all likeli-

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80. CAI obtained traffic rights to London, Manchester and Paris through PWA Corporation's acquisition of Wardair.

81. As of September 1988, multiple designated countries included: Austria, Brazil, Chile, Dominican Republic, Egypt, Fiji, Finland, France, Germany, Hong Kong, India, Ireland, Italy, Jamaica, Mexico, Netherlands, New Zealand, Pakistan, Panama, Portugal, Saudi Arabia, Singapore, Spain, St. Kitts, St. Lucia, Thailand, Trinidad/Tobago, Turkey, United Kingdom, Venezuela and Yugoslavia.
hood, the Canadian government would have to grant reciprocal rights to the designated air carrier of the foreign country. For example, if CAI and its interline partner Australian Airlines proposed to code-share on flights between Sydney and other domestic points, a similar arrangement between Qantas Airways and a Canadian air carrier would have to be permitted in Canada.

Second, foreign air carriers could establish code-sharing arrangements on Canadian sectors of third and fourth freedom routes. For example, Aerolineas Argentinas provides service from Buenos Aires to Toronto and Montreal. The foreign air carrier could feed traffic to a Canadian air carrier at Toronto, and dual designator codes could be shown on flights between co-terminal points. If underlying route authority is not required, a foreign air carrier's code could also be used on other domestic routes. Unless reciprocal rights are granted, this arrangement could pose a substantial threat to the designated air carrier because its foreign competitor would be offering online service to numerous Canadian points.

Third, a Canadian air carrier could code-share on foreign sectors of third and fourth freedom routes. Here, the air carrier and its foreign competitor would mutually feed traffic at Canadian and foreign points of entry and dual designator codes would be used on the foreign sector. Not only would the Canadian air carrier's share of foreign-originating traffic increase, but both air carriers could dominate the market. For example, Air Canada and Air New Zealand have an interline arrangement at Vancouver and Los Angeles. If CAI and the foreign air carrier conduct code-sharing operations on competitive routes, Air Canada would carry few Auckland-bound passengers on domestic and transborder flights.

Fourth, Canadian air carriers could code-share on foreign sectors of third and fourth freedom routes operated by foreign air carriers. Here, the two air carriers would mutually feed traffic at a Canadian point of entry. Since dual designator codes would be used on the foreign sector, the Canadian designated air carrier could lose traffic on domestic and international routes. For example, if Air Canada's code is shown on Cathay Pacific flights, a significant amount of transpacific traffic could be diverted from CAI. Today, the two airlines already offer joint fares and coordinate schedules in Vancouver. In addition, Aeroplan members receive mileage points for flying Cathay Pacific. However, if underlying route authority is required, Air Canada would be precluded from code-sharing.

Fifth, Canadian air carriers could establish code-sharing arrangements on foreign sectors of fifth freedom routes. There are four ways in which these routes could be operated on a shared code basis. For simplicity, CAI's Toronto-Amsterdam-Munich route is used as an example. First, the Canadian air carrier and KLM could code-share on the Toronto-Amsterdam sector and mutually feed traffic at both points. Second, CAI
and Lufthansa could code-share on the Toronto-Munich sector and feed traffic to each other at both points. Third, CAI and KLM (or Lufthansa) could mutually feed traffic at Amsterdam, and dual designator codes could be shown on the foreign air carrier’s flights between Amsterdam and Munich. And fourth, CAI and KLM could also feed traffic to each other at Amsterdam, but dual designator codes would be used on both foreign sectors. Depending on the relationship established, CAI could carry more foreign originating traffic on the transatlantic route and/or Canadian originating traffic on domestic routes. As a result, the airline could gain access to markets beyond its European gateway.

Sixth, Canadian air carriers could code-share on foreign sectors of fifth freedom routes operated by foreign air carriers. At least three types of relationships could be established. First, on the foreign-Canada-foreign route, a Canadian and foreign air carrier could mutually feed traffic at the Canadian point, and dual designator codes could be used on competitive sectors. For example, on Sabena’s Brussels-Montreal-Chicago route, dual designator codes could be shown on transborder flights operated by Air Canada and/or the foreign air carrier. Alternatively, the Canadian air carrier’s code could be used on the first foreign sector of British Airways’ London-Montreal-Detroit route. Second, on the foreign-foreign-Canada route, two air carriers could feed traffic to each other at the Canadian point, and dual designator codes could be used on competitive sectors operated by the foreign air carrier. For example, Air Canada’s code could be used on the transborder sector of Royal Air Maroc’s Casablanca-New York-Montreal route. And third, on the foreign-foreign-Canada route, a Canadian and foreign air carrier could mutually feed traffic at the second foreign point, and dual designated codes could be shown on flights operated by the Canadian air carrier. For example, if Cathay Pacific obtains Hong Kong-San Francisco-Toronto permit authority, its code could be shown on transborder flights operated by Air Canada. While passenger load factors would increase on these flights, CAI could lose a significant amount of the Eastern and Central Canada-Hong Kong market.

Finally, foreign sectors of sixth freedom routes82 could be operated on a shared code basis. Like the previous arrangements, two air carriers could establish a feed relationship at a Canadian or foreign point and use dual designator codes on one or both foreign sectors. There are, however, no sixth freedom routes operated by Canadian air carriers. Usually, an air carrier provides connecting service via its home country. For example, Air Canada offers service between Chicago and various European points via Toronto.

82. The sixth freedom is the right to pick up traffic in a foreign country and to carry it to a third country via the home country.
IX. CODE-SHARING CHALLENGES

At least two types of code-sharing arrangements between U.S. and foreign air carriers could divert international traffic from Canadian air carriers via the U.S. First, a U.S. air carrier could code-share on foreign sectors of third and fourth freedom routes. Here, the air carrier would feed Canadian originating traffic to a foreign air carrier at the U.S. point, and dual designator codes would be used on the foreign sector. Either a major air carrier or its affiliate would operate between the transborder city-pairs. For example, a passenger travelling from Hamilton, Ontario to Budapest, Hungary could fly Pan Am Express between Hamilton and New York, and then Malev Hungarian Airlines between New York and Budapest. Both flights segments are listed under the designator code of Pan American World Airways. Even though no Canadian carrier serves Budapest, the passenger could have been carried as far as a European point.

Second, a foreign air carrier could code-share on the transborder sector of fifth freedom routes. Here a U.S. air carrier would feed Canadian originating traffic to the foreign air carrier at a U.S. point, and dual designator codes would be shown on transborder flights operated by the U.S. air carrier. For example, Lan Chile and Delta Air Lines could establish a code-sharing arrangement on the second sector of the Santiago-Miami-Montreal route. Currently, CAI provides connecting service between Montreal and Santiago via Toronto.

X. CONCLUSION

In the end, international code-sharing arrangements would result in the globalization of airlines. Even if operations are limited to designated routes, an airline could gain access to, and establish a presence in, all major markets of the world. For example, a global partnership between British Airways and United Air Lines would combine approximately 169 and 165 points respectively, and their two route networks would span six continents. But, if the world community adopts a code of conduct on CRSs, code-sharing would not longer play a role in the competitive strategies of international airlines. Instead, airlines would have to compete for a greater share of the world market by establishing interline arrangements, joint frequent flyer programmes and CRS links. Unless the nationality criteria to operate internationally is abolished, there would then be few, if any, truly global airlines.

83. Whitaker, Feeding Time, AIRLINE BUSINESS, March 1988, at 23.
The Detrimental Effects of Hostile Takeovers, Leveraged Buyouts, and Excessive Debt on the Airline Industry

Michele M. Jochner†

I. TAKEOVER SPECULATION COUPLED WITH EXCESSIVE DEBT MAY PUSH THE AIRLINE INDUSTRY TO THE BRINK OF DISASTER

A. INTRODUCTION

Within the past several years, takeover bids for airline carriers have been in vogue. The individuals bidding for these airlines have been attracted by the high level of concentration which has occurred since the advent of deregulation. A handful of mega-carriers which have amassed enormous market power now dominate the skies.¹ By developing hubs at

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¹ At present, the eight largest mega-carriers dominate roughly 94% of the domestic airline passenger market. Dempsey, The Dangerous Cost of Airline Deregulation, The Christian Science Monitor, Sept. 27, 1989, at 18. Indeed, this situation has been summed up by public-
major airports, the airlines have in essence created "mini-monopolies" in which they can maintain relatively stable prices.\(^2\) This concentration is reinforced, moreover, by the incumbents' use of frequent flyer programs and ownership of computerized reservation systems.\(^3\) This, coupled with an industry-wide increase in cash-flow and a belief that carriers' assets are undervalued, make these companies prime takeover targets.

The recent trend in hostile takeover bids for airlines, however, may bring the industry to the precipice of economic catastrophe. An industry which has been marginally profitable during most of the 1980's cannot afford to be saddled with the mountain of debt which can result from hostile takeovers or leveraged buyouts (LBOs). This is reinforced by two key factors: (1) the airlines have a great need for liquidity in order to replace an aging fleet of geriatric jets; and (2) the airline business is cyclical and thus is exposed to the risk of a severe downturn at the end of the current economic expansion. In addition, an increase in uncontrollable costs, such as fuel prices or labor costs, and/or a decrease in demand resulting from an economic recession or threats of terrorism, could also send the debt-laden carriers into deep trouble.\(^4\)

\(^2\) See interest attorney Donald Pevsner as "a de facto cartel of eight major airlines that is dictating the travel patterns of 250 million people for their own gain." Friday & Schwartz, Who Wins the Air Wars? NEWSWEEK, Sept. 18, 1989, at 41.

\(^3\) An added benefit of establishing a hub at a major airport is the virtual domination the hub-carrier can exercise over that facility. A carrier's possession of the majority of landing gates at a terminal may not only allow it to limit the entry of new competitors into that city-market, but also to increase fares in that market due to the resultant lack of competition. This situation has led the Justice Department this summer to initiate an investigation into the possible antitrust violations of these practices. Nomani & Barrett, Control of Major Airports by Carriers Is Focus of Justice Department Inquiry, Wall St. J., June 18, 1990, at A3, col. 2.

\(^4\) Frequent flier programs serve to keep the mega-carriers' customers loyal, at least for the limited time of the promotion. The frequent flier concept, which was initiated by American Airlines in 1981, finds its success in the fact that frequent fliers are usually business people who can accumulate miles and then use the free trips or reduced fares on nonbusiness trips. Bailey & Williams, Sources of Economic Rent in the Deregulated Airline Industry, 31 J. L. & Econ. 173, 188 (1988).

Moreover, the control of computerized reservation systems by the major carriers allows them to participate in various anti-competitive practices. Customers are often steered to the flights offered by the carrier-owner of the system the travel agent uses, a practice usually known as the "halo effect." In exchange, the travel agent often receives bonuses from the carrier. Airline Concentration at Hub Airports: Hearings Before Senate Comm. on Commerce, Science, and Transportation, 100th Cong., 2nd Sess. 41 (1988)(statement of Kenneth Mead, Assoc. Dir., United States General Accounting Office).

\(^4\) The recent events in the Persian Gulf area have clearly shown these factors to be a genuine threat to a carrier's survival. Since the start of the hostilities on August 2, the price of oil has doubled. In concrete terms, a $3 per-barrel increase results in an 11-cent per gallon rise in jet fuel costs. For every cent-per-gallon increase in fuel prices, the industry suffers $160 million in additional costs. Gaines, Overseas Air Fare to Rise 7%, Chicago Trib., Sept. 25, 1990, § 3, p.1, col. 2.

The escalating price of jet fuel coupled with a drop in passenger bookings attributed to
Indeed, the industry’s total debt now stands at roughly $15 billion, with another $108 billion set aside to purchase new aircraft. Excessive debt, however, will make it not only extremely difficult for the airlines to accomplish this much needed modernization of their fleets, but also to adequately maintain the planes it already operates. Recently, an aviation task-force of public and private experts, formed after a section of fuselage ripped off an Aloha Airlines 737, called for a $563 million overhaul of 1,900 aging McDonnell-Douglas jetliners. This group’s call followed a Federal Aviation Association (FAA) order for the overhaul of 1,300 aged Boeing aircraft. These moves were taken in an effort to rejuvenate the 3,300 United States jet fleet, which on the average contains aircraft which is thirteen years old, making it the oldest fleet in the non-communist world.

Thus, in response to public concerns for aircraft safety, the U.S. carriers have placed enormous orders for new aircraft. This comes at a time when the industry’s cash flow for 1988, which by industry standards was a very good year, totalled less than $5 billion. It is estimated that by 1997, less than seven years from now, U.S. carriers will take delivery of these new jets with their multi-billion dollar price tags, and the industry will be forced to hire 50,000 new mechanics to service these planes. These enormous increases in capital and labor costs will be extremely difficult for a carrier to meet if it is strapped for cash. This foreshadows the fact that highly-leveraged airlines will be forced to finance these aircraft purchases and increased labor costs by adding even more debt. Therefore, any increase in debt brought about by speculative takeover activity clearly increases the threat of an economic catastrophe.

Such takeover activity is extremely troublesome when coupled with the estimate that the profits of the U.S. carriers will drop by about one-half...
in 1990 because of a sluggish economy. The signs of this industry slow-
down have already begun to appear: the number of passengers on U.S.
airlines has fallen from 212.7 million during the first half of 1988 to 208.3
million during the same period in 1989.\textsuperscript{10} This overall downturn in the
amount of air travelers could precipitate a resurgence of the cut-throat
fare wars which were the catalyst for a shake-out of the industry during
the 1980's. Therefore, in order to attract consumers to the market, the
airlines may have no choice but to offer lower and lower fares, in an at-
ttempt to grab market share from the nearest competitor in order to stay
alive. Such cut-rate pricing may be especially necessary in light of the
excess capacity which may result from an infusion of new aircraft into the
airline system over the next few years. Thus, a price war this time may
lead to even more devastating consequences than those of the price wars
of the early 1980's. A downturn in the economy, causing a concomitant
decrease in air travel, coupled with excessive capacity due to the delivery
of new jets, and the enormous debt saddled on the carriers due to hostile
takeovers and purchases of new aircraft may spell bankruptcy for many
major carriers, as well as total disaster for the industry as a whole. The
minimal amount of competition which has remained during the past dec-
da could finally be eliminated and the industry may be characterized by
even tighter concentration.

Debt laden carriers, moreover, may be tempted to decrease capital
spending due to their lack of cash, thereby jeopardizing their future
growth.\textsuperscript{11} These carriers may be unable to develop new business, hubs,
and routes in such untapped and growing markets as East Asia.\textsuperscript{12} Simi-
larly, serious labor disputes may arise if the companies are forced to de-
mand further concessions from the employees in order to cut costs. This,
combined with the constant threat of not being able to meet the debt pay-
ments and the threat of ultimate bankruptcy, severely circumscribes man-
agement's freedom. These considerations may force management to pull
back from investment plans because the company's cash flow is instead
largely dedicated to the suppliers of capital. In essence, changing the
company's capital structure from one laden heavily with equity to one
laden with debt effectively transfers control over the company's cash flow
from managers to creditors. This is an inefficient allocation of society's
scarce capital resources. The service of needless debt, brought about
solely because of takeover speculation and individual greed, surely is not
the optimum use of society's capital. These transactions serve merely to
rearrange capital; they do not create capital.

\textsuperscript{10} Can United Afford to be Taken Over?, supra note 8, at 148.
\textsuperscript{11} Power, Off We Go Into The Hazy Blue Yonder: Just How Will Today's Buy-out Boom
\textsuperscript{12} Id.
B. DEBT FINANCING: ITS EVOLUTION FROM SACRED COW TO PARIAH

Years ago, however, it was thought that corporate debt was quite a wonderful tool in catapulting a company to the top of the heap. The rationale for debt financing was based upon the premise, advanced by economists Merton H. Miller and Franco Modigliani during the 1950's, that a company’s earning power, not its financial makeup, is what determines its market value. It was also thought that a high debt level spurred a company to be more competitive and more efficient. This philosophy may in part explain why, during this decade, corporate America has retired nearly $500 billion in equity, and replaced it with almost $1 trillion in debt. The interest payments on this mountain of debt absorb almost 30% of the total cash flow, a figure surpassing by several percentage points the record levels of debt reached during the two worst post-war recessions. Thus, instead of investing in research and development, training, and long-term goals, American business has fallen into the habit of gambling on short-term deals that jeopardize the nation’s long-term economic security.

Worse, not only does a high level of debt serve to detour a company’s capital from more productive uses, it also impairs the competitiveness of the company as well. Indeed, a company which is buried under a mountain of debt cannot easily respond to changes in the market. Cash-rich, non-debt-burdened competitors can easily wrest market-share away from the debt-laden company through aggressive price-cutting. An increase in competition coupled with a change in technology can diminish revenues as easily as an economic downturn. High debt levels are especially a hindrance to companies, such as airlines, involved in areas where there is constant technological change. A company deeply in debt will not be able to keep up with this change and soon may find itself in a decided competitive disadvantage.

The airline industry is particularly ill-suited for carrying high levels of debt. Airlines are particularly sensitive to even the smallest change in the economy, and any recession could spell catastrophe for those carriers mired in a swamp of debt. The carriers must not only be able to service the debt, but also must be able to meet the unforeseen changes in day-to-day business. For example, a one-cent change in the price per gallon of

14. Id.
15. Id.
16. Id.
jet fuel may mean a $15 to $20 million change in a carrier’s operating profits. This could mean that the carrier may not be able to meet its heavy obligations and thereby default on its loans. Couple this with the ever-present threats of terrorism, labor disputes and new FAA safety rules, plus increased global competition, and the skies may become quite unfriendly for the industry, especially in light of the fact that this year the industry as a whole is expected to make only $3 billion in operating profits, even though the carriers have been charging higher fares.

Some observers may believe that these predictions of doom and gloom are exaggerated since presently there is no recession and interest rates are relatively low. However, a look at the impact of excessive debt in other industries reveals the serious problems debt creates. The newspapers are filled with stories about companies, saddled with enormous debt obligations due to takeovers and LBOs, which are defaulting on their loans. The debt financing which looked so easy a few years ago is now turning into a nightmare for many companies. In 1989 alone, there were bond defaults and debt moratoriums amounting to more than $4 billion. This suggests that companies swamped with debt may find themselves on the verge of collapse even without any type of economic downturn. Companies which must meet astronomical debt repayments may be vulnerable to even the mildest setbacks in their markets.

Because of the increasing number of defaults on corporate debt, equity is beginning to come back into fashion. Today the thinking concerning debt is starting to change; many companies disdain the use of junk bonds as antithetical to their corporate image. Moreover, those companies which took on a great deal of debt as part of leveraged buyouts or stock buy-backs are now attempting to “deleverage” their balance sheets by replacing their debt with equity. Ironically, even junk-bond king Michael Milkin has now called for companies to return to equity financing, urging an exchange of their junk debt for a combination of equity

19. Id.
20. The Bills Are Coming Due, supra note 13, at 84.
22. Berman & Weisman, Be Wise, Equitize, FORBES, Nov. 27, 1989, at 38. Indeed, the trend towards de-leveraging is not surprising in view of the current condition of the debt market. For example, the junk-bond market during 1989 was disastrous. The purchasers of junk, worried about a possible recession and concomitant defaults on these high-yielding securities, had been demanding ever-increasing premiums from borrowers. In 1989 the spread between the Treasury Bill rate and the average rate on junk bonds widened to five to six points, the largest spread since the creation of the junk-bond concept. At the same time, the total return for investors of junk bonds had dropped into negative numbers. Hector, Junk After Milken, FORTUNE, Nov. 6, 1989, at 121.
and higher-grade debt carrying a lower interest burden.\textsuperscript{23}

\section*{C. \textsc{The Corporate Raider's Gameplan}}

Much damage has already been done to the American corporate landscape; a great deal of it precipitated by the making of hostile, unwanted bids for large companies.\textsuperscript{24} These bids are usually made by corporate "raiders" whose first, and most likely, only concern is making a profit on the stock which they have accumulated at bargain-basement prices. This is especially true of airline stocks, which usually sell at a discount of approximately one-third of the stock market's price-to-earnings ratio, which is currently pegged at about thirteen times earnings.\textsuperscript{25}

This discount is directly attributable to the fact that airline earnings are subject to the cyclical ups and downs of the economy.\textsuperscript{26}

Instead of seeing the cyclical perils, some individuals look to airline stocks and see previously overlooked assets, such as the value of the carrier's air fleet, landing slots at overcrowded airports, computer reservation system, spare parts, and even orders, delivery dates and deposits on new airplanes from backlogged manufacturers such as McDonnell-Douglas and Boeing.\textsuperscript{27} These individuals also see untapped value in the sale and lease-back of the carrier's planes. In such a transaction, the

\begin{itemize}
  \item On April 20, 1990, Michael Milken agreed to plead guilty to six felony counts and to pay $600 million in fines and restitution, the largest individual criminal settlement ever. This decision came just before a grand jury was to indict him on charges of insider trading, bribery, cheating customers and his former employer, Drexel, Burnham, Lambert, and destroying incriminating evidence. Cohen, \textit{About Face: How Michael Milken Was Forced To Accept The Prospect of Guilt}, Wall St. J., April 23, 1990, at A1, col. 1.
  \item For example, the largest LBO was that of RJR Nabisco, which was done for $26 billion in debt, an amount of debt greater than that of "most developing countries." Dobrzynski, \textit{Running the Biggest LBO: RJR's Lou Gerstner Has A Plan. So Far, It Works}, Bus. Wk., Oct. 2, 1989, at 73. In order to meet the multi-billion dollar interest payments RJR has, among other things, cut its work force and sold several well-known assets, such as Chun King and Del Monte Foods. Not surprisingly, the employee morale at RJR has steadily declined. \textit{Id.} at 72-73.
  \item \textit{Id.}
  \item \textit{Dogfight for Dominance}, supra note 5, at 54. For example, McDonnell-Douglas has a record order backlog of $18 billion. The company has 401 firm orders, which will take well into 1993 to fill; it also has 518 options, which if exercised, would keep its work force busy until the end of the century. Henkoff, \textit{Bumpy Flight at McDonnell-Douglas}, \textit{FORTUNE}, Aug. 28, 1989, at 80. Similarly, Boeing has an $80 billion backlog of orders to fill. Boeing's orders jumped 70%
airline sells its planes, and then leases them back from the purchaser. Takeover raiders have discovered that such arrangements allow them not only to borrow from banks at interest rates lower than those attached to junk bonds, but also allows them to convert debt into an operating expense that usually does not appear on the carrier’s balance sheet as a liability. Nevertheless, whether these amounts are part of the balance sheet debt, or are merely contained in a financial footnote, no amount of financial sleight of hand can obviate the fact that the airline is still obligated to meet these lease payments.

Yet, many corporate raiders never get as far as having to worry about their target’s financial books. The usual modus operandi of these individuals is to make a bid and/or launch a hostile tender offer merely to shake up the market, hoping to draw in other bidders, or to force the company to restructure in order to fend off the hostile attack. The final goal is to drive up the airline’s stock price in order for the raider to reap substantial profits on his investment when he sells his shares to the eventual purchaser. In any event, the airline may end up buried under a mountain of debt, and the management may find itself selling off bits and pieces of the company, or even declaring bankruptcy. Such a situation may further increase industry concentration.

Moreover, and perhaps more frightening, a company buried under debt will certainly be less able to devote economic resources to upgrading and maintaining its equipment when its very existence as a business entity is on the line. Yet, it is precisely within the deregulated environment that more, not less, attention must be devoted to aircraft maintenance.

The emergence of hub-and-spoke systems has caused flights to be shorter, but more frequent. This constant pressurization and depressurization places the greatest stress on an aircraft, and concomitantly shortens its life-span. This would appear to suggest that the nation’s airfleet may be in need of more maintenance. However, during 1987 the airlines allocated roughly 11.2% of operating expenses to aircraft mainte-


29. Indeed, a great amount of the corporate debt is based upon the premise that it will be paid off as the issuing company is broken up and sold off, piece by piece. See Hector, supra note 22, at 128.

30. Payne & Vogel, Sure, The Plane is Old - But Is It Dangerous?, Bus. Wk., March 13, 1989, at 36. For example, the Aloha Airlines plane in which the jet’s fuselage tore away like a convertible top in March of 1989, had made more than 89,680 flights during its nineteen year life. This figure exceeds the manufacturer’s own “design objective” of 75,000 flights. A design objective is the number of flights a jet could make before the airline would find maintenance so expensive that it should consider replacing the plane. Ramirez, How Safe Are You In The Air?, FORTUNE, May 22, 1989, at 80 [hereinafter How Safe Are You?].
nance, less than the 13.2% which was allocated in 1977, even though the nation's fleet today is older and therefore, costlier to maintain.\textsuperscript{31}

Perhaps one plaintiffs' attorney correctly pinpointed the emerging problem when he succinctly stated: "'[t]he overall problem is the aviation industry right now is being run and acquired by financiers — not aviation people — whose business is business.'\textsuperscript{32} A recent study done by the U.S. Office of Technology Assessment found that "airline management practices are an important control valve for commercial aviation safety," and that recent FAA inspections showed that "airlines undergoing management turmoil tend to overlook details of safety programs."\textsuperscript{33} Thus, the constant machinations involved in protracted takeover fights may very well be diverting the attention of airline management from safety to dollars.

Instead of focusing their attention on running safe, efficient, and stable carriers, airline executives such as Frank Lorenzo and Carl Icahn, devote most of their energy to making the bottom line look attractive. This has not only shifted the airlines' primary focus away from resembling a public service organization towards a money-making business, but also may portend a concomitant decrease in the safety of the carriers. In order to stay competitive and make the financial reports look good, airlines have made efforts to reduce the amount of operating costs, including costs for maintenance.\textsuperscript{34} Indeed, in the airline environment of today, a company which strives to increase its margin of safety by devoting more resources to maintenance may be punished in the marketplace if its fares are higher than those of its competitors who cut safety corners in order to have lower fares.\textsuperscript{35}

Corporate raiders such as Lorenzo and Icahn, however, are not afraid to launch hostile attacks because they know that the law concerning such tender offers usually runs in their favor if they play their cards correctly. Since there is no federal common law which defines the fiduciary duties owed by directors of a corporation to its shareholders, takeover activities are subject to the corporate laws of the state in which the target corporation is incorporated. Since a majority of the major corporations are incorporated in the state of Delaware, most other states follow the lead of Delaware's courts in the area of corporate law. A landmark case

\textsuperscript{31} Id. at 76.


\textsuperscript{33} OFFICE OF TECHNOLOGY ASSESSMENT, SAFE SKIES FOR TOMORROW: AVIATION SAFETY IN A COMPETITIVE ENVIRONMENT, 14-15 (1988).

\textsuperscript{34} Id. at 34.

in Delaware corporate law, *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, provided many takeover artists with the ammunition they needed to mount assaults on large companies.\(^{36}\)

When a company is faced with the receipt of an unsolicited merger or tender offer, often termed a “bearhug,” the question becomes whether the target’s board has a duty to negotiate with the potential acquirer. Although it has been held that there is no duty to negotiate *per se*, this may not prevent the potential acquirer as well as dissatisfied shareholders from asserting that the board did have such a duty. The basis for a rejection of an unsolicited offer rests in the so-called business judgment rule, which generally states that if a board acts with good faith and with loyalty to the corporation, the decision of the board is protected from legal attack.\(^{37}\)

However, if a board, as in *Revlon*, should decide to implement antitakeover measures in response to a hostile suitor’s attempts to buy up a large share of the company’s stock, the board’s decisions are subjected to a type of intermediate-scrutiny, for the specter arises that the board may be fending off the bid in an attempt to merely entrench itself.\(^{38}\) This potential for conflict places a burden upon the directors to prove that they

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36. 506 A.2d 173 (Del. 1986). The Revlon litigation arose out of a series of events beginning in June 1985 when the heads of Revlon, Inc. and Pantry Pride, Inc. privately met to discuss a friendly acquisition of Revlon by Pantry Pride. (MacAndrews & Forbes Holdings, Inc. was the controlling shareholder of Pantry Pride). After these talks proved unsuccessful, Pantry Pride launched an all-cash for all-shares hostile tender offer for Revlon stock in August 1985, with the intent of financing the acquisition through a later sale of the company. Revlon’s investment banker advised Revlon’s board that Pantry Pride’s $45 per share offer was inadequate. *Id.* at 177.

Subsequently, Revlon’s board adopted a two-fold defensive strategy to ward off Pantry Pride’s attack. First, Revlon commenced a self-tender offer for up to ten million shares. *Id.* Second, Revlon implemented a “shareholder’s rights plan” by which the shareholders received the right to be bought out by the acquirer at a stated premium. *Id.* at 180.

After these measures were implemented, Revlon negotiated with Forstmann, Little, & Co., and agreed to a leveraged buyout by Forstmann, even though Pantry Pride continued to increase its offer. *Id.* at 178. Forstmann also increased its offer, but the increase was based upon several conditions. First, Revlon would grant Forstmann a lock-up option to purchase Revlon’s vision and health care unit for $100-$175 million below its estimated value if another acquirer were successful in obtaining 40% of Revlon’s shares. Second, Revlon was required to accept a no-shop provision. *Id.*


The business judgment rule is a fundamental axiom of corporate law which restricts the scope of judicial review into the managerial decisions of a corporation’s board of directors. Traditionally, the business judgment rule has been applied to shield directors who have no financial interest in the questioned transactions and who follow an appropriately deliberative process from personal liability for damages arising out of an action taken by the board.

38. Revlon, 506 A.2d at 180; Unocal, 493 A.2d at 954.
had reasonable grounds for believing there was a danger to corporate policy and effectiveness. The board can satisfy this burden by showing it was acting in good faith and with reasonable investigation. In addition, the board must analyze the nature of the takeover attempt and its effects on the corporation in order to ensure that the defensive response is reasonable in relation to the threat posed. Once this is shown, the business judgment rule then attaches and the decision of the board is insulated from judicial attack.

The actions the board takes in order to defend against a hostile attack, however, may lead to a series of events which will legally mean that the company is "for sale." For example, if, as in Revlon, the defensive measures cause the acquirer to increase his offering price to extremely high levels, or if the target company attempts to negotiate a friendly merger with a third party, this may effectively mean that the company is "for sale." Under the Revlon decision, when a company is deemed to be for sale, the duties of the directors change from the preservation of the company as an entity to the "maximization of the company's value at a sale for the stockholders' benefit." In essence, "[t]he directors' role change[s] from the defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company." Thus, once a hostile acquirer tenders a bid for a company, and the company makes a move to defend itself, or if the bid attracts other bidders to the fray, then the directors may find themselves in a Revlon-type situation where they are legally required to "auction" off the company to the highest bidder in order to fulfill their fiduciary obligations to the shareholders. The raiders are aware of this; thus, many will launch a hostile bid just to attract others to the fray in hopes that the company will be forced to put itself on the auction block, thereby providing the raider a hefty return on his investment.

This Delaware view, however, is considered to be rather pro-corporation when compared with the far more free-market-oriented "Chicago School" of economic thought. The basic tenet of "Chicago School" economics is that any takeover, either friendly or hostile, which is successful in the market is of benefit to the economy and thereby beneficial to the majority of individuals who participate in it. The proponents of this view

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40. Id.
41. Revlon, 506 A.2d at 182.
42. Id.
43. Id.
44. See, e.g., Easterbrook & Fischel, The Proper Role of a Target's Management in Responding to a Tender Offer, 94 Harv. L. Rev. 1161 (1981)[hereinafter Proper Role of Target's Management]. Ironically, this is the same type of free-market philosophy which led to airline deregulation and the excessive market concentration in the industry today.
assert that any and all resistance to takeover attempts is to the detriment of shareholders, as well as to the economy as a whole. They contend that resistance to takeovers results in inefficient management as well as management entrenchment; after all, they argue, the company would not be a target if it was run properly in the first place. Therefore, they assert that hostile takeovers are a significant means of displacing these inefficient managers, because the constant threat of a takeover increases the incentive to perform in the best interests of the shareholders.

A major problem with this theory is that these commentators argue that resistance to an offer is premised on one of two grounds: mismanagement or self-interest. They in essence raise this belief to an irrebuttable presumption, and therefore eliminate the need for a case-by-case determination of whether management is acting in the best interests of the shareholders. Thus, they maintain that defensive measures are never engaged in for the best interests of the shareholders. Because of this, the argument goes, the company should remain passive and allow any predator which comes along the opportunity to feast upon the company under the premise that if this is allowed by the free market, then it must be the best and most efficient use of society's resources.

It appears that the better view is that expressed by the Ninth Circuit Court of Appeals in connection with a 1984 takeover case: "It is nowhere written in stone that the law of the jungle must be the exclusive doctrine governing parties in the world of corporate mergers." When a corporate takeover results in the liquidation of a company or some of its parts, real jobs are lost, real communities are disrupted or destroyed, and real production is lost. These events spill over into the rest of the business world where employee morale may be destroyed, corporate policies disrupted, and employees forced to live in a constant state of fear.

This is especially true of the airline industry which is among the most vital parts of the nation's transportation infrastructure. The stability of the nation's economy is dependent upon the efficient and safe transportation of people from one destination to another; transportation is the lifeblood for all communities. In light of this, the constant wrangling over who will get this air carrier or that airline not only hurts the carrier itself, but also

45. Id. at 1174-75.
46. This was precisely the philosophy of "junk bond king" Michael Milken, who was on a crusade to save corporate America from itself. He liked to generalize corporate executives as being poor managers who squandered excess capital and did not put their assets to the best use. Although these statements may be true in certain situations, Milken used this as justification for creating the junk bond market. BRUCK, THE PREDATOR'S BALL, 12 (1989)[hereinafter THE PREDATOR'S BALL].
47. The Proper Role of Target's Management, supra note 44, at 1175.
49. See generally, Dempsey, Market and Regulatory Failure as Catalysts for Political
harms the industry as a whole, thereby adversely affecting the nation. The carriers are forced to play the bidders’ game, where short-term profits are glorified and long-term stability and growth are forsaken. Speculative manipulation of corporate ownership has come to replace productive investment and competition.

D. EXAMPLES OF THE DETRIMENT OF EXCESSIVE DEBT AND TAKEOVER SPECULATION ON THE AIRLINE INDUSTRY AND THE NATIONAL ECONOMY

There have been several recent examples illustrative of the destabilization which takeover machinations in the airline industry have wrought on various aspects of the nationwide economy. Perhaps most notorious is the United Airlines fiasco which resulted in a collapse of the stock market on the day it was announced a management-led LBO of the carrier had failed. However, the United Airlines case does not stand alone. Continental Airlines, Eastern Airlines, and TWA, all victims of earlier leveraged takeovers, today find themselves in deep financial trouble. Each of these situations will be examined individually.

1. UNITED AIRLINES

United Airlines, the second largest U.S. carrier, has one of the oldest fleets of planes, and as recently as 1986, only earned $11.6 million. United also has obligations of $19 billion, for new aircraft which it has on order. Marvin Davis, a former oilman and self-styled Hollywood mogul who has no experience in running an airline, launched a tender offer for United’s parent, UAL Corp., which eventually reached $300 per share, when months earlier, UAL’s shares had been trading for around $120. Davis’s offer sent UAL stock soaring, helping to push the Dow Jones average to within ten points of the previous record high. In order to fend off this hostile attack, UAL’s management put together an LBO which had a price tag of almost $7 billion. The deal was structured so that British Airways would invest $750 million in cash equity in exchange for a 15% voting stake in UAL; 75% of the company would have been owned by UAL employees, and the remaining 10% would have been owned by UAL.


50. Can United Afford to be Taken Over?, supra note 8, at 145.
52. Id.
The agreement, however, was beset with problems from the beginning. United's machinist union asked several government agencies to investigate the deal, including the Treasury Department, the Securities and Exchange Commission, the Labor Department, and the Department of Transportation. The machinists had opposed the management-led buyout from the onset because they were not invited to participate and they had reservations that the enormous amount of debt involved would overburden the company.

The management-led LBO collapsed on ‘’unlucky’’ Friday the 13th, of October 1989. The deal was unsuccessful because the management group could not get the financing from the Japanese banks which were originally part of the agreement. These banks were very skeptical of the rosy predictions made by UAL’s commercial and investment bankers, especially in light of the bumpy, cyclical nature of the airline industry. As one senior executive of a Japanese bank was quoted as stating, UAL’s projections were “stretched — it’s a cyclical industry, and all the projections that the banks are working off are straight up. So where’s the cycle?” The Japanese banks were not persuaded that the carrier could generate enough cash to cover the interest payments, and instead believed that UAL’s advisors had overvalued many of the airline’s assets, such as the airline’s Pacific routes, which if needed to be liquidated would not have covered the value of the loan package. The banks were also wary of the opposition to the management-led deal by UAL’s 25,000 member machinist’s union. Ironically, just as Davis’s original offer for United sent the stock market soaring, the collapse of the management-led buyout sent the stock market crashing, with UAL stock plunging

55. Id.
57. Flawed Portent, supra note 56. For example, the management group projected that the carrier’s revenue would maintain an average growth rate of 10% for the next few years. It also estimated that income yields for United would increase an average of 3.5% per year. Finally, they projected that load factors would remain constant. Apparently, the management group decided that the nation would not suffer an economic downturn during the next few years.
59. Id.
$111.25.60 After this, British Airways withdrew from the deal.61

After the collapse of the $6.75 billion bid, the UAL board decided that it would seek to keep the company independent.62 The board’s announcement came as UAL’s shares were trading for $178. After the board made the announcement, the shares of UAL dropped to around $151.63 The board appeared to be in a holding pattern: it did not put the company up for sale, yet it also did not state that it would not consider a better offer. Yet, the options available to the board at this time all had potential drawbacks. For instance, if the board decided to buy-back a large portion of UAL’s stock from the public in order to make a takeover more difficult, it would probably have had to sell and lease-back its aircraft in order to gain the cash necessary to carry out the transaction. Such a transaction, however, could have conceivably resulted in a large capital-gains tax liability. Alternatively, the board stood to lose all credibility, as well as expose itself to shareholder lawsuits, if it agreed to accept a bid lower than the original LBO agreement and the financing for that bid fell through as well.64 Finally, the prospect of putting the company up for sale and then receiving no bids could also have been very embarrassing to the board.

If the board opted to do nothing to alter the previous status quo, however, it may have found itself in the proverbial “catch-22,” leaving itself open to legal challenges from those speculators and arbitragers who accumulated large positions in the company’s stock on the assumption that the airline was for sale and there would be a buyout. These arbitragers are estimated to have suffered paper losses amounting to $600 million due to the collapse of the deal.65 Indeed, many of these takeover traders purchased their stock at $280 per share with the expectation that the deal for $300 per share would materialize.66 Because over one-third of the UAL stock resided in the hands of these arbitragers, the board was vul-

61. Jouzaitis & Storch, British Airline Pulls Out of Bid for UAL, Chicago Trib., Oct. 20, 1989, § 3, at 1. There has been speculation that British Airways initially decided to become involved in the deal primarily as a means to cement a lucrative marketing relationship between itself and United. However, the Department of Transportation (DOT) has recently begun to scrutinize airline deals which involve foreign ownership of U.S. air carriers. In this particular deal, DOT expressed its view that British Airway’s involvement might have allowed it to exert effective control over United in violation of U.S. law, which states that no foreign investor can own more than 25% of a U.S. carrier.
62. UAL Tries to Keep Itself Intact, supra note 60, at 25.
63. Id.
64. Id.
nerable to a consent solicitation procedure, whereby these arbitragers/shareholders could call for a special vote to replace the members of the current UAL board.67

Six months after the $7 billion management bid for United collapsed, the UAL board broke this deadlock by accepting a $4.38 billion buyout offer made by United’s three labor unions.68 This offer includes $2 billion in wage concessions by the unions over the next five years, translating into first year pay cuts of 11% for pilots, and 7.6% decreases for flight attendants and machinists with more than five years’ seniority.69 The union bid is supported by Conniston Partners, an investor group which owns 11.8% of UAL and which has pressured the board to sell the company, threatening a proxy fight to unseat the board if it blocks any future bids.70 Once again, however, this buyout bid for United faces the serious obstacle of financing. Analysts predict that the unions will have great difficulty in lining up the almost $4.4 billion required to make this deal fly.71

In the end, all these needless machinations brought about by Davis’s original unwanted bid, partly contributed to a 38% drop in UAL earnings for the third quarter of 1989.72 Moreover, this series of events saddled UAL and its shareholders with a $58.7 million bill from investment bankers, analysts, advisors and attorneys, all participants in the failed deal.73

These figures accurately foreshadowed UAL’s net decrease in earnings during 1989 by 71% to $324 million.74 Thus, this situation, which has resulted in increases in operating costs, decreases in profits, and embarrassment for the airline, has left UAL with both unhappy shareholders and an unhappy labor force, the two key components necessary to run a viable and efficient company.75 Yet, at this point, it appears that

67. Valente & Smith, Revised Offer for UAL Corp. Being Readied, Wall St. J., Oct. 23, 1989, at A3, col.4; Trying to Land UAL, supra, note 65, at 38. Under Delaware Corporate Law (Delaware is the state of UAL’s incorporation), shareholders may act by written consent if the consents are signed by the holders of a number of shares that would have been sufficient to take the action in question at a meeting at which all shareholders were present and voting. 8 Del.C. 228 (1988).


70. Alpert, supra note 68.

71. Id.

72. Jouzaitis & Storch, UAL Earnings Fall 38% in 3rd Period, Chicago Trib., Oct. 27, 1989, § 3, at 1. United was also hurt by rising expenses, such as fuel prices and slower increases in domestic traffic.


74. Alpert, supra note 68.

75. See Ellis, Bernstein, Meehan & Friedman, This is Too Big a Genie to Put Back in the Bottle, Bus. Wk., Nov. 6, 1989, at 43. The bickering among United’s unions has intensified since the failure of the management LBO. The machinists, who favor a recapitalization for the shareholders and an employee ownership plan coupled with assurances of job protection from themselves, are angry that management was willing to profit so handsomely from the LBO without
however the events during the next few months unfold, the UAL board probably will be unable to satisfy all its constituencies. Labor would prefer increases in wages and benefits, but under the circumstances will agree to wage cuts in order to purchase the carrier and preserve their jobs; the shareholders want an increase in the value of their shares; and management may want to fortify the company's capital base to ensure future growth. With the omnipresent specter of future turmoil ahead, however, it is unlikely that any of these desires will be fulfilled soon.

2. **FRANK LORENZO'S TEXAS AIR, INC.**

Frank Lorenzo, who began his career as a financial analyst for TWA, set up a holding company, Jet Capital Corp., during the early 70's and raised cash through a public offering of its stock.\(^{76}\) This allowed him to enter the exclusive club of airline owners by using Jet Capital's funds to take over frail Texas International Airlines in 1972.\(^{77}\) Thereafter, Lorenzo and Texas Air took over Continental Airlines, and in 1986 borrowed heavily for the purchase of Eastern Airlines, assuming a $300 million annual interest liability required to service this high level of debt.\(^{78}\) Eastern is currently in the midst of bankruptcy proceedings precipitated by a fifteen month strike by its machinists, who were unhappy with what they believe were Lorenzo's anti-union policies.\(^{79}\) As a means to quell the union uprising, Lorenzo had Eastern file for Chapter 11 bankruptcy protection in March 1989. Thereafter, he replaced many of the striking union members with non-union employees.\(^{80}\)

As a result of Eastern's labor troubles and bankruptcy proceedings, the airline posted a $852 million loss for 1989, the largest single-year loss ever recorded by a U.S. carrier, leading Lorenzo's Texas Air Corp. to report a 1989 net loss of its own of $886 million.\(^{81}\) Lorenzo's other carrier, Continental, managed to post a net income of $3.1 million for 1989, after a disastrous loss of $315.5 million the previous year.\(^{82}\) This gain,


\(^{77}\) *THE PREDATOR'S BALL*, supra note 46, at 173.

\(^{78}\) Labich, *The Showdown at Eastern Airlines*, FORTUNE, April 11, 1988, at 66 [hereinafter *Showdown at Eastern*].

\(^{79}\) Debt Propelled, supra note 6, at 53.


\(^{82}\) Id.
however, came after Continental sold $60 million in assets.83

Indeed, Eastern's present position is precarious. The carrier's once highly-respected image is now significantly tarnished. Recently, in response to a substantial decline in passenger bookings after Eastern's preferred shareholders informed the bankruptcy court that they favored liquidation of the carrier, Eastern implemented a refund protection program to assure ticket holders that they would not lose money in the event of a liquidation.84 Contributing further to Eastern's tarnished image, Standard & Poor's debt-rating service has rated Eastern's subordinated debt at "D" for default.85 As if this is not bad enough, during 1988 Eastern finished last in on-time performance and had the highest number of passenger complaints except for Continental, Lorenzo's other national carrier.86

On March 1, 1990, a report filed by bankruptcy court examiner David I. Shapiro provided more fuel for the fire. The report investigated the pre-bankruptcy asset exchanges between Texas Air, Continental, and Eastern, disclosing evidence that Eastern was stripped of between $285 million and $403 million in assets, a contention strongly denied by Eastern's management.87 Approximately two months later, federal bankruptcy Judge Burton Lifland removed Lorenzo from the helm of Eastern, saying that Lorenzo and his management team were "not competent to reorganize this estate... It is time to change the captain of Eastern's crew."88 Ironically, Lorenzo's court-appointed replacement is Martin Shugrue, who Lorenzo pressured out of Continental's presidency in 1989.89

Nevertheless, Lorenzo discovered a way to transform this seemingly dismal situation into a windfall for himself. On August 9, 1990, Lorenzo resigned as Chairman and Chief Executive Officer of Texas Air [which changed its name to Continental Airline Holdings shortly after Shugrue was appointed to head Eastern] although he retained a seat on the company's board.90 Lorenzo sold the majority of his stock to Scandinavian Airline Systems for a reported $10 million, and reaped another $19.7 million in salary and severance pay. Lorenzo was replaced by Hollis L. Harris, the former president of Delta Airlines. Lorenzo, therefore, has ended

83. Ivey & DeGeorge, supra note 80, at 48.
84. Fotos, supra note 81.
85. Id.
86. Showdown at Eastern, supra note 78, at 65. During this time only 61.5% of Eastern's flights arrived within 15 minutes of schedule.
89. Id.
his tenure at the helm of Texas Air by bailing out before the ship has completely sunk.\footnote{Exiting Lorenzo Cites Bad Labor Reputation, Chicago Trib., Aug. 10, 1990, § 3, p. 1 col. 2.}

It is Shugrue who must now contend with Eastern’s myriad of problems. He must attempt not only to rebuild passenger confidence in the carrier, but also restore harmonious relations with Eastern’s employees. Shugrue’s mission, however, will be further hampered by the recent criminal indictment lodged against Eastern based upon alleged maintenance abuses. The indictment, handed down by a New York Grand Jury on July 26, 1990, charged Eastern with falsifying aircraft and safety maintenance records between July 1985 and October 1989.\footnote{Washburn & Franklin, Eastern Charges Refuel Safety Debate, Chicago Trib., July 26, 1990, § 1, p. 1, col. 2.} Yet, perhaps the most pressing of Shugrue’s problems is the handling of Eastern’s debt. Presently, Eastern owes creditors roughly $2.3 billion.\footnote{Debt Propelled, supra note 6, at 53.} Indeed, when Eastern filed for bankruptcy in March 1989, it defaulted on $1 billion in unsecured debt.\footnote{Oneal & DeGeorge, supra note 87.} At that time Lorenzo explicitly promised that Eastern would repay its unsecured creditors in full.\footnote{Id.} Thereafter, Texas Air proposed a settlement whereby creditors would be paid only fifty cents for every dollar Eastern owed.\footnote{Id.} In order to raise cash, it was rumored that Frank Lorenzo would sell part or all of Continental Airlines, which itself is in debt for $2.4 billion.\footnote{Debt Propelled, supra note 6, at 51.} Indeed, market analysts have calculated that Lorenzo’s Eastern and Continental have an incredibly high ratio of debt to capital; Continental’s amounting to 96.6% debt to capital, and Eastern’s amounting to 100.1% debt to capital, only faring better than Carl Icahn’s TWA and industry laggard Pan Am.\footnote{Vogel, Carl Icahn Has Lots of Cash. Will He Spend it on TWA?, Bus. Wk., July 17, 1989, at 86 [hereinafter Carl Icahn Has Lots of Cash].}

Shugrue has his work cut out for him in trying to bring Eastern back to life. If he is unsuccessful, however, the demise of Eastern will further increase the concentration in the airline industry. Moreover, if Eastern’s sister carrier, Continental, flies into trouble again, the airline industry and the traveling public may suffer not only one loss, but two.

3. TWA

Carl Icahn took over TWA in 1986 because, according to him, the management of the airline was inefficient and lax, as evidenced by the
fact that the carrier was losing money.\footnote{Icahn, \textit{Icahn on Icahn}, \textit{FORTUNE}, Feb. 29, 1988, at 55 [hereinafter \textit{Icahn on Icahn}].} Over four years later, TWA still finds itself in a mess. Its service is notoriously bad, its planes are falling to pieces, and labor is unhappy. Moreover, TWA's operating income lags far behind those of other carriers. While industry-wide operating income rose 33\% in 1988, TWA's increase amounted to an anemic 8\%.\footnote{Carey, \textit{Can Raiders Run What They Raid?}, \textit{FORTUNE}, June 4, 1990, at 193.} Even this figure, however, is somewhat inflated. TWA's operating income would have been $44 million less if it had not adopted an industry-accepted accounting change which served to stretch out the carrier's depreciation charges over a longer term.\footnote{\textit{Id.} at 193.} TWA's financial situation worsened during 1989. Last year, TWA lost $298 million on revenues of $4.5 billion,\footnote{\textit{Id.} at 196.} and its market share has decreased from 15.3\% to 13.1\%, each percentage decrease representing a revenue loss of more than $80 million.\footnote{\textit{Id.} at 196.} Many observers believe that TWA's problems can be traced directly to Icahn's lack of investment in the carrier. Compared to industry norms, Icahn's capital outlays for TWA have totaled a paltry 5.4\% of revenues, compared with expenditures made by American Airlines of 20\%, 18\% by Delta, and 16\% by United.\footnote{\textit{Id.} at 193.} These minuscule capital outlays prevent TWA from performing needed capital improvements, leading to increased passenger disenchantment with the carrier, directly translating into decreased revenues. Without capital investment, TWA is unable to secure a second U.S. hub to unclog the heavy traffic at TWA's St. Louis hub. The congestion in St. Louis has led to increased flight delays and baggage mishandling.\footnote{\textit{Id.} at 196.} TWA, moreover, has one of the oldest fleets of jets in the industry, a fleet in serious need of replacement. \footnote{\textit{Id.}}

In light of the financial turmoil at TWA, Icahn has turned up the heat on the carrier's pilot union in an effort to make them agree to at least $80 million in wage concessions.\footnote{\textit{Icahn's Incredible Shrinking Airline}, Bus. Wk., Feb. 19, 1990, at 42.} Icahn stated that "I'm not running the airline for the purpose of losing money. If we don't get concessions, we're going to have to shrink it."\footnote{Alpert, supra note 68.} The pilots, on the other hand, believe they have already granted enough concessions for Icahn to begin rebuilding the airline, in terms of new planes and routes, but Icahn has instead pared the carrier's assets, and it appears, he will continue to do so.\footnote{\textit{Icahn's Incredible Shrinking Airline}, supra note 107.}
For example, on February 7, 1990, TWA received permission to sell part of its reservation system to Delta Airlines. Furthermore, TWA is close to finalizing deals whereby the airline would sell $400 million worth of its aging jet fleet, thereafter leasing back the same planes. If Icahn does not receive the concessions, it is thought that he may shut down the St. Louis hub and retain the deeds to the jets still owned by TWA. He could then lease the jets to the hub’s next owner. Whatever he may do, Icahn has clearly stated that “I don’t want to preside over an airline bleeding to death.”

How did Icahn, a one-time stock trader, and of late a “greenmailer,” end up with control of TWA? How did this individual, who has stated “I enjoy collecting money,” and who, in a memo to recruit partners during 1980, wrote: “... sizeable profits can be earned by taking large positions in ‘under valued’ stocks and then attempting to control the destinies of the companies... by convincing management to liquidate or sell the company... waging a proxy contest... making a tender offer... [or] selling back our position to the company,” end up owning an airline? Initially, Icahn purchased TWA stock with the belief that he could either extract greenmail from the board, or that he could at least put the airline “in play” so that it would eventually be bought at a premium by someone else, allowing Icahn a tidy return on his investment when he tendered his shares to the new purchaser. At the worst, he would end up with an airline which he intended to partially liquidate.

Enter Frank Lorenzo of Texas Air. Up to this point, Icahn’s script was being followed perfectly. Here was the “white knight” that would rescue TWA and would present Icahn with a hefty profit of $95 million. However, complications arose which destroyed Icahn’s best-laid plans, among them the fact that TWA’s unions preferred Icahn over Lorenzo, who in 1983 had sought Chapter 11 bankruptcy protection for Continental...
Airlines, abolished union contracts and cut labor costs by 50%.\textsuperscript{119} Thus, by way of unforeseen events, Icahn found himself the owner of TWA. His often-used script had suddenly been rewritten. Icahn, however, has turned this unanticipated outcome to his own advantage. In taking TWA private, Icahn recouped his entire $436 million investment plus an additional $33 million.\textsuperscript{120}

Moreover, it may not be too surprising that, amidst the mess which TWA is in today, Icahn has come up with a new, innovative way to fatten up his war chest for future raids: sell $300 million in junk bonds, paying 16% interest, and secure them with TWA's light bulbs and spare gaskets.\textsuperscript{121} This new debt was piled on top of about $2.5 billion already owed by the airline, secured by practically all of the airline's assets. Furthermore, the airline has a negative net worth of approximately $30 million.\textsuperscript{122} Ironically, TWA documents state that it does not yet know what it will do with the additional $300 million.\textsuperscript{123} This, from an airline where interest payments alone will amount to $90 million every quarter, or $360 million per year, if this new financing goes through.\textsuperscript{124} This, however does not appear to phase Icahn, who has used TWA as an investment vehicle for his past two raids on Texaco and USX Corp.\textsuperscript{125}

II. CONCLUSION AND RECOMMENDATIONS

Although the major carriers today have tremendous market power, this does not mean they also have financial health. Only in the last two years have the carriers become profitable. Yet, because the airline industry is cyclical, the carriers' financial health is directly linked to the fluctuations in the economy. Any downturn in the economy will be accompanied by a concomitant decrease in the number of travelers, an event which will hit the industry especially hard in the coming years due to the infusion of new aircraft and thus an increased number of seats which must be filled. The industry is also keenly susceptible to changes in operating costs, such as labor and fuel prices, and also to threats of terrorism which may scare away the traveling public in droves.

The carriers' financial health may be further diminished by speculative takeovers. The recent trends in hostile takeovers shifts the focus of management to short-term results, burdens companies with excessive

\begin{footnotesize}
\begin{itemize}
  \item \textsuperscript{119} Id.
  \item \textsuperscript{120} Carey, supra note 102, at 200.
  \item \textsuperscript{121} Sandler, TWA to Sell $300 Million Notes Secured in Part by Light Bulbs, Wall St. J., June 2, 1989, at C1, col. 3 [hereinafter TWA Notes].
  \item \textsuperscript{122} Raiders May Not Make the Best Pilots, supra note 18, at 35.
  \item \textsuperscript{123} Id.
  \item \textsuperscript{124} TWA Notes, supra note 121.
  \item \textsuperscript{125} Id.
\end{itemize}
\end{footnotesize}
debt, and threatens the viability of communities. Short-term gains and takeover defenses become top priority instead of capital reinvestment to foster research and development needed to sustain long-term growth. This also shifts management's focus away from the maintenance of planes. Moreover, if a hostile raider, such as Carl Icahn or Frank Lorenzo, is successful in acquiring an airline, he may have no qualms about burying it under debt, stripping it of its assets, curtailting service, cutting corners on safety, and breaking labor contracts all in the name of their own greed. Today, the manipulation of money for speculation rather than for financing production appears to be the name of the game.

Hostile takeovers and the excessive amount of debt they create, can exacerbate any decline in ridership or profits and push the industry to the precipice of financial ruin. The consolidations and bankruptcies such a catastrophe would cause could leave the industry with one or two major carriers, and leave the public with even higher fares for even less service. This could also have repercussions throughout the entire economy, since airline transportation is an infrastructure industry vital to the health of the nation's economy.

Enlightened regulation is desperately needed, however lately it appears that Congress will only act once it is faced with a catastrophe. The recent upswing in the economy appears to be coming to an end, and the following downturn has the potential to create a catastrophe meriting Congress' attention. Congress can avoid such a melee by acting now, before the situation becomes any worse. Arguments that the financial problems existing in the airline industry merely mirror problems of other unregulated industries which are remedied by the market, simply miss the point. The airline industry cannot be equated with other industries, for the transportation of people from here to there facilitates the economic growth which a country requires to remain globally competitive. If an airline finds itself in financial trouble, moreover, Congress' own study shows that the first expense which may be cut is maintenance, and in this industry such a cut is deadly. The airline industry needs limited regulation which will help return to it the element of stability.

A. FORMULATE LEGISLATION GIVING THE GOVERNMENT BROADER OVERSIGHT OF DEBT-FINANCED TAKEOVERS

A good place for Congress to start would be to carefully redraft Section 408 of the Federal Aviation Act to cover hostile bids/acquisitions by corporate raiders. Presently, this section provides that the government has regulatory oversight over combinations of carriers only if the acquirer is "substantially engaged in the business of aeronautics." (emphasis ad-
Ironically, this language considerably narrowed the class of persons whose involvement in combinations was subject to government oversight. Previously, the statute provided that government oversight would attach when "any person engaged in any other phase of aeronautics," attempted to consolidate carriers. The statute also previously provided that government oversight would attach when "any other person [wished to] acquire control of any air carrier in any manner whatsoever." Thus, before this section of the Federal Aviation Act was re-drafted during the deregulation wave in 1978, the government had far more power to not only supervise combinations where one party was merely "engaged" in aeronautics, but also where "any person" attempted to acquire control of a carrier.

Furthermore, although there is Department of Justice oversight of anti-competitive aspects of airline consolidations, there is no similar oversight for detrimental results of hostile and/or leveraged takeovers. Perhaps Congress could draft legislation requiring an individual who wishes to acquire a carrier to show that his acquisition will not be detrimental to the public interest and that the carrier will be financially viable. The burden of proof should be placed upon the acquirer. These two changes are vitally important, for the traveling public should be worried most about acquisitions of carriers by individuals who have no experience in the airline industry and may be solely motivated by reaping windfall profits from the carrier by either stripping it of all its assets and thus rendering it non-competitive, and/or squeezing all the cash out of it and totally neglecting maintenance. The public deserves some amount of protection from such a situation.

Along these same lines, Congress should pass legislation strengthening the "fitness" requirement contained in section 401 of the Federal Aviation Act. Congress should mandate that "fitness" be determined in terms of the carrier's economic well-being, and as a way to examine its debt to equity ratio. Indeed, Transportation Secretary Samuel Skinner has made proposals along these lines. He has proposed that those carriers saddled with a great deal of debt be required to make more frequent and more detailed financial reports than other carriers. They would also need to obtain government approval before any major refinancing or major sale of assets. Recently, the financial condition of the airline

127. Id.
129. Id.
131. Can United Afford to be Taken Over?, supra note 8, at 148.
industry has also prompted action on Capital Hill, where a House Subcommitte has approved a bill vesting the Transportation Secretary with authority to review and approve leveraged buyouts of carriers.\textsuperscript{133} These recommendations could be further strengthened by a provision that all debt secured by assets of an airline be used solely for the airline, and not as a means to finance other takeovers or similar speculative transactions which have nothing to do with the airline’s well-being. Although it appears that the Bush Administration, at present, is not in favor of such legislation,\textsuperscript{134} these are good ideas which should be implemented in order to return a level of stability to this important industry.

\textbf{B. Provide Tax Incentives Favoring the Use of Equity Instead of Debt}

Another way to attack the problem of excessive debt is a tax incentive aimed at encouraging the use of equity instead of debt. At present, the country’s tax laws are definitely biased against the formation of capital and equity. For example, corporations which invest in research and development usually must account for these expenses in the years they are made.\textsuperscript{135} The depression of earnings effected by this accounting requirement may make a company look less attractive to potential investors. The expensing of research and development costs in the year incurred depresses earnings because the company cannot offset these costs against any long-term benefit it derives from the investment. In order to provide an impetus for increased funding of research and development in the private sector, Congress should make it easier for companies to match these costs against the benefits in the year derived.

In addition, the tax code requires corporate earnings to be taxed to the corporation at its tax rate. Then, if the corporation declares a cash dividend from this already-taxed income, the funds received by the shareholders are considered to be part of their gross income,\textsuperscript{136} and thus is taxed again. This amounts to double taxation. The bias in the Internal Revenue Code thus makes the payment of interest on debt, which is tax deductible, look more appealing, especially if the company is in the 35% tax bracket. A firm is allowed to deduct interest expenses, but not dividends and retained earnings.\textsuperscript{137} This, in essence, amounts to the gov-

\begin{footnotesize}
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\item \textsuperscript{134} McGinley, \textit{Transportation Chief’s Warnings on Airline LBO’s Put Him in Hot Seat Over Role in Stock Sell-Off}, Wall St. J., Oct. 17, 1989, at A30, col. 1.
\item \textsuperscript{135} I.R.C. § 174 (1988).
\item \textsuperscript{136} I.R.C. § 61(a) (1988).
\item \textsuperscript{137} I.R.C. § 163 (1988). Indeed, two highly respected commentators have stated that Section 163(a) contains a “pro-debt bias,” and that it “encourages the corporation to meet its fi-
\end{enumerate}
\end{footnotesize}
ernment paying a portion of a company's interest expenses, the percentage equal to the company's nominal tax rate.

One way to lessen the tax code's bias towards debt would be to phase out the double taxation of corporate dividends. Congress could thereby make equity look far more attractive. Equity financing is preferable for the airline industry to debt financing because debt must be repaid whereas there is no requirement for the company to pay cash dividends, and in some states, such distributions are prohibited if the company finds itself in a precarious financial position.\(^\text{138}\)

\section*{C. Require Airline Acquirers to Disclose Their Intent, Subject to Fines if They Make False Statements}

This suggestion does not advocate that LBOs or takeovers should be banned across the board, for under certain situations they effect legitimate business purposes. Instead, the focus should be on transactions performed purely for speculation. Perhaps there should be restrictions on junk-bond financing of takeovers and restrictions on the amount of debt used to purchase stock. Moreover, the government could formulate a "test" to determine whether an LBO is "good." A "good" LBO could be defined as a transaction where buyout investors intend to hold the property for the long-term, with the goal of ownership-management, as opposed to an intent to turn around and sell the company and/or strip its assets just to make a profit.

Of course, such a determination is dependent upon statements made by the acquirers. One way to ensure they provide truthful answers would be to implement a system of fines similar to that found in Section 16 of the Securities and Exchange Act of 1934, which imposes penalties for short-swing profits made on a company's stock by insiders.\(^\text{139}\) This section requires that all officers, directors, and shareholders who own 10\% of the company must file reports disclosing their stock positions in their company, and must update these every time they transact in the company's stock.\(^\text{140}\) Thereafter, if one of these insiders enters into a purchase and sale of the company's stock within six months of each other, the company can claim the profits made by the insider. Under Section 16, the corporation can claim these profits without proving that the trader used inside information: the matching of a purchase and sale within six months of

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  \item \text{nancing needs by borrowing ..." } Bitker & Eustice, \textit{FEDERAL INCOME TAXATION OF CORPORATIONS AND SHAREHOLDERS}, § 4.01, at 4-3, 4-4 (5th ed. 1987).
  \item \text{138. See Darrow, Tax Considerations — From the Company's Standpoint — In Structuring Venture Capital Investments, 45 BUS. LAW. 233, 239 (Nov. 1989).}
  \item \text{139. 15 U.S.C. § 78(a) (1982).}
  \item \text{140. 15 U.S.C. § 78ff (1982).}
\end{itemize}
each other acts as a conclusive presumption of a violation of the law.141

Similarly, then, if the airline acquirer's acts deviate from his state­ments, he could be subject to fines amounting to a percentage (or all) of
the gain reaped by selling off the airline's assets. The statute could mirror
Section 16's conclusive presumption that if the acquirer stated he would
be a manager-owner and then sells the company piece-by-piece, within,
say, two years of purchase, his acts amount to a violation of the law.

In conjunction with this, Congress should aim to formulate a policy
which recognizes that in an industry affecting the economy and the public
interest as much as the airline industry does, takeovers directly affect
c Constituencies other than the shareholders of the airlines. In these situ­
ations, the effect of the acquisition on all groups should be considered.
Perhaps legislation should require acquirers to prepare a social-impact
study of the effect of their takeover on travelers as well as the nation.

These are only a few suggestions which can start the process of
thinking of limited re-regulation of the airline industry. It is a fact that if
government regulation is dropped, then this must be replaced with a
"regulation" of a different kind: competition. This has not happened in
the case of the airline industry. The problems posed by the lack of com­
petition have been exacerbated by the trend in hostile takeovers of air­
lines and the resultant debt saddled on the carriers. Simply, deregulation
without competition does not serve the public interest. A "competitive"
market is not a self-perpetuating entity — in some cases it must be pro­
tected from anticompetitive forces by government supervision.

Airlines in the Wake of Deregulation: Bankruptcy as an Alternative to Economic Reregulation

JEFFREY S. HEUER*
MUSETTE H. VOGEL**

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I. INTRODUCTION

In 1975, an economist wrote this about the status of the airline industry:

A heated debate surrounds the issue of governmental regulation of transportation. Nowhere is the debate more intense than in air transport where the ten U.S. Domestic carriers have reported aggregate losses of $52.5 million for the first half of 1975. Regulators maintain that, while regulation has not been entirely successful, a reevaluation of the existing regulatory framework is all that is necessary. Opponents, on the other hand, argue that deregulation is the only course that can restore the industry's lost profitability.¹

The airline regulation debate continues, except now, the regulators are calling for an overhaul and intensification of the regulatory scheme and the deregulators claim reevaluation of the present program would solve a majority of the airline industry's problems.²

Critics of the current deregulated state of the airline industry cite a laundry list of airline afflictions that warrants a more paternalistic handling of the industry's affairs. Among these problems are monopolistic air fare rates in some markets, loss of small community service, lowered safety standards, predatory mergers and an overabundance of bankruptcy filings.³ To help resolve these perceived problems, specific regulatory bids are being made by a host of regulation advocates to provide for stricter policies having to do with service,⁴ safety,⁵ pricing,⁶ and market concentration.⁷ One regulator even calls for the implementation of regulations vis à vis a new federal transportation commission independent of the executive branch.⁸

Deregulators repeatedly insisted at the onset of deregulation in the late 1970's that deregulation was only intended for economic concerns—

¹ Gritta, Profitability and Risk in Air Transport: A Case for Deregulation, 7 TRANS. L.J. 197 (1975) [hereinafter Profitability and Risk].
⁵ Id. at 240-241 (increase air traffic control standards, input congressional resources in the construction of new airports, direct regulation of landing and takeoff through tariffing airlines flying at peak periods, regulation of carrier maintenance, regulation of pilot qualifications and overall stronger enforcement of current and any new promulgated regulations).
⁶ Id. at 239 (Amend Robinson-Patman Act to add services to price discrimination prohibition on goods and creation of 'mileage-based formula to assess reasonable rates').
⁷ Id. at 240 (Forced sale of single airline controlled airport hubs to new entrants, taxation of frequent flyer programs to discourage loyalty to particular airlines).
⁸ Id. at 242-244 (Independent regulatory agency that self-selects its own officers to avoid political bias of president in power).
essentially that laissez-faire policy should only dictate in competitive markets and artificial government supports should be removed to allow efficient and competitive companies to survive and weak ones to fail. Deregulation was never intended to be the basis for abandoning safety, air traffic control, or for failing to implement the antitrust and consumer protection laws. In fact, when Congress deregulated the industry, it essentially lifted only the restraints on entry into the market, price and route structure. Deregulation firmly stood and still stands for the proposition that the governmental mechanisms in place have the potential to sufficiently handle the deregulator's public interest concerns, while the market can adequately provide the most reasonable price to the consumer.

One of the mechanisms in place is bankruptcy. It will be argued in this article that bankruptcy, which functions at a microeconomic level, more adequately serves the entire airline industry than direct government economic regulation for three reasons. First, the bankruptcy courts are without power to affect those airlines which have succeeded in the deregulated era. Second, the courts have greater power and more flexibility to especially rehabilitate a failing airline. Third, bankruptcy courts, as courts of general equity, will more adequately balance the interests of the debtor-airline, creditors, employees, government, airline industry and the public.

The article is divided into three parts. The first part briefly overviews airline regulation and deregulation and summarizes the opposing views on the health of the airline industry. The second part details the delicate balance of powers allocated to the debtor and other parties in interest as provided for in the Bankruptcy Code and analyzes the fate of airlines that have entered bankruptcy in the deregulated era. Specifically, the Conti-

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9. "In testifying in favor of a statutory change mandating gradual and progressive movement toward essential reliance on competitive market forces in the long run, the Board [Civil Aeronautics Board] is not advocating a statutory deregulation of domestic air transportation - that is, Congress' removal of all regulatory controls. We do not think that we nor anyone else knows enough at this time to prescribe that in the law or precisely set forth the ultimate regime. Our recommendation for increasing reliance on competitive market was stated as being part of an integrated program which included adequate safeguards and retention of sufficient regulatory authority to step in when and if serious injury to the public interest appeared likely to result." 1977 Aviation Subcommittee Hearings, supra note 2 (statement of Hon. John E. Robson, Chairman of the Civil Aeronautics Board).

10. Had the Department of Transportation heeded the warnings of the Department of Justice, the premier antitrust agency, a series of significant mergers, e.g., United and Pan American's trans-Pacific assets, Northwest and Republic, Delta and Western, TWA and Ozark, would not have taken place and market concentration would not be of concern. See generally, Kahn, Deregulatory Schizophrenia, 75 CALIF. L. REV. 1059, 1064-65 (1986) (Kahn also questions the Department of Transportation's approval of Texas Air's acquisition of People's Express when Texas Air already owned New York Air, Continental and Eastern and had cornered 57 percent of the Newark and LaGuardia departure market).
nental, Braniff, Eastern, Airlift and Global International bankruptcies are examined in their relevant part. The third and final section sets forth the authors' opinion that bankruptcy has and will continue to serve its varied purposes. Attempts to neutralize the delicate balance will result in a less effective bankruptcy system which will inevitably culminate in a weakened airline industry.

II. BACKGROUND

A. OVERVIEW OF AIRLINE REGULATION

The airline industry was highly regulated at its inception because Congress feared it would fall into the same disastrous economic hole as the railroads and motor carriers had in the 19th and early 20th century. Congress was forced to step in and save those troubled industries as the competitors practiced policies developed under a pre-Depression government which condoned market domination of every industry aspect. Rivals had predatorily priced each other out of business and each industry suffered enormous economic losses that required liquidation and eventual dissolution of the majority of the competitors. After the destructive competition dust settled, what remained was a railroad monopoly/oligopoly extracting unreasonably high prices and a very unhealthy and chaotic motor carrier industry essentially threatening the same result. To avoid similar results in the airline industry, Congress enacted

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11. Congress passed the Act to Regulate Commerce, which called for the creation of the Interstate Commerce Commission (ICC) and a strict regulatory scheme to control interstate railroads. The Judiciary adhered to a strict view of limited federal power over commerce and struck down the powers granted the ICC. However, Congress responded by enacting further legislation expanding the ICC's power. Consequences at 14 and nn. 41 & 42. Congress also promulgated special provisions in the bankruptcy code for railroad reorganization. See 11 U.S.C. §§ 1162 et. seq. and infra at nn. 247-252 and accompanying text for a discussion of Chapter 11 reorganization for railroads. Note that one of the restraints on railroads is the inability to abandon the railroad line without strict adherence to provisions concerning replacement lines and ICC approval of abandonment. NORTON'S BANKR. LAW. ED. § 44:48 (Supp. 1989). Also note that "cashlessness" does not allow a railroad to extinguish its obligation as a common carrier, nor does it provide sufficient reason to justify abandonment, although it might make it difficult to provide service. Gibbons v. United States, 660 F.2d 1227 (7th Cir. 1981).

12. Consequences, supra note 4, at 12.

13. The motor carrier industry had an additional element that evoked public interest and Congressional attention that was absent in the railroad dilemma. The Depression created an oversupply of trucks and truckers because entry into the field was relatively easy, all that was required was a license and a truck. As each trucker went bankrupt or went out of business due to the intensive competition of shippers only meeting their short term marginal costs, the trucks were sold to other truckers and the whole process recycled again. Since the Depression had motivated Congress to erect regulatory schemes to protect against troublesome wages, working conditions and general instability, the fact that the effect on the truckers was highly visible was enough to regulate for economic and safety reasons. Consequences, supra note 4, at 15-18.
the Civil Aeronautics Act of 1938\textsuperscript{14} and the Civil Aeronautics Authority (later the Civil Aeronautics Board),\textsuperscript{15} to control the growth of the industry.

The goal of regulating the airline industry was analogous to that of the railroad and motor carrier legislation: to achieve stability in the industry.\textsuperscript{16} The regulatory scheme called for regulation of three economic areas: 1) airline entry/exit of the market, inclusive of the power to grant certification to enter the market, approval, allocation and assignment of routes, and service to certain communities;\textsuperscript{17} 2) rates and air fares;\textsuperscript{18} and 3) antitrust.\textsuperscript{19} The Civil Aeronautics Board (CAB) was granted the power to interpret the regulations in light of the Congressional purposes for promulgating the statute.\textsuperscript{20}

The next forty years of regulation led to such stability that the market became stagnant, concentrated and began to lose profitability.\textsuperscript{21} Among the problems complained of were constraints on the innovation of service

\begin{itemize}
  \item \textsuperscript{14} In 1958, the name of the act was changed to Federal Aviation Act. The Federal Aviation Act, which was amended by the Airline Deregulation Act in 1978, is codified at 49 U.S.C. §§ 1301 et.seq. (Supp. 1989).
  \item \textsuperscript{15} In 1939, the Civil Aeronautics Authority name was changed to the Civil Aeronautics Board. Dempsey, \textit{Rise and Fall of the Civil Aeronautics Board - Opening Wide the Floodgates of Entry}, 11 TRANS. L.J. 91, 93, note 2 (1979) [hereinafter \textit{Rise and Fall}].
  \item \textsuperscript{17} 49 U.S.C. § 1371.
  \item \textsuperscript{18} id. at § 1374.
  \item \textsuperscript{19} id. at § 1384.
  \item \textsuperscript{20} The Congressional policy statement for the Civil Aeronautics Board is as follows:
    In the exercise and performance of its power and duties under this chapter, the Board shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity:
    (a) The encouragement and development of an air-transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the United States Postal Service, and of the national defense;
    (b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure the highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by, air carriers;
    (c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;
    (d) Competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the United States Postal Service, and of the national defense;
    (e) The promotion of safety in air commerce; and
    (f) The promotion, encouragement, and development of civil aeronautics.
  \item 49 U.S.C. § 1302.
  \item \textsuperscript{21} To reemphasize, the airline industry lost $52.5 million in the first half of 1975. \textit{See supra} note 1.
alternatives, restricted market entry and lack of competitive pricing. Many rationales were cited for the problems plaguing the industry. One of the strongest was that CAB regulation in the mid-70's governed a different economic environment than existed when regulation was instituted. Regulation of the airline industry was desirable when the economic environment after the Depression was favorable and technology was rapidly changing. Forty years later, deregulation became favorable because the economic environment caused sluggish productivity, moderate traffic growth and rising costs. Another reason given for the slow market was that the CAB maintained a *de jure* policy of denying certification requests. In 1938, 21 main route carriers served the then 48 states. In 1976, only 10 were left. Of the mid-size carriers, only 7 survived of the 17 carriers originally certified and in the local service market, only 8 carriers remained of the 32 certified.

The chairman of the CAB testified to the Aviation Subcommittee of the House of Representatives that regulation resulted in greater inefficiency because it,

> [I]Induced costly inefficiencies through overscheduling, overcapacity, competition in frills and equipment races . . . . It has not provided the environment or the incentives for the basic price competition. Because of these inefficiencies, and the regulatory system's insulation of labor-management bargaining, neither the airline investor nor the consumer has fully reaped the potential benefits of the industry's enormous past productivity gains and growth. Nor has regulation produced a financially strong airline industry.

In fact, several published studies examined deregulated intrastate markets, and maintained that CAB regulation brought about the inefficiency and effectuated higher fares than would have resulted had the CAB not controlled the industry. In 1975, the CAB took up the matter and considered the effect of the proposals for deregulation and determined that the "airline industry 'is naturally competitive, not monopolistic,' and that regulation caused higher-than-necessary costs and prices, weakened the

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24. *Id.* at 73 ("... despite the tremendous growth of commercial aviation, the existing system of regulation has certainly not expanded the number of significant participants or reduced concentration.") (remarks of CAB Chairman Robson).

25. *Id.* at 70 (remarks of CAB Chairman Robson).

26. *Profitability and Risk*, supra note 1, at 197-98, n. 2 (citing W.A. JORDON, AIRLINE REGULATION IN AMERICA: EFFECTS AND IMPERFECTION, 226 (1970) (deregulated intrastate California carrier study that showed rates were 47% lower than they would have been under the CAB) and G.W. DOUGLAS and J.C. MILLER III, ECONOMIC REGULATION OF DOMESTIC AIR TRANSPORT; THEORY AND POLICY, (1975) (study reached similar result that deregulated Texas intrastate market had lower fares); *Deregulation and the Troglodytes*, supra note 22, at 299, n. 8 (citing in addition to Gritta's sources, Keeler, *Airline Regulation and Market Performance*, BELL J. ECON. & MGMT. SCI. 399 (1972); R. CAVES, AIR TRANSPORT AND ITS REGULATORS: AN INDUSTRY STUDY (1962).
ability of carriers to respond to market demands and narrowed the range of price/quality choices available to the consumer." The CAB report concluded that the regulations treating the industry as a public utility should be abandoned in the three to five year time span.

In 1978, federal legislation was passed which reflected the CAB's view of regulation and the findings of the Congressional hearings which examined the pros and cons of deregulation. To date, the Air Deregulation Act of 1978, which amended the Federal Aviation Act, comprises the deregulated provisions. The relevant parts of the Act required the following:

1. Federal subsidization for air carriers in small communities with a prohibition against discontinuing essential service until the CAB can find a satisfactory replacement.
2. Fares falling within a "zone of reasonableness" are not suspendable or subject to the jurisdiction of the CAB or the Department of Transportation upon the dissolution of the CAB.
3. Two or more carriers may not merge if unlawful according to the consolidation and merger guidelines in the Act.

The intended consequences of airline deregulation all fell under the umbrella of shifting the focus of regulation from ensuring the "well-being of the aviation industry, to making service economically available to more of the American public." Deregulating pricing, market entry and routes would allow competition in these areas, instead of granting automatic profit to the airlines at the consumers' and investors' expense. Deregulation promised:

Wide-open competition, with the free entry of new firms 'policing' the market, and assuring adequate reasonably-priced service; substantial fare reductions; deregulation would provide the public with new price/service options, such as lower-fare, no-frills service; benefits of deregulation would be equitably distributed and markets that lacked their own direct competition would benefit from the constant threat of competition from new entrants, and by providing freedom to compete in pricing, deregulation would obviate the pre-

27. Deregulation and the Troglodytes, supra note 22, at 301, n. 11 (quoting Executive Summary of Report of the CAB Special Staff on Regulatory Reform at 1 (1975)).
28. Id.
29. See generally, 1977 Aviation Subcommittee Hearings supra note 2; Senate Subcomm. on Administrative Practice and Procedure, 94th Cong. 1st Sess., Airline Regulation of the Civil Aeronautics Board (Comm. Print 1975) [hereinafter 1975].
31. Id. at § 1389.
32. Id. at § 1482.
33. Id. at § 1378. Section 1551(a)(7) of the Transportation Federal Law transferred the authority over antitrust from the Secretary of Transportation to the Department of Justice as of January 1, 1989.
34. 1975 Airline Regulation Hearings, supra note 29.
vious need to compete in service, and would particularly eliminate scheduling pressure and resulting excess capacity.\textsuperscript{35}

The deregulators were not without warning in their pursuit of limiting the government's role in the industry. Critics of deregulation cautioned that reform would not bring the results that deregulation advocates hoped for. Specifically, the predicted effects were abandoned service, capital starvation, possible carrier failure, employee hardship, excessive industry concentration and destruction of the U.S. air system.\textsuperscript{36} Whether or not these predictions came to life, suggesting that the industry cannot survive in a deregulated state, is discussed below.

\section*{B. Health of the Airline Industry}

Just how healthy the airline industry is depends on whether a follower of John Maynard Keynes or Adam Smith is conducting the examination. A determination of whether the airline industry has fared well under deregulation also depends on at what stage the inquiry is taking place.

Immediately after the Deregulation Act was signed into law, the industry appeared to flourish with the entry of new carriers into new routes. The incumbent carriers experienced major increases in loads.\textsuperscript{37} The industry was profitable and consumers felt the results of deregulation in lower fares.

However, as early as 1979, the airline industry took a public relations nose-dive. Reports of industry-wide problems began to appear. Losses for late 1979 and early 1980 totaled $500 million.\textsuperscript{38} Service was discontinued in 49 cities.\textsuperscript{39} Many of the airlines experienced large Federal Aviation Administration maintenance fines.\textsuperscript{40} Airlines attempted to recover their operating losses by increasing fares in the monopoly markets.\textsuperscript{41}

There are a number of rationales for the appearance of early failure on the part of deregulation. In early 1979 and 1980, fuel prices doubled due to the OPEC oil embargo and in response, the CAB allowed the air-


\textsuperscript{36} 1977 Aviation Subcommittee Hearings, supra note 2, at 70.

\textsuperscript{37} Deregulation and the Troglodytes, supra note 22, at 303.


\textsuperscript{39} Consequences, supra note 4, at 29.

\textsuperscript{40} Id. at 31, citing Gonzales, \textit{Airline Safety, a Special Report}, \textit{Playboy}, July, 1980, at 140, 209 (the fines assessed against the airlines were $1,500,000 against Braniff; $385,000, PSA; $166,000, Prinair; $500,000, American; and $100,000 Continental).

\textsuperscript{41} CONSEQUENCES, supra note 4, at 37.
Airlines in Wake of Deregulation

lines to raise fares 31 percent to compensate. The economy was in a recession, interests rates were extraordinarily high and the PATCO strike handicapped the industry.

The industry's immediate plunge after passage of the Deregulation Act was viewed as the fault of deregulation by the deregulation critics. The criticism was that without regulation, entrants were allowed to freely enter the market, destructive competition followed and the losses piled up without any controls. Nearly $2 billion in overall losses were suffered from 1979 to 1983. The fact that Air New England, Braniff, Continental, El Al, Laker, and 16 other air carriers entered various stages of bankruptcy after the promulgation of the Airline Deregulation Act of 1978 was enough to show that the market virtually chewed up and spit out the airlines daring enough to enter the market. The theory of contestability heralded by the deregulators, that the threat of new entrants into the market will keep the market competitive and fares reasonable, was also being chewed up and spit out as each new entrant either merged into another line or totally stopped operating.

Today, regulation proponents fault deregulation for an unacceptable, oligopolistic industry that has cut costs and safety standards to increase profits. Regulators are concerned that the industry is too highly concentrated without rate regulation to control the monopoly markets. Regulators find no solace in the market's current profitability and they claim that any success enjoyed by the incumbent airlines are the result of monopoly extracted profits, reduction in service and diminished labor costs.

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43. CONSEQUENCES, supra note 4, at 39.
44. Id.
46. In support of their view of the industry, those in favor of stricter regulation of the industry can cite to overall industry losses of $6.7 billion in the first eight years of deregulation versus the $2.2 billion profit realized in the eight years preceding passage of the Act. M. Brenner, Airline Deregulation-A Case Study in Public Policy Failure, 16 TRANSPI. L.J. 179, 224 (1988). The optimistic studies that claim deregulation has actually increased profitability by $2.5 billion are neutralized by the charge that the recession and high fuel prices were not factors by 1986 and the
Finally, the regulators, who lack an understanding of the function of bankruptcy, assert that deregulation is a failure because of the 150 bankruptcies that have been filed over the history of deregulation. Supposedly this number evidences a plagued industry with a doubtful recovery because few are willing to enter a market where so many companies have gone belly up.

On the other hand, deregulators claim that the industry was only able to recover from the dismal state in the early 1980's because deregulation allowed the airlines the ingenuity to create alternatives for survival. The former CEO of Southwest Airlines claimed that the problems in the industry were not created by the deregulation of fares and route structures, but by other factors that were unforeseeable by Congress, such as the high interest rates, high fuel prices and highly leveraged carriers facing unexpected increases in cost.

Deregulators are quick to refute complaints of high concentration in the market with a reminder that the CAB, or later, the Department of Transportation, approved all the mergers that were proposed and that because of this, antitrust jurisdiction was transferred to the Department of Justice. Deregulators also argue that markets with only one carrier should be regulated, that monopoly pricing should not be allowed to occur because the fare does not reflect the market forces. Deregulators are quick to point out that promoting regulation based on the fact that deregulation allows the market to extract monopoly pricing is unfounded. If stronger antitrust enforcement is desired, then enforce the antitrust laws and remove or amend the antitrust exemption for airlines from the federal transportation laws.

In fact, proponents urge that deregulation has allowed the industry to produce "societal benefits." Lower fares reflect market forces at a cost savings of $11 billion a year and as another example, approximately 90 percent of all passengers traveled in 1986 on fares that were 61 percent

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industry's net did not yet exceed its interest payments even after those external problems had ceased. The Brookings study published in 1986, made such a claim and also asserted that deregulation aided the public by $6 billion a year. See S. MORRISON & C. WINSTON, THE ECONOMIC EFFECTS OF AIRLINE DEREGULATION (1986); But c.f., M. Brenner, A Case Study in Public Policy Failure 16 TRANSP. L.J. at 224 (which asserts that the profit margin was negative 0.7% in 1986 versus the 2.7% that it had been prior to the Deregulation Act).

47. Deregulation and the Troglodytes, supra note 22, at 304.
48. Id. at 303-304; R. Gritta, Bankruptcy Risks Facing the Major U.S. Airlines, 48 J. OF AIR L. & COM. 90 (1982) (prediction that conservatively financed airlines through the issuance of stocks, were able to survive and liberally-financed companies that acquired capital through assumption of debt, would fail).
49. 49 U.S.C. § 1384.
below the coach fare.\textsuperscript{51}

The bottom line of the deregulation argument is that while the industry has experienced a large number of bankruptcies in the past eleven years, this is not a sign of a weakened industry necessarily failing. Bankruptcy, discussed at length below, is the proper forum to handle rapid growth and an equally rapid attrition of the many new entrants into the airline industry.

III. ANALYSIS

A. INTRODUCTION TO BANKRUPTCY USES

The United States Bankruptcy Code (Code), enacted in 1978, was a Congressional attempt to conform the bankruptcy laws to prevailing business realities.\textsuperscript{52} A cornerstone of the Code is Chapter 11, Reorganization.\textsuperscript{53} Chapter 11 has multiple purposes: to relieve the debtor from immediate payment of pre-petition debt;\textsuperscript{54} to reorganize the debtor's finances;\textsuperscript{55} to return the debtor to the marketplace as a viable enterprise;\textsuperscript{56}

\begin{itemize}
\item \textsuperscript{51} ld. at 237.
\item \textsuperscript{52} 11 U.S.C. §§ 101 et seq.
\item \textsuperscript{53} ld. at §§ 1101-1174. While Chapter 11 will be the primary focus of this article, Chapter 7 will also be explored in part. The focus of Chapter 7 is more limited and concerns the liquidation of the corporate debtor's assets and distribution of those funds in accordance with the priority scheme as enumerated in the Bankruptcy Code. R.E. Ginsberg, 1 Bankruptcy: Text, Statutes, Rules 1031 (2nd ed. 1989) [hereinafter Ginsberg].
\item \textsuperscript{54} 11 U.S.C. § 362. § 362 creates an automatic stay as to all legal actions affecting the bankruptcy estate. § 362 applies to the following proceedings:
\begin{itemize}
\item (1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;
\item (2) the enforcement, against the debtor or against property of the estate, of a judgement obtained before the commencement of the case under this title;
\item (3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;
\item (4) any act to create, perfect, or enforce any lien against property of the estate;
\item (5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;
\item (6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of a case under this title;
\item (7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and
\item (8) the commencement or continuation of a proceeding before the United States Tax Court concerning the debtor.
\end{itemize}
\item \textsuperscript{55} Gerstell, Hoff-Patrinos and Morgan, Alternatives to Chapter 11 and Contingency Planning for a Chapter 11 Filing in Aviation Industry Bankruptcy Issues, 43 Com. L. & Prac. 391 (1986) [hereinafter Alternatives to Chapter 11].
\end{itemize}
to reform or rescind burdensome contracts;\(^5\) to provide continued employment to the debtor's workforce;\(^6\) to treat creditors in an even-handed manner;\(^7\) to further the public interest;\(^8\) to attempt to ensure the stockholders a fair return on their investment;\(^9\) and to consolidate in as great a manner as possible all of the debtor's widespread interests. Companies seek the bankruptcy court's protection for reasons that include cash flow problems, generally inclement economic conditions, ineffective labor and contract situations and to stay litigation.\(^10\)

In order to balance these varied and conflicting purposes and reasons for bankruptcy, the bankruptcy courts have been given wide powers to decide all "core proceedings" concerning the debtor's estate.\(^11\) The bankruptcy courts are courts of equity and may issue any order, process

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59. Alternatives to Chapter 11, supra note 55, at 44.


61. Corporate Management Tool, supra note 56, at 64.

62. Id.

63. 28 U.S.C. § 157 includes a list of possible core proceedings. Core proceedings include, but are not limited to:

(A) matters concerning the administration of the estate;
(B) allowance or disallowance of claims against the estate or exemptions from property of the estate, and estimation of claims or interests for the purposes of confirming a plan under chapter 11, 12, or 13 of title 11 but not the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death claims against the estate for purposes of distribution in a case under title 11;
(C) counterclaims by the estate against persons filing claims against the estate;
(D) orders in respect to obtaining credit;
(E) orders to turn over property of the estate;
(F) proceedings to determine, avoid, or recover preferences;
(G) motions to terminate, annul, or modify the automatic stay;
(H) proceedings to determine, avoid, or recover fraudulent conveyances;
(I) determinations as to the dischargeability of particular debts;
(J) objections to discharges;
(K) determinations of the validity, extent, or priority of liens;
(L) confirmations of plans;
(M) orders approving the use or lease of property, including the use of cash collateral;
(N) orders approving the sale of property other than property resulting from claims brought by the estate against persons who have not filed claims against the estate; and
(O) other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship, except personal injury tort or wrongful death claims.

or judgement to carry out the Code.\textsuperscript{64} In Chapter 11, the management remains firmly in place and is called the debtor-in-possession (DIP).\textsuperscript{65} The DIP is given a wide range of rights and powers in order to reorganize.\textsuperscript{66} Wary that the management may have been partially or fully to blame for the debtor’s necessity in seeking relief in bankruptcy, the Code has provided creditors and parties-in-interest a wide variety of countervailing rights.\textsuperscript{67}

\textsuperscript{64} 11 U.S.C. § 105.
\textsuperscript{65} Id. at § 1101
\textsuperscript{66} The debtor-in-possession is granted substantial rights and powers in accordance with § 1107 of the Code. These include the protection of the automatic stay, the right to reject or assume executory contracts, the right to reject collective bargaining agreements, the right to use, sell or lease property, the right to obtain credit and the right to exercise avoidance powers. 11 U.S.C. §§ 362-365, 1113, 544, 545, 547 and 548. The debtor-in-possession is entrusted with all the rights, powers, duties, and limitations of a bankruptcy trustee, save for the right to receive statutory compensation under § 330. Id. at § 1107. The debtor-in-possession is authorized to operate the debtor’s business. Id. at § 1108.
\textsuperscript{67} 11 U.S.C. § 1109 allows certain parties in interest to be heard on any issue in a Chapter 11 proceeding. These parties include the Securities and Exchange Commission, the creditors’ committee, equity security holder’s committee, creditors, equity security holders, the debtor and the trustee (if one is appointed). 11 U.S.C. § 1109(a) and (b). While “parties in interest” includes the debtor and debtor-in-possession, the term as used in this article will exclude those parties. This is done as a matter of style rather than to recite all possible parties in interest or by referring only to a term such as “creditors” which may be underinclusive. This power to be heard is a strong counter balance to the notion that a debtor-in-possession has virtually unlimited powers to further its own agenda in disregard of other interests. Additionally, individual sections of the Bankruptcy Code provide that notice be given and an opportunity to be heard to parties affected outside of those who have an automatic right to be heard. Parties in interest are given two types of rights: procedural and substantive.

Procedural rights can be referred to as the rights to notice and hearing. These rights are important as they give parties in interest the right to information about actions the debtor-in-possession must necessarily bring forth for court approval. Further, the procedural rights to notice and hearing are often the springboard to the substantive rights discussed below.

By requiring notice and hearing, the debtor-in-possession is on alert that parties in interest will know about its actions and will be able to object or negotiate the terms of the action. Notice and hearing is necessary for the debtor-in-possession to use, sell or lease property outside the ordinary course of business, 11 U.S.C. § 363(b), to obtain credit and incur debt outside the ordinary course of business, Id. at § 364(b), the allowance of an administrative expense, Id. at § 503(b), actions under the avoidance powers, Id. at §§ 544, 545, 547-50, and the abandonment of property, Id. at § 554.

While the procedural rights are undoubtedly important, the substantive guarantees of the Code allow parties in interest to defend their rights and interests and effect the general direction of a Chapter 11 proceeding in both its pre- and post confirmation stages. Under Chapter 11, the greatest source of rights for secured creditors derives from the theory of “adequate protection,” Id. at § 361, while the greatest source of power for unsecured creditors is the ability to form a creditor’s committee with its attendant rights to information and investigation. Id. at §§ 1102 and 1103. Finally, the secured and unsecured creditors have a right to examine the reorganization plan and vote on the plan. Id. at §§ 1125(b) and 1128.

Some commentators have suggested that the powers given to parties in interest are insufficient “for them to exercise meaningful control or to make their participation profitable.” LoPucki, The Debtor in Full Control-Systems Failure Under Chapter 11 of the Bankruptcy Code, 57 AMER.
To determine the relative benefits of bankruptcy to the airline industry, it is necessary to study how various airlines and parties in interest have fared in bankruptcy in the deregulated era. This first part of the section will analyze the actual and potential uses of the bankruptcy courts by various parties. The second section will detail the results of airlines in bankruptcy. It is hoped that after a thorough analysis of the activities of airlines in Chapters 7 and 11, one is left with the firm conviction that the bankruptcy courts are less intrusive, more flexible, more equitable and are quicker to respond than an administrative agency. Consequently, the public is served by lower fares and better service; management is spurred by competition to think aggressively and innovatively; labor is encouraged to take a more active role in corporate well-being through an increase in efficiency and participation; creditors are served by a single forum in which to recoup their debt and, finally, government energy is better channeled into enforcing antitrust and consumer protection laws.

B. THE USAGE AND POTENTIAL USAGE OF CHAPTER 7 AND 11 IN THE AIRLINE INDUSTRY

1. FILING A BANKRUPTCY PETITION IN "BAD FAITH"

The initial question parties in interest may seek to determine is whether a case was filed in bad faith. If it is filed in bad faith, the proceeding must be dismissed. The bankruptcy court was faced with this question in Continental's bankruptcy proceeding. In Continental, the Airline Pilot's Association (ALPA), the Union of Flight Attendants (UFA), and the International Association of Machinist and Aerospace Workers (IAM) challenged the good faith bankruptcy filing of the airline. After a long set of hearings, the court found that Continental did not file bankruptcy solely or primarily to modify its collective bargaining agreement.

BANKR. L.J. 99, 248 (1983). A non-use of powers granted such as the right to bring an involuntary petition, to form creditor's committees, to use the creditor's committees' powers and to propose plans of reorganization has resulted in the debtor remaining in full control. Id. at 247-48. This may be the case in certain reorganization plans where there is little hope of reorganization or of recovering the debt owed. (Essentially, why throw good money after bad?) However, the rights are very real and powerful, and exercised when necessary.

68. 11 U.S.C. § 1129(a) sets forth the requirements that must be met before a Chapter 11 reorganization plan may be approved. § 1129(a)(3) requires that the plan be proposed in good faith.


70. Id. at 69. The debtors and unsecured trade creditors opposed the petitioner's motion. The action by the petitioners was apparently taken in response to new wage rates and rules unilaterally implemented by Continental. Unilateral changes were allowable in pre § 1113 proceedings.

71. Id. at 71. The court heard testimony on the issue of good faith for 11 days and reviewed extensive briefs. See infra nn. 174-184 and accompanying text for further explanation of collective bargaining agreements [hereinafter CBA] in the bankruptcy context.
Rather, the court found that Continental had not paid $42 million in trade debt on time, "was in violation of its liquidity provisions with secured lenders," would run out of cash within one week and had no credit. 72

Given the difficulty in proving "bad faith" and the burdensome debt and dire straits that Continental faced, bankruptcy was its only option. 73 Continental's objectives in filing the petition, to reduce mounting debt, to gain adequate credit, to preserve jobs, and to restore consumer confidence, were "consistent with the purposes, spirit and intent of that statute." 74 Therefore, while it is in bad faith to file a bankruptcy petition solely for the purpose of modifying or rejecting a collective bargaining agreement, it is perfectly within the debtor's right to file a petition even if one of its intentions, *inter alia*, would be to reject a collective bargaining agreement in furtherance of other legitimate bankruptcy objectives. 75

2. Property of the Estate

Another initial question is what constitutes property of the estate under § 541. An estate is created at the commencement of a bankruptcy petition and the property of the estate consists of "all legal or equitable interests" of the debtor. 76 An issue that arose in the first Braniff bankruptcy was whether "slots" are property of the estate. 77 Slots are the landing and take-off rights granted to an airline. 78 The court ruled against Braniff and determined that slots were not property of the estate. 79 Rather, the court found that the Special Federal Aviation Regulation established slots as "rules" of the Federal Aviation Administration. 80 "Slots are actually restrictions on the use of property-airplanes; not property in themselves." 81

This case does not seem to comport with bankruptcy analysis on at

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72. *Id.* at 70. "This court would reject any argument that a financially troubled company, which is losing money and is insolvent . . . is unable to pay its debts as they mature, has no credit and no free assets, and is about to run out of cash; nevertheless, cannot file a Chapter 11 proceeding if rejection of its collective bargaining agreements is a planned element in the reorganization of its business."

73. *Id.* at 71. The unsecured trade creditors testified that if the case were dismissed, they would have filed an involuntary bankruptcy petition under 11 U.S.C. § 303.

74. *In re* Continental Airlines Corp., 38 Bankr. at 71.

75. *Id.* at 71.

76. 11 U.S.C. § 541(a)(1).

77. *In re* Braniff Airways, Inc., 700 F.2d 935 (5th Cir. 1983).


79. *Braniff*, supra note 77, at 942.

80. *Id.* at 942 (noting Northwest Airlines, Inc. v. Goldschmidt, 645 F.2d 1309 (8th Cir. 1980)).

81. *Braniff*, supra note 77, at 942.
least two levels. The Fifth Circuit admitted that the slots may "rise to some limited proprietary interest."\textsuperscript{82} The court then stated that because licensing and certification remain subject to the "jurisdiction and approval of the applicable agency,"\textsuperscript{83} jurisdiction vested outside the bankruptcy court. If the estate retains an interest in the property, jurisdiction should co-exist with the bankruptcy court and the administrative agency because the concept of property of the estate is very broad. The DOT should, therefore, seek the modification of the automatic stay because its actions would affect the rest of the estate or object to the sale of the slots and gates.\textsuperscript{84}

Another basis for questioning the continuing validity of this holding is the fact that the Department of Transportation currently allows the sale and purchase of slots.\textsuperscript{85} At least one recent instance was the purchase of eight gates by Midway Airlines from Eastern in Philadelphia.\textsuperscript{86} Further, the bankruptcy court in the Eastern proceeding approved the sale of Eastern's Latin American routes, slots and miscellaneous equipment to American Airlines for $349 million.\textsuperscript{87} Because the DOT now recognizes the sale of slots, gates and routes and because it seems apparent that the debtor-in-possession retains at least a limited property interest in slots, routes, and gates, the continuing validity of \textit{Braniff} must be questioned.

\section{3. § 362: THE AUTOMATIC STAY}

Most judicial and administrative actions taken against the debtor are stayed pursuant to 11 U.S.C. § 362.\textsuperscript{88} But the police and regulatory ex-

\textsuperscript{82} Id.
\textsuperscript{83} Id.
\textsuperscript{84} § 362(a) and see infra at nn. 88-101 and accompanying text. Section 363(b)(2)(A) requires the DIP to give notice when selling property. See infra n.121.
\textsuperscript{85} Airline Operations, supra note 78, at 522.
\textsuperscript{86} Chicago Tribune, Nov. 16, 1989, § 2, at 1, col. 2.
\textsuperscript{87} Chicago Tribune, Mar. 30, 1990, § 3, at 3, col. 1.
\textsuperscript{88} 11 U.S.C. § 362 automatically stays a wide array of actions that could be taken against a debtor but for the filing of a bankruptcy petition. The automatic stay takes effect immediately upon the filing of a bankruptcy petition, § 362(a). These actions include commencing or continuation of judicial or administrative proceedings, the enforcement of judgments, the attempt to gain possession of property and to create or perfect liens. 11 U.S.C. § 362(a)(1). For a full listing, see supra note 63. This section affords the debtor a "breathing spell" from the payment of pre-petition debt. H. Rep. No. 95-595, 174; H & H Beverage Distributors v. Dep't of Revenue, 850 F.2d 165 (3rd Cir. 1988). It also affords the debtor the right to consolidate many claims into the bankruptcy proceeding rather than defend itself in multiple forums subject to conflicting decrees. Kommanditselskab Supertraus v. O.C.C. Shipping, Inc., 79 Bankr. 534 (Bankr. D.C.N.Y. 1987).

For a party to proceed in an action against the debtor outside the bankruptcy forum, the debtor must modify the automatic stay or be specifically excepted. The exceptions are reviewed infra at note 89. A creditor must prove that it is not adequately protected or the debtor retains no equity in the property and the property is not necessary to an effective reorganization. Typically, this provision is enforced upon motion of a secured creditor seeking the return of their collateral.
ception to the stay exempts most governmental actions that protect health, safety, welfare and morals. It is generally recognized that the National Labor Relations Board is exempt from the automatic stay. By analogy, the Railway Labor Relations Board should be similarly exempt.

In the Continental bankruptcy, the National Mediation Board (NMB) was not automatically excepted from the stay. The NMB contended that the election was not a proceeding against the debtor and that it was governed by the police power exception. The bankruptcy court found both arguments unpersuasive, holding that the election proceedings were clearly between the International Brotherhood of Teamsters and the airline. Further, the court found that the NMB "investigates . . . conducts elections and it certifies in representation disputes. It has no enforcement authority."
Continental also faced problems from the Airline Pilots Association (ALPA). The ALPA scheduled 317 pilots of Continental to attend disciplinary hearings at the same date and time. The court found this action would result in irreparable harm to the airline by forcing Continental to cancel flights for three days, would damage Continental’s reputation and goodwill and thus constituted interference with the debtors assets and operations. The court also found that the hearings constituted an “unreasonable harassment” of Continental.

Both Continental decisions make perfect sense in a bankruptcy setting. The police power exception to the stay is narrow. It is important to remember that the stay may be lifted in the proper circumstances. That is essentially what Continental requested in the NMB case. The court also proceeded, quite equitably, to hold that while the ALPA’s actions violated the stay, the actions could be undertaken over a longer period, so as not to disrupt the airline’s operations. Therefore, a corporation in bankruptcy is protected from unwarranted harassment, including harassment by employees.


The recovery of airline equipment is not affected by the automatic stay. Section 1110’s scope has come into conflict with other provisions of the Code. The specific conflict in the bankruptcy of Airlift International was the relationship between § 365 and § 1110, and the estate’s

96. Id. at 127.
97. Id. at 128. Action that interferes with the debtor’s estate violates the automatic stay.
98. Id. at 129. The court explained that the debtor’s interest would be far more damaged than the union’s interest as the union “would be required to merely reschedule the hearings” over a longer period.
99. See supra note 89.
100. In re Continental Airlines, Corp., 40 Bankr. at 301.
102. 11 U.S.C. § 1110(a). The Code makes special provisions for the secured creditors of aircraft equipment. Section 1110 is a limited exception to the automatic stay for the secured creditors of “aircraft, aircraft engines, propellers, appliances or spare parts.” The purpose of section 1110 is to “encourage new financing in the transportation industry and to promote industry modernization by protecting equipment financiers.” Alternatives to Chapter 11, supra note 55, at 312. The creditor may repossess aircraft equipment without seeking the lifting of the automatic stay. 11 U.S.C. § 1110(a). The debtor-in-possession may prevent the repossession by curing all defaults that occurred within 60 days of filing the bankruptcy petition, perform in accordance with the financing agreement and cure all post-filing defaults “before the later of (i) 30 days after the date of such default; and (ii) the expiration of such 60-day period.” Id. at § 1110(a)(2)(B).
liability because of its use of an aircraft. The conflict also involved what priority payment the secured lender was entitled to. The appellate court found that the Congressional intent behind § 1110 mandated GATX to receive the full amount of failed payments up to the date of surrender of the airplane and the payments be accorded an administrative expense. The court rejected the bankruptcy court's analogy of § 1110 to § 365. Because the theory of § 1110 was to offer "equipment financiers greater certainty with regard to their ability to protect collateral in bankruptcy," the bankruptcy court's determination wholly under-compensated GATX. Further, the estate is liable for the full contract if it assumes the contract during bankruptcy proceedings. The same is true under § 1110 except the debtor may cut liability by return of the aircraft. Thus, because the aircraft was a necessary component to the bankruptcy proceeding, GATX was entitled to an administrative expense.

Section 1110 was also at the center of controversy in further litigation in the Airlift International bankruptcy. The issue was "whether a stipulation entered pursuant to § 1110 precludes a trustee in bankruptcy from recovering preferential transfer under . . . § 547." The appellate court found § 1110 required all defaults be cured prior to retaining the air-

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103. In re Airlift International, Inc., 26 Bankr. 61 (Bankr. Fla. 1982); In re Aircraft International, Inc., 761 F.2d 1503 (11th Cir. 1985). The debtor-in-possession is given the right to assume or reject executory contracts and unexpired leases under Code section 365. An executory contract is one "in which performance remains due to some extent on both sides." N.L.R.B. v. Bildisco, 465 U.S. 513, 522 n. 6 (quoting H.R. Rep. No. 95-595 at 347 (1977)). This ability to assume or reject commercial contracts remains a strong weapon in the arsenal of the debtor-in-possession to jettison burdensome contracts and retain contracts necessary to a successful reorganization. This right to assume an executory contract is conditioned on the debtor-in-possession curing a default or adequately assuring that a default will be cured and future performance adequately assured. 11 U.S.C. § 365(b). Further, the rejection of an executory contract constitutes a breach of contract to which a creditor is entitled to file a proof-of-claim. 11 U.S.C. § 365(g)(1).

104. In re Aircraft Intern., Inc., 761 F.2d 1503 (11th Cir. 1985). The debtor and the secured lender, GATX, entered into a stipulation under § 1110 for the use of an aircraft. Payments were not made for approximately 1 1/2 months that totalled $178,966.59. GATX sought full payment as an administrative expense. The co-trustees argued that payment should be had only for the reasonable value of actual use and should not be entitled to an administrative expense. Id. at 1507.

105. Id.

106. The bankruptcy court found that § 365 and § 1110 had similar purposes thus GATX was entitled to merely an award of reasonable actual use value, the standard remedy under § 365. See also, In re Airlift Intern., Inc., 26 Bankr. 61 (Bankr. Fla. 1982).

107. Id. at 1507.

108. Id. at 1509.

109. Id.

110. Id. at 1510-11.

111. Seidle v. GATX Leasing Corp., 778 F.2d 659 (11th Cir. 1985).

112. Id. at 662. The trustee sought the return of $326,902.32, that was paid by Airlift to GATX.
craft. The trustee, by seeking the return of all pre-petition payments to the estate as a preference, would cause an inequitable result: if the debtor defaulted and then wished to have the airplanes, the default must be cured; if the debtor made payments up to filing, it could retain use of the aircraft and recover the payments as a preference. This would essentially undermine the purpose of § 1110 to either "prompt and certain repossession . . . or . . . satisfaction of all past due amounts and a promise to make future payments." Therefore, the trustee could not recover the pre-petition payments as preferences having entered into a stipulation under § 1110.

In Global Int'l Airways, the bankruptcy court was faced with the issue of when to allow a debtor to assume a lease under § 365. The debtor attempted to assume a lease for an airplane from Air Canada. The court must approve the assumption of a lease after the debtor proves that the assumption is a benefit to the estate. The court found that the debtor could not meet this burden because the estate stood to lose at least $1.6 million.

The Airlift and Global cases illustrate the court's ability to balance equities. Clearly, § 1110 protects airline financiers, and the appellate court correctly granted the financier an administrative expense for the amount of money defaulted upon by the trustee. Further, a preference action would render § 1110 a nullity. The Global court correctly examined within 90 days prior to the filing of a bankruptcy petition which seemingly constituted an avoidable preference under § 547.

The trustee's avoiding powers allow the debtor-in-possession to undue certain transactions undertaken prior to or after the filing of the bankruptcy petition. 11 U.S.C. §§ 544-50. The most powerful avoiding power is the ability to recover preferences under § 547. 11 U.S.C. § 547 provides that a preference action may be undertaken to recover a transfer of property of the estate that was for the benefit of a creditor on account of an antecedent debt made while the debtor was insolvent within 90 days of the filing of the bankruptcy petition (or within one year of the transfer if an insider) that enabled the creditor to receive more than it would have received under a liquidation proceeding. 11 U.S.C. § 547(b). This power allows the debtor-in-possession to recover all funds paid out by the debtor prior to the filing of the petition, provided the conditions are met. Essentially it allows the debtor-in-possession to undue unfavorable (to the debtor and to non-preferred creditors) transactions.

113. Seidle v. GATX, 778 F.2d at 662.
114. Id.
115. Id. at 664.
116. Id. at 662. The bankruptcy and district courts essentially agreed with the appellate court's ultimate decision.
118. Id. at 882.
119. Id. at 886.
120. Id. at 887-88. The debtor proposed to run one charter flight per month for three months. The lease ran for one year and would cost between $1.9 million (debtor's estimate) and $2.9 million (Air Canada's estimate). The debtor claimed it would make between $210,000 and $300,000 per charter flight.
the potentially devastating effect that the assumption of the aircraft lease would have on the reorganization of the estate and possible payout to all classes of creditors.

5. 11 U.S.C. § 363(b): The Use, Sale or Lease of Property Outside the Ordinary Course of Business and Its Effect on the Reorganization Plan

A vigorously litigated area in the airline industry bankruptcy situation is over the use, sale or lease of property outside the ordinary course of business.\textsuperscript{121} The court in \textit{Lionel}\textsuperscript{122} explained that the debtor must articu-
late a business justification other than "appeasement of major creditors" to use, sell or lease property outside the ordinary course of business. The question specifically facing the appellate court during the Braniff bankruptcy was "when does a transaction go outside the ordinary course of business such that it is also outside the scope of § 363 so as to render a bankruptcy court without power to approve the sale?" The court held that the proposed transaction "had the practical effect of dictating some of the terms of any future reorganization plan." The court concluded that the transaction would short circuit the requirements for confirmation of a Chapter 11 plan. The court found the sections of the agreement which forced the secured creditors to vote with a majority of the unsecured creditor's committee, and provided for the release of claims against Braniff, the secured creditors and its officers and directors particularly appalling. Where the effect of a sale would leave little choice for reorganization, the court is without power to approve the transaction.

notes 138-142 and accompanying text. The difference between liquidating a Chapter 11 through a plan and converting a proceeding to a Chapter 7 is one of tactics. A liquidation plan under Chapter 11 allows the debtor-in-possession to liquidate itself (believing itself to be more efficient than a Chapter 7 trustee) and saves the added layer of administrative expenses under 11 U.S.C. § 330. The disadvantage is that the plan must be accepted, often an arduous task. The distribution scheme under Chapter 7 or Chapter 11 is identical and can be found in 11 U.S.C. § 507.

In a hearing under § 363(b) the debtor-in-possession must articulate a business reason for its decision and the sale must be in the best interest of the creditors. Neither requirement is explicitly stated in the Code, although both have been implied by the courts. See, From Airwaves, at 268. See generally, Lionel and White Motor Credit. Non-ordinary transactions are further burdened by the requirement that the creditor’s security interest be adequately protected against loss. 11 U.S.C. § 363(c). The concept of Adequate protection is delineated in § 361. Adequate protection may be assured by periodic cash payments to the creditor, an additional or replacement lien, or other compensation that will result in the indubitable equivalent of the creditor’s interest. § 361(1-3). See generally, Baird and Jackson, Corporate Reorganization and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy, 51 U. Chi. L. Rev. 97 (1984). The debtor-in-possession must also adequately protect the use of cash collateral. Benefits of Bankruptcy, at 387.

122. In re Lionel Corp., 722 F.2d 1063 (2d Cir. 1983).
123. Id. at 1070.
125. Id. at 940. At issue was the "PSA Agreement." The PSA Agreement provided in great part that Braniff would transfer for cash, airplanes, equipment, terminal leases and landing slots in exchange for unsecured notes, travel scrip and profit participation in PSA’s proposed operations. The Agreement also called for a restructuring of Braniff’s creditors. The action raised “a blizzard of objection to each of these elements.” Id. at 939.
126. Id. at 940. The transaction would establish the “terms of the plan sub rosa.” Id. at 940. The requirements for a confirmation of a Chapter 11 plan are found at 11 U.S.C. § 1129(a) (1983).
127. Id.
128. Id.
A similar situation faced the appellate court in the Continental proceeding. Judge Gee succinctly phrased the issue as, "how far a debtor-in-possession can stretch the bankruptcy laws to undertake transactions outside a plan of reorganization." In this case, the transaction in question concerned the ability of Continental to enter into a lease agreement for two aircraft. Some creditors objected on grounds that the transaction "represent[s] pieces of a creeping plan of reorganization." The court agreed that these creditors' fears of being denied the rights guaranteed under a reorganization plan were valid.

The court in Braniff certainly seemed correct in disallowing the sale of such a large proportion of the assets as to render any chance of rehabilitation a nullity. While the court explicitly protected the rights of creditors in formulating and confirming a reorganization plan, the court implicitly protected the public interest. By not allowing the transaction, the court forced the airline to reconsider its reorganization plan and remain a viable airline.

Continental, on the other hand, defeated in part, the ability of a debtor-in-possession to operate the business under § 1108. Continental seemingly proposed a transaction that would increase its value and improve its position in a lucrative market. It not only articulated a business reason, it made a bold initiative for strengthening itself. Merely because a transaction involves a large amount of money does not mean its is "likely to short circuit the requirements of reorganization." The result of Continental affects the ability of a debtor-in-possession to effectuate meaningful changes through the operation of its business. It may also alter the analysis of whether an individual business decision is sound by raising the level of scrutiny above that of the business judgement rule. There may be sound reasons for requiring a higher burden upon the DIP than

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129. In re Continental Airlines, Inc., 780 F.2d 1223 (5th Cir. 1986).
130. Id. at 1224.
131. Id. Continental's proffered reasons for entering the agreement were to "strengthen and enhance profitability and cash flow and to increase the asset value of its mid-Pacific and South Pacific operations."
132. Id. at 1227.
133. Id.
134. In re Braniff, 700 F.2d at 935.
135. Id. at 940. One commentator astutely recognized that "Braniff simply does not hold that § 363(b) precludes a sale of all or substantially all of the debtor's assets . . . [rather] the true holding of Braniff is that § 363(b) does not permit a sale of assets which would change the composition of the debtor's property and dictate the terms of any future reorganization plan." From Airwaves, supra note 121, at 270-71.
136. Courts have generally held that it will not scrutinize business decisions made by the DIP as long as the decisions are made in good faith and within the scope of its authority. See generally, in re Southern Biotech, Inc., 37 Bankr. 318 (Bankr. Fla. 1983); in re Johns-Manville Corp., 60 Bankr. 612 (Bankr. N.Y. 1986).
the business judgement rule, given that present management presumably caused the corporation to enter bankruptcy. However, this reason does not change the fact that the test for scrutinizing management’s business decisions is whether it was in the DIP’s sound business judgement.137

The Braniff and Continental decisions strongly endorse the need for debtors-in-possession to formulate and implement a plan of reorganization.138 By forcing debtor’s to “scale hurdles erected in Chapter 11,” i.e., information disclosure, voting, a plan developed in the best interest of creditors and subject to the absolute priority rule, the courts have encouraged debtors-in-possession to quickly formulate and implement plans.139 The importance of confirming a plan benefits the debtor, creditors and the public as the rules for reorganization are laid out.140 The failure to implement a plan may lead to the court appointing a trustee.141 The bankruptcy court does not have the authority to compel a trustee to operate a debtor’s business and this may not be in anyone’s interest.142 Often, the debtor-in-possession, as opposed to a trustee, is more likely to have a vested interest in running the debtor’s business.

6. THE APPOINTMENT OF A TRUSTEE IN CHAPTER 11: EASTERN AIRLINES

While the debtor-in-possession is generally the best entity to run the business during the pendency of the bankruptcy, there are circumstances

137. Id.
138. The debtor is given the first chance to propose a reorganization plan. 11 U.S.C. § 1121(b) (1988). Under § 1121(b) the debtor, and only the debtor, may file a plan within the first 120 days after the filing of a petition. This period may be extended or reduced after notice and hearing by the court. Id. at § 1121(d). This power to propose the plan is important because it allows the debtor-in-possession to control the Chapter 11 and post Chapter 11 proceedings via the plan of reorganization. Upon a plan being confirmed, it controls the workings of the Chapter 11 proceeding by binding parties whether they have accepted or not. Id. at § 1141(a).

Finally, parties in interest have a great deal of say in the formulation, acceptance and modification of a reorganization plan, because all affected parties are bound by the terms of a plan upon confirmation. Id. at § 1141. Any party in interest may file a plan subject to the first attempt being given to the debtor. Id. at § 1121. The contents of a plan are too long to be adequately dealt with in this article and the requirements can be found in § 1123 and § 1129. The plan must be voted on and accepted by one-half of the number of allowed claims and two-thirds of the amount of claims in each class. Id. at § 1126(d). Every claim holder must receive adequate information before casting a vote. Id. at § 1125(b). “Adequate information means information of a kind, and in sufficient detail . . . that would enable a hypothetical reasonable investor . . . to make an informed judgement about the plan.” Id. at § 1125(a)(1). The court then must hold a confirmation hearing at which any party in interest may object. Id. at § 1128. The plan may only be confirmed once the requirements of § 1129 are met. The plan may be modified by § 1127.

139. In re Braniff, 700 F.2d at 940.
141. Id. at § 1104(a).
142. In re Airlift Int’l, Inc., 18 Bankr. 787, 788 (Bankr. Fia. 1982). The trustee may operate the debtor’s business if it is in the best interests of the estate, but the court may not force the trustee to run the business.
in which a trustee will be appointed to operate the debtor's business. A trustee may be appointed for cause or if the appointment is in the best interest of the estate. The trustee has all the power to operate the debtor's business.

In the Eastern bankruptcy, the unsecured creditors petitioned for the appointment of a trustee. The bankruptcy court, after analyzing Eastern's increased losses and reduction of amounts to creditors with each proposed reorganization plan, appointed the former President of Continental Airlines, Martin Shugrue, as trustee. Mr. Shugrue's immediate intent seems to focus on the reorganization of Eastern rather than the sale of substantially all of Eastern's assets or its liquidation. To achieve this end, Shugrue authorized the sale of Eastern's Latin American routes to American Airlines subject to the bankruptcy court's and Department of Transportation's approval. In addition to formulating a plan that will pay creditors an acceptable amount and restoring positive cash flow, Mr. Shugrue will need to restore public confidence and ease labor tensions.


The Air Florida bankruptcy produced two important decisions concerning the power of the debtor-in-possession to recover preferences under § 547 and avoid liens under § 544. In the first action, the DIP attempted to avoid the security interests of Trans World Airlines in the sale of a portion of a Fort Lauderdale, Florida airport terminal and two loading

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143. 11 U.S.C. § 1104(a)(1). "'Cause' includes "'fraud, dishonesty, incompetence or gross mismanagement by current management.'"
144. Id. at § 1104(a)(2).
145. Id. at § 1106(a).
146. Chicago Tribune, Apr. 19, 1990, § 3 at 1, col. 6.
147. Id. Undoubtedly, Bankruptcy Judge Lifland's primary consideration in appointing Mr. Shugrue was his experience in restoring Continental to financial health during its bankruptcy.
149. Id. Apr. 25, 1990, § 3, at 1, col. 1. The effect of the sale would presumably ease Eastern's cash-flow and liquidity problems.
150. In fact, the appointment of Mr. Shugrue has already softened the stance of several unions, including the International Association of Machinists. Id., July 4, 1990, § 3, at 1, col. 5.
151. 11 U.S.C. § 1107(a), gives the DIP all the rights of a trustee save for the right to receive compensation. The trustee's power to avoid preferences pursuant to § 547 is described supra at note 112.

A DIP may avoid certain liens pursuant to § 544. The DIP stands as a hypothetical lien creditor and may avoid transfers which are not perfected due to inadequate or incomplete documentation, unrecorded mortgages and unperfected security interests. Ginsberg, supra note 53, at 664. See also, Schechter and Heuer, The Trustee's Avoiding Powers Under the Bankruptcy Code, Chi. B.A. Bankr. Sem., at 8 (Sept. 17, 1990).
bridges to Air Florida. The court reviewed and interpreted various memoranda agreements and determined the nature of the collateral and the adequacy of TWA in perfecting its security interests. The court found the failure by TWA to file a financing statement with the Florida Department of State resulted in a failure to perfect its security interests, which the DIP could avoid and which resulted in the collateral being unsecured.

Having determined that TWA's lien could be avoided, the court was left to decide whether payments to TWA in furtherance of the above note on the airport terminal and loading bridges constituted a preference. The debt was now classified as unsecured and payments were made on account of an antecedent debt made while the debtor was insolvent. This allowed TWA to receive more than it would in a liquidation. The payments were a preference and could be avoided.

In another Air Florida proceeding, the DIP was able to recover payments made to the Airlines Clearinghouse Inc. (ACH), which made payments to Eastern Airlines with money that Air Florida owed Eastern. The payments were made as part of a reciprocal agreement between airlines to carry other airline's passengers. Various airlines then filed claims with ACH for payment from other airlines. Air Florida failed to make payments to ACH for three months totaling $3,015,601 and was expelled from the ACH. To regain its privileges in the ACH, Air Florida satisfied the debt owed to Eastern. The court found the payments were made to Eastern for an antecedent debt made while Air Florida was insolvent, allowing Eastern to receive more than it would in a liquidation proceeding. Thus, the court allowed Air Florida to recover the payments made to ACH to regain its good standing.

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153. Id. at 439. The court examined a sublease, Bill of Sale, Chattel Mortgage and Security Agreement, and a Financing Statement.
154. Id. TWA had filed the Chattel Mortgage and Financing Statement with the public records office of the county where the airport was located and argued that this action perfected its security interests.
155. Id. at 440. The requirements for recovering a preference are discussed supra note 112.
158. Id. at 888.
159. Id.
160. Id.
161. Id.
162. Id.
163. Id. However, the court did allow Eastern a setoff for monies owed Air Florida through the ACH pursuant to 11 U.S.C. § 553. Eastern remitted to Air Florida $241,010. Id. at 889.
Section 1102, the right to have a creditor’s committee appointed, may be one of the strongest tools the creditors have in forcing a debtor-in-possession into a confirmed plan status or the appointment of a trustee.\(^\text{164}\) Until recently, it was unknown whether a union could be a creditor and sit on a committee. The court in *Altair Airlines*,\(^\text{165}\) finally and firmly decided that a union, as exclusive bargaining agent, was an "entity" that had a right of payment.\(^\text{166}\) Therefore, unions may sit on creditor’s committees if they meet the requirements under § 1102(b).\(^\text{167}\)

9. **LABOR/MANAGEMENT RELATIONS**

The union/debtor-in-possession relationship is among the most important in attempting a successful reorganization of any business.\(^\text{168}\) Generally, labor costs are both the single largest variable cost (between airlines)\(^\text{169}\) and the largest cost factor.\(^\text{170}\) A large percentage of the ma-

\(^{164}\) This is due primarily to the great powers of investigation given to the committee to protect the interest of unsecured creditors as explained below.

\(^{165}\) In re *Altair Airlines, Inc.*, 727 F.2d 88 (3rd Cir. 1984).

\(^{166}\) Id. at 91. Essentially, an entity with a right of payment makes one a creditor. 11 U.S.C. § 101(9). Here the union represented 88 pilots of the airline. Their claims totalled $676,120, making it the second largest unsecured creditor. *Altair* at 89.

\(^{167}\) One commentator noted that there are five situations in which the union is not a creditor, and hence may not sit on the creditor’s committee and, indeed, may not have a substantial voice in the reorganization. A union may not sit on a creditor’s committee if the collective bargaining agreement is 1) assumed; 2) the rejection of the CBA is denied; 3) the debtor’s operations are discontinued; 4) the union strikes in response to the filing of a petition and rejection of the collective bargaining agreement; and, 5) the collective bargaining agreement expires prior to rejection.


\(^{169}\) *Labor Contract Issues*, supra note 168, at 139.
ajor Chapter 11 cases have significant unionized labor. The situation was particularly grave in the pre-deregulated airline industry as wage rates were especially high. "[A]irline management generally felt that it had made overly generous pre-deregulation concessions to the unions and that both labor as well as management should endure the post-de-regulation shakedown."173

Section 1113 codified the debtor-in-possession's ability to reject a collective bargaining agreement.174 It is primarily aimed at the danger of

170. Bankruptcy Dynamics, supra note 168, at 170.
171. Id.
173. Derregulation in the Airline Industry, supra note 90, at 1015.
174. 11 U.S.C. § 1113. A collective bargaining agreement (CBA) between a labor union and management is an executory contract. In re Bildisco, 465 U.S. 513 (1984). However, CBA's have often been treated as a fundamentally different situation primarily because of the countervailing public policy considerations of the federal labor laws. See generally, In re Bildisco, 682 F.2d 72 (3rd Cir. 1982), aff'd, 465 U.S. 513 (1984); Local Joint Executive Bd., AFL-CIO v. Hotel Circle, Inc., 613 F.2d 210 (9th Cir. 1980); In re Brada-Miller Freight Sys., 702 F.2d 890 (11th Cir. 1983); Brotherhood of Ry., Airline, and S.S. Clerks v. REA Express, Inc., 523 F.2d 164 (2d Cir. 1975), cert. denied, 423 U.S. 1073 (1976); Shopmen's Local Union No. 455 v. Kevin Steel Products, Inc., 519 F.2d 698 (2d Cir. 1975). For this reason, the courts developed a more stringent test than the business judgment rule in deciding when to allow rejection of a collective bargaining agreement.

A split in the circuits developed over the proper standard to use in allowing a debtor-in-possession to reject a CBA. Compare REA with Brada-Miller and Bildisco, 682 F.2d 72 (3rd Cir. 1982). This was the question the Supreme Court squarely faced in Bildisco, and held "that because of the special nature of a collective bargaining agreement, and the consequent 'law of the shop'...a somewhat stricter standard should govern the decision of the bankruptcy court to allow rejection of a collective bargaining agreement." 465 U.S. at 524. Bildisco noted that "there is no indication in section 365 of the bankruptcy code that rejection of a collective bargaining agreement should be governed by a standard different from that governing other executory contracts." Id. at 523. Commenting on the section 1167 special exemption of railway laborers from changes in their collective bargaining agreement, the Court stated "[C]ongress knew how to draft an exclusion when it wanted to." Id. at 522. The Court was faced with a decision of whether to apply the labor conscious standard of REA or whether to focus on the ultimate goal of Chapter 11 to reorganize the debtor's business. The Court in REA found that a debtor-in-possession could only reject a CBA if the debtor-in-possession "can demonstrate that its reorganization will fail unless rejection is permitted." Id. at 524. See REA, 523 F.2d at 167-69. The appellate court in Bildisco focused on the equitable powers of the bankruptcy court and the goal of reorganization. Bildisco, 682 F.2d at 74. The Supreme Court found the formulation in REA was unduly restrictive as "the authority to reject an executory contract is vital to the basic purpose of a Chapter 11 reorganization because rejection can release the debtor's estate from burdensome obligations that can impede a successful reorganization." Bildisco, 465 U.S. at 528.

The Supreme Court in Bildisco found that rejection of a CBA was proper if that agreement is burdensome to the reorganization and that balance of equities favored rejection. Id. at 527. The
management initiating unilateral changes but essentially adopts the substantive and procedural guarantees of Bildisco. This section has generally been interpreted by the test set forth in American Provisions, with court believed that balancing the equities included consideration of the debtor, creditors and employees with an eye towards a successful reorganization.

The Supreme Court was faced with a second issue in Bildisco, whether a debtor-in-possession which unilaterally rejects a CBA has committed an unfair labor practice under section 8(a)(5) and 8(d) of the National Labor Relations Act. *Id.* at 528. The Court concluded that a debtor-in-possession does not commit an unfair labor practice. *Id.* at 529. To conclude that an unfair labor practice had been committed "would largely, if not completely, undermine whatever benefit the debtor-in-possession otherwise obtains by its authority to request rejection." *Id.* at 529. The union has a remedy, it may file a proof-of-claim for damages stemming from the breach of the CBA. *Id.* at 530.


Section 1113 emphasizes the consensual nature of collective bargaining. The debtor-in-possession must "make a proposal . . . based on the most complete and reliable information . . . which provides for necessary modifications . . . necessary to permit the reorganization of the debtor and to assure that all creditors, the debtor and all of the affected parties are treated fairly and equitably." *Id.* at § 1113(b)(1)(A). The debtor-in-possession shall provide the employees' representative with information relevant to evaluate the proposal. *Id.* at § 1113(b)(1)(B). The parties must meet in "good faith." *Id.* at § 1113(b)(2). The bankruptcy court shall approve a rejection of a CBA only if the above criteria are met, the employee representative refused the proposal without good cause and "the balance of equities clearly favors rejection." *Id.* at § 1113(c).


176. In re American Provisions, 44 Bankr. 907, 909 (Bankr. Minn. 1984). The nine-part test is as follows:

(1) The debtor-in-possession must make a proposal to the union to modify the CBA;
(2) The proposal must be based on the most complete and reliable information available at the time of the proposal; (3) The proposal modifications must be necessary to permit the reorganization of the debtor; (4) The proposed modifications must assure that all the creditors, the debtor, and all the affected parties are treated fairly and equitably; (5) The debtor must provide to the union such relevant information as is necessary to evaluate the proposal; (6) Between the time of the making of the proposal and the time of the hearing on approval of the rejection of the existing collective bargaining agreement, the debtor must meet at reasonable times with the union; (7) At the meetings, the debtor must confer in good faith in attempting to reach mutually satisfactory modifications of the collective bargaining agreement; (8) The union must have refused to accept the proposal without good cause; (9) The balance of the equities must clearly favor rejection of the collective bargaining agreement.


Essentially the debtor-in-possession must now make a proposal to the union to modify the
bargaining as the linchpin. Therefore, it is a misnomer to label a collective bargaining agreement as rejected under § 1113, rather, it is a modification.


While bargaining may be the linchpin of a modified collective bargaining agreement in airline bankruptcies because of § 1113, the normal mechanisms of negotiation do not apply. It has been argued that collective bargaining agreements may not be rejected except by the method delineated under § 1167. The Railroad Reorganization Act prohibits rejection of collective bargaining agreements except for the modification procedures under subsection VI of the Railway Labor Act. In Braniff and Air Florida, the petitioner-unions attempted to boot-strap the inclusion of airline unions as governed by the RLA into the provisions of § 1167. Both courts found that § 1167 pertained solely to railroads despite the references to the RLA and that rejection may be had by means other than those found at subsection VI of the RLA. Both cases arose prior to § 1113 and were decided in accordance with 11 U.S.C. § 365, although Air Florida was decided in the post § 1113 era.

11. RIGHTS AND POWERS RETAINED BY THE UNION

While unions may not have all the protections of the RLA, the airline collective bargaining agreement based on complete and reliable information that is provided to the union. The proposal must be necessary to permit reorganization and to assure all affected parties are treated fairly and equitably. American Provisions, supra at 909. The necessity component of this test has resulted in a split of the circuits. Cf. Wheeling Pittsburgh, supra at 1079 ("necessity" should be strictly construed and should only be allowed to avoid debtor-in-possession from going into liquidation); and Truck Drivers Local 807 v. Carey Transportation, Inc., 816 F.2d 90 (2d Cir. 1987) (§ 1113 did not overturn the substance of Bildisco, it only codified the procedure). "Necessary should not be equated with "essential" or bare minimum." Id. at 89. The court should look to the long term for "[C]hanges that will enable the debtor to complete the reorganization process successfully." Id. at 90. The debtor-in-possession and union must meet at reasonable times, in good faith, to attempt to reach a satisfactory modification. The union must have refused this proposal without good cause and the balance of equities must clearly favor rejection. Id. at 90. Thus, the union can have a powerful say in either rebutting a possible rejection or in setting the terms in a new modified agreement.

177. Repudiation, supra note 175, at 815.
184. Air Florida, id. at 444.
still retains the duty to bargain in good faith. The union retains the right to strike and may not be enjoined under the general power of the court to carry out the provisions of the code. Its status as bargaining agent is unaffected by the expiration or rejection of a CBA, and it may utilize its powers to investigate management's operations and garner knowledge as a member of the creditor's committee. A union may be able to seek an appointment to a separate union-creditors' committee if its interests differ so substantially from other unsecured creditors' interests. If a rejection of a CBA is authorized and a new CBA negotiated, the debtor-in-possession may not alter the agreement except with respect to subsection VI of the RLA. In relationship to non-unionized labor, unionized labor is much better off in bankruptcy.

It has been noted that § 1113 may allow a broader range of negotiation issues. Unions are entitled to receive information in modification proceedings as a member of the creditor's committee. It may contest any reorganization plan to ensure that all are treated fairly and equitably. Subjects such as the number and type of managers, management salaries and fringe benefits, general corporate organization and the use of capital are ripe matters for collective bargaining discussion.

While unions may be gaining some management control, particularly through stock options and seats on the Board of Directors, Chapter 11 is not a tool "in which labor shares in the management of the enterprise." While labor models and stances are becoming increasingly non-adversarial and debtor-union cooperation may be a key compo-

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185. Labor Contract Issues, supra note 168, at 84.
186. Id.
187. In re Petrusch, 667 F.2d 297 (2d Cir. 1981); In re Crowe & Assoc., 713 F.2d 211 (6th Cir. 1983), cert. denied, 456 U.S. 974 (1981) (§ 105(a) allows the court to "issue any order, process, or judgement necessary or appropriate to carry out the provisions of this title.").
188. Protecting Union Interests, supra note 178, at 315.
189. Id. at 310, and Bankruptcy Reorganization, supra note 167, at 8.
190. Bankruptcy Reorganization, Id. at 19. A special union-creditors' committee was established in the Continental bankruptcy proceedings.
191. Id. at 11.
192. Judge Merrick noted that employers will normally reduce non-organized labor as a matter of course. "Non-unionized labor compensation maybe reduced without prior explanation or external approval. . . . Reduction (of wages) is swift and certain for unorganized employees but slow and conjectural for organized employees. . . . Newspaper accounts of the outrage of union leaders over the Bildisco decision suggest that the addition of Section 1113 was political and not cerebral." Bankruptcy Dynamics, supra note 168, at 228. Section 1113's focus for cost cutting must not be directed exclusively at unionized workers.
193. Repudiation, supra note 175, at 816.
194. Id.
196. Bankruptcy Reorganization, supra note 167, at 8.
nent to a successful reorganization, ultimately Chapter 11 reorganization has multiple objectives. A commentator notes, "[u]nderstandably, the union desires to emerge from this proceeding having preserved the terms and conditions of its collective bargaining agreement. However, if by doing so, the company is pushed into liquidation, the union's victory will have been a Pyrrhic one."

C. THE RESULTS OF AIRLINES IN BANKRUPTCY

News accounts of airlines in bankruptcy are often greeted by front page news. Yet, the coverage subsides as the on-goings of bankrupt airlines are often relegated to the business section. This clearly demonstrates that the public has, to a great degree, accepted the fact that businesses, even service industries, go into bankruptcy without the sky falling.

The theoretical balancing of equities inscribed in the Code has worked remarkably well in the real world of airlines. The ideal path of a bankrupt airline and the path of airlines in the deregulated era are strikingly similar. The airline industry, just like individual airlines in bankruptcy, goes through a painful, cathartic period. They emerge a more lean, productive, efficient and profitable business. Bankruptcy proceedings have an ability to "run silent, run deep." They effectuate great changes within the structure of an airline, yet allow the industry as a whole to function well.

The bankruptcy forum is the ideal arena for determinations of liquidation and reorganization. The bankruptcy court’s great equitable powers and flexibility allow it to work changes on an individually troubled airline without affecting the industry as a whole. The debtor’s, creditor’s, and public’s interest can be balanced in the bankruptcy forum far better than by a plodding, unresponsive bureaucracy. The bankruptcy court has been particularly adept at remedying three main concerns of the deregulators: 1) what to do with non-viable airlines; 2) providing financing to a credit-starved industry; and 3) dealing with the gamut of management-labor problems.

Deregulation spurred a tremendous growth in the number of opera-
tional airlines. This was foreseeable, as was the fact that many airlines would cease operations, merge or declare bankruptcy. The bankruptcy court's ability to liquidate airlines that are deeply in debt and have a going concern only as airplanes, slots, employees and management, is formidable. The assets are sold to other airlines or returned to creditors. Debts are paid in part and workers may retain jobs. Certainly this is preferred to a situation of idle planes, workers and customers.

1. **Midway: Building an Airline Through Bankruptcy Acquisition**

Midway Airlines is an example of building an airline through bankruptcy liquidation or sale of assets pursuant to a reorganization plan. Much of Midway's growth can be attributed to purchases from bankrupt airlines. Midway purchased substantially all of Air Florida's assets during the latter's bankruptcy proceeding. The bankruptcy court found this sale was in the best interest of creditors and employees as there was no other "prospective purchaser and no other operating plan." Midway also purchased eight gates and aircraft from Eastern in Philadelphia. The effect of this purchase was to give Midway a foothold in the eastern markets and challenge the strong position held by USAir in the Philadelphia market. Midway has further attempted to strengthen its Florida position by offering to purchase three gates from Braniff at Orlando International Airport for $2.25 million.


204. There seems to be the assumption that bankruptcy necessarily means the termination of business. This is not the case. Airlines may continue to operate during the pendency of the bankruptcy. Examples include Eastern and Continental which decreased service, but did not stop flying upon filing Chapter 11. Moreover, the slack caused by airlines that do stop operating is usually quickly picked up. For instance, in Braniff's case, passengers' tickets were honored by several competitors. Wall Street J., Sept. 28, 1989, § A, at 5, col. 6.


208. Id.


210. Id.

211. Chicago Tribune, Feb. 10, 1990, § 2, at 7, col. 2. The sale is pending approval before the bankruptcy court. Finally, there has been speculation that Midway may expand to Kansas City by acquiring Braniff's 28 gates and 52 aircraft at Kansas City International Airport. Chicago Tribune, Nov. 13, 1989, § 4, at 1, col. 5.
2. REORGANIZATION AND REHABILITATION

A better gauge of bankruptcy success is the rehabilitation of a debtor. One of the problems facing airlines is great debt coupled with an inability to gain adequate financing.\(^{212}\) Richard Gritta prophetically predicted which airlines would seek bankruptcy based on debt/equity ratios in 1982.\(^{213}\) Braniff's tale is particularly revealing as its initial bankruptcy was preceded by an aggressive expansion program. Its second bankruptcy was preceded by its great expansion in Kansas City.\(^{214}\) Financing airlines in bankruptcy is not particularly hazardous.\(^{215}\) General financing,

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\(^{212}\) Miller, Ho and Rosen, *Obtaining Credit and Incurring Debt by a Trustee or Debtor-In-Possession Under the Bankruptcy Code*, 4 PRAC. L. INST. 211 (Comm. L. & Prac. Handbook No. 391 1989) [hereinafter *Obtaining Credit*].

\(^{213}\) Gritta, *Bankruptcy Risks Facing the Major U.S. Airlines*, 48 J. OF AIR L. & COMM. 89, 90-97 (1982) [hereinafter *Bankruptcy Risks*]. Gritta explained that debt financing "presents opportunities for higher rates of return, but it also increases risk. The ultimate risk is [that] an air carrier may not be able to pay interest charges and therefore may become insolvent." *Id.* at 93. Gritta found the financial strategy of accumulating debt had been going on in the airline industry for 20 years. The airline industry was particularly vulnerable to recessions, and the combination of debt and recession would cause many bankruptcies. *Id.* at 91. Indeed the three major airlines with the highest debt/equity ratios, Braniff, Continental and Eastern, all declared bankruptcy. The fourth highest, Western, merged with Delta. The remaining big five, United, American, Delta, Northwest and TWA continue to operate.


\(^{215}\) The debtor-in-possession may obtain credit and incur debt under § 364. See generally, *Obtaining Credit*, supra note 212. Often the success or failure of a Chapter 11 is predicated on obtaining sufficient funds to continue the business. *Id.* at 211, and *Benefits of Bankruptcy*, supra note 121, at 393.

As under § 363, § 364 may be neatly divided between obtaining credit in the ordinary course of business and outside the ordinary course. 11 U.S.C. § 364(a)-(d). The debtor-in-possession "may obtain unsecured credit . . . in the ordinary course of business." *Id.* at § 364(a). This debt will be allowed as an administrative expense under § 503. *Id.* at § 364(a). A debtor-in-possession's administrative expenses are paid out immediately after all secured debt is repaid from the secured property or the secured property is abandoned to the secured creditor. Typically, ordinary course debt will include trade credit and utility services. *Obtaining Credit*, supra note 215, at 220.

The debtor-in-possession may also obtain credit and incur debt outside the ordinary course of business. § 364(b) allows the trustee, after notice and hearing and with court approval, to obtain non-ordinary course debt. 11 U.S.C. § 364(b). The financing must be for an appropriate purpose. *Obtaining Credit*, supra note 215, at 225; *In re Club Development and Management Corp.*, 27 Bankr. 610, 611-12 (Bankr. 9th Cir. 1982). This credit or debt is unsecured but generally is entitled to an administrative priority. 11 U.S.C. § 364(b). The most common forms of non-ordinary credit or debt are funds to pay operating expenses or payroll. *Obtaining Credit*, supra note 215, at 220.

If a debtor-in-possession in unable to entice sufficient credit or debt through § 364(a) and (b), the court may authorize credit or debt under § 364(c), which provides that after notice and hearing, a creditor may be given priority over 1) all administrative expenses, or 2) a security interest on otherwise unencumbered property, or, 3) a junior lien on encumbered property. 11 U.S.C. § 364(c)(1-3).

If sufficient credit cannot be generated by the provisions of § 364(c), the court may authorize
outside the ordinary course of business, is usually secured by unencumbered property or by super lien.\footnote{216} Aircraft and equipment is protected to an even greater degree by § 1110,\footnote{217} under which a debtor must cure all defaults and make all payments in a timely fashion or face repossession.\footnote{218}

While it may be easier to obtain financing in bankruptcy because of the reduced risks, it may also be easier to retire an airline's debts. Lenders prefer airlines to reorganize rather than liquidate.\footnote{219}

The establishment of an estate protects an airline from being dismembered by a particularly rabid creditor and thus preserves the assets and increases the chance for reorganization for all creditors. Bankers have become increasingly flexible in repayment plans\footnote{220} and innovative in new types of financing.\footnote{221}

Similarly, bankruptcy has ushered in a new era in labor/management relations. Certainly § 1113 is a management tool that allows the airline to cut labor costs and institute other work rule changes. An aggressive, active union may use its role as either a creditor or a rejectee of a collective bargaining agreement to its advantage. It is entitled to vast information in either role.\footnote{222} The union may negotiate on issues it could not previously insist upon.\footnote{223} While organized labor wages have gone down while increased productivity has been required,\footnote{224} bankruptcy has created opportunities to participate in fundamental business decisions not available under the labor laws.\footnote{225}

Bankruptcy law has perhaps been more responsive to the changes in

\footnote{1. A "super lien" under § 364(d). A super lien is credit or debt secured by a "senior or equal lien on property" that is already secured. Id. at § 364(d)(1). The court may only authorize this type of credit when the debtor-in-possession "is unable to obtain such credit otherwise." Id. at § 364(d)(1)(A), i.e. the DIP is not able to obtain credit via §§ 364(a)-(c) and there is adequate protection for the already secured property. Id. at § 364(d)(1)(B). The trustee has the burden of proof on the issue of adequate protection. 11 U.S.C. § 364(d)(2).


219. Bankruptcy Risks, supra note 213, at 107. "The world wide market in used aircraft is already gutted and prices are falling."

220. Id.

221. The idea of the operating lessor is but one innovation. Impacts of Deregulation, supra note 201, at 12.

222. As a member of the creditor's committee it may oversee operations and investigate actions. See supra note 174. As the recipient of a rejection it is entitled to all relevant information used by the company in formulating a modified agreement. See supra note 164.

223. Repudiation, supra note 175, at 816.

224. Deregulation in the Airline Industry, supra note 90, at 1027.

225. Protecting Union Interests, supra note 178, at 307.}
labor/management relations than the traditional labor laws. The complex
demands of a new economic order have emphasized cooperation rather
than conflict, and performance-based compensation.226 Rigid rules on
classifications have been relaxed in order to facilitate change and there
has been a recognition of the industry’s need for smarter, better-educated
workers whose skills are constantly changing to match the demands of
new technology.227 Even the more traditional, adversarial unions have
had to soften their positions.228

3. CONTINENTAL: A BANKRUPTCY SUCCESS

Perhaps the most well-known success story of airlines in bankruptcy
is Continental Airlines.229 Continental operated the eighth largest airline,
employing 12,000 people and generating $1.5 billion in annual revenues
prior to filing bankruptcy.230 However, it had lost $520 million since 1978
and was unable to compete due to high labor costs.231 Having no free
assets, cash flow problems and failure to reach satisfactory modifications
with its creditors and unions, it fled to Chapter 11.232

Continental’s many court battles have been documented above.233
But Continental’s case of Chapter 11 was a sound one. It staved off cred­
itors, reduced costs and formulated an aggressive, expansion-oriented
reorganization plan.234 As Continental emerges from bankruptcy, it is in­
teresting to note that it is at the approximate pre-filing size,235 and flies
double the seat miles.236 Continental’s management decided that it must

226. Id.
228. For instance, many of Eastern’s pilots have crossed the picket lines since a strike began
on March 4, 1989, and a war has boiled over on the question of whether to end the strike,
leading to the replacement of the ALPA President with a “more militant leader.” Wall Street J.,
Sept. 11, 1989, § B, at 11, col. 1. The Eastern flight attendants recently ended their 8½ week
strike. Chicago Tribune, Nov. 24, 1989, § 3, at 1, col. 5.
229. The contention that Continental has succeeded is hotly disputed by those proponents of
organized labor who saw their wages cut by as much as 50% and then saw the dismantling of
union power at Continental. Comment, Deregulation in the Airline Industry: Toward a New Judi­
cia/ Interpretation of the Railway Labor Act, 80 Nw. U.L. REV. 1003, 1016 (1986). However, the
animus between management and organized labor was so great that it became apparent that
one had to go. Continental was legitimately in bankruptcy because of its high costs, debt and
231. Id.
233. See supra notes 69-75 and accompanying text.
234. Labor strife continued for most of the Continental bankruptcy proceeding as unions
struck the airlines for almost two years. Bankruptcy Reorganization, supra note 167, at 7. The
upshot of the strikes played into Continental’s hands as Continental could lay-off and fire strikers
rather than seek a drastically modified and reduced collective bargaining agreement.
235. Id. at 298.
236. Airline Operations, supra note 78, at 526.
grow to compete or face a failed reorganization. Thus Continental came armed to the bankruptcy court with reliable financial projections and detailed expansion and marketing plans. In the first half of 1989, Continental reported net income of $15.6 million on revenues of $2.1 billion. The result is a rehabilitated airline.

Deregulation opened the market to new entrants, price-slashing, cost consciousness and improved efficiency. Deregulation has strengthened some airlines, but others have failed or should not have entered the market in the first place. Bankruptcy is concerned with the losers of the game. Its broad powers to effectuate changes where administrative agencies cannot, its inability to interfere with healthy airlines (which administrative agencies can-and often do-effect across-the-board industry changes) and its unique ability to balance the equities has worked at the microeconomic level to which it is aimed. Bankruptcy is not aimed at institutional stability or consumer desires, yet it has served those interests well. It is through the bankruptcy process that the airline industry was able to pull through a trying period of confusion and recession. The conditions that caused problems in the airline industry were problems that affected business in general and problems that are often solved through resort to the bankruptcy process.

IV. IMPACT OF BANKRUPTCY AND CONCLUSIONS

Because general economic conditions and the policy decisions of airline management during the pre-deregulated era and the infancy of the deregulated age caused many of the problems facing the airline industry today, it is disheartening to hear some “solutions” which so completely misperceive the problem. The problems have fermented and have only recently come home to roost. One particularly appalling suggestion is the so-called “two-time loser” bill. A recent congressional proposal would disallow airlines from entering bankruptcy a second time. There is little possible good that can come from passing this bill into law. In bankruptcy, either an airline is rehabilitated and allowed to provide service or its assets are sold to those airlines that can provide service. The two-time loser bill cannot assure the same orderly system of rehabilitation or redistribution.

Industrial problems often set off a clarion call for regulatory schemes heralded as a solution for an industry’s ills. More often problems that

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237. Id.
238. Id.
240. The problem is large debt and high costs pulled through a recessionary period. See supra notes 212-213 and accompanying text.
241. See supra notes 4-8 and accompanying text.
occur in an industry are caused by the tension that remains in a newly deregulated industry, which remains, in part, regulated. Certainly this seems to be the present situation of the airways. Robert Poole, of the Reason Foundation, has found that the monopoly of airlines in certain cities has not been caused by cutthroat competition which reduced the number of airlines that compete in a given market. Rather, remnants of the regulated era have caused monopolies. During the regulated era airports and airlines signed long-term leases which often gave the dominant airline veto power over bond issues for airport expansion. These long-term leases made perfect sense in the regulated era, when government dictated price, routes and allocation of slots. Today, the long-term leases are barriers to airlines which would ordinarily attempt to move into markets where excessive fares are the rule. Rather than a regulatory scheme which would adjust fares in those monopoly markets, the airports should be deregulated.

There has also been a proposal that the airlines be subjected to a set of parallel bankruptcy provisions as provided for the railroad industry. Therefore, it is somewhat worthwhile to examine the special provisions for railroad reorganization under the Code. The purpose of the Railroad Reorganization Act is to protect the public interest. A trustee is appointed as a matter of course. The Interstate Commerce Commission, Department of Transportation and state regulatory commissions may appear on any issue. Collective bargaining agreements may only be modified in accordance with subsection VI of the Railway Labor Act, where abandonment of a railway line may only be had if it is in the "best interest of the estate; or . . . essential to the formulation of a plan; and . . . consistent with the public interest." Railroad reorganization is far more concerned with the interests of the public and unions. Railroad reorganization restricts the flexibility of the court, eliminates the debtor-in-possession and reduces the input of creditors in the reorganization process.

There is some facial resemblance between the railroad and airline industries. Both are transportation industries providing a public utility. Certain provisions in the Railroad Reorganization Act would be particu-

243. *id.*
244. *id.*
245. *id.*
246. *id.*
248. *id.* at § 1165.
249. *id.* at § 1163.
250. *id.* at § 1164.
251. *id.* at § 1167.
252. *id.* at § 1170(a).
larly helpful to airline creditors.253

But there are historical and practical differences between the industries that are so great that a parallel airline subchapter would make airlines vulnerable to successful rehabilitation. First, it is far easier to build new landing strips and gates than it is to build railroad lines. Second, airline routes are multi-directional while railway lines are bi-directional.254 While any number of airlines may fly the same routes, railways are far more monopolistic, and the regulation over price and routes is necessarily greater. High labor and other fixed costs fit easily into the price figuration in a monopoly setting. Airlines, in price competition, must be acutely aware of its fixed costs. The Railroad Reorganization subchapter posits a traditional labor model where collective bargaining agreements may only be modified by subsection VI of the Railway Labor Act.255 Airlines have increasingly abandoned union labor or have developed a new model for labor/management relations.256 By triumphing the public interest and union rights, the Railroad Reorganization subchapter may have hurt both. The delicate balance of equities, rights and powers has been removed.257

It is precisely the balancing of equities, rights and powers that has allowed airlines in bankruptcy to successfully rehabilitate while selling off the on-going enterprises of non-viable airlines. What might we expect from airlines in bankruptcy? Less of the same. The lion's share of reorganization, liquidation, merger and consolidation has taken place. The most debt-ridden, inefficient airlines have been lost in a war of attrition. Twenty-two airlines, most of them healthy, have survived. Perhaps a few airlines, due to mismanagement, over-aggressive expansion, high costs, poor service or inefficiency may be subjected to bankruptcy. After all, the decision to deregulate was a policy decision based upon a belief that management could run the airlines better than government.258 Economic

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253. For instance, the rights of a secured creditor of rolling stock under § 1168 are parallel to those of a secured creditor of airline equipment under § 1110.

254. Airline routes may be conveniently set up provided embarking and disembarking are possible. The same claim cannot be made about railway lines; railway lines do not share the flexibility of air routes.


256. At TWA, the "Icahn Agreements . . . demonstrate a new framework for bargaining, covering not only wages and work rules, but also stock plans, investment and capital spending requirements, business strategy, restriction on [the] ability [of membership] to dispose of TWA assets, and extensive information sharing." Potential of Collective Bargaining, supra note 172, at 17.

257. 11 U.S.C. §§ 343, 1102, 1104, 1105, 1107, 1113, 1129(a)(7) and 1129(c) do not apply.

258. This decision reminds one of de Tocqueville's ruminations on how government, and especially bureaucracy, blunts the creative powers of mankind. "Above this race of man stands an immense and tutelary power, which takes upon itself alone to secure their gratifications and to watch over their fate. That power is absolute, minute, regular, provident, and mild. It would be
deregulation has to a great extent worked in opening the skies to more people at reduced fares to more destinations.\textsuperscript{259} This is all it promised. Where deregulation has failed, bankruptcy has adequately filled the gap. It has kept some airlines flying and sold off the effective parts of airlines that could not stay afloat. It has balanced the interests of all concerned, including the government and the public on a microeconomic level that has produced positive results on a larger scale. Bankruptcy does not and will not trample the ability of strong airlines to effectively run their business. It is an excellent complement to economic deregulation.\textsuperscript{260}

'It's hard to fathom,' said a Braniff pilot on learning that this company had suspended operations. 'You can chalk this one up to deregulation.' . . . in one sense, the pilot was right. Deregulation gave Braniff the latitude to make errors, mistakes by management that proved fatal in the unforgiving climate of a recession. Such freedom is what free enterprise is about and it is difficult to believe the country would be better off without it. Braniff's collapse can be traced to a decision in 1978 to expand as rapidly as the airline deregulation law allowed. Before deregulation, airline had to have government permission to fly new routes. Such applications were usually held up for years by challenges from competing carriers. But the new law let Braniff grow, in months, from a regional airline serving the Midwest and Latin America to a giant carrier among major cities on four continents. . . . The expansion was poorly planned. Travelers will not suffer much; other carriers will fill the gap. If the loss of Braniff's jobs is blamed on deregulation, then the new jobs at upstart airlines . . . must be credited to deregulation. In any case, it is not the government's duty in a free economy to guarantee total employment in any particular industry. No one should take pleasure from Braniff's troubles. Workers' lives are being disrupted, investors' capital lost. But without the possibility of failure, there is no way to penalize inefficiency. A Braniff kept alive by government patronage would be even worse than a Braniff in bankruptcy.\textsuperscript{261}
Computer Reservation Systems, Creative Destruction, and Consumer Welfare: Some Unsettled Issues

JEROME ELLIG

I. INTRODUCTION

Airline computer reservation systems (CRS) present new challenges and opportunities for both the travel industry and policy analysts. Travel agents used to book passengers through a time-consuming combination of telephone calls and paper transfers. Now, U.S. travel agents can book passengers quickly by using one of five computer systems that list information about a variety of airlines, hotels, rental car companies, and other complementary services. Many authors credit CRS for allowing travel agents to keep track of the explosion of new fare and service options that accompanied deregulation. For example, in 1985, the industry-leading Sabre system listed 330 days of flight information for 590 different carriers, or approximately 44,000 flights per day. This innovation touches most airline passengers because travel agents sell approximately 80% of all airline tickets.

CRS are also one of several factors spurring a reassessment of the economic theories once thought to explain airline behavior. The Airline Deregulation Act of 1978 eliminated federal control over entry and ticket prices. Economists favoring deregulation often touted airlines as an example of contestable market theory in action, since highly mobile capital meant that the sunk costs of entering individual city-pair markets were quite low. However, recent research has suggested that not all airline markets are perfectly contestable.4

Dempsey,5 Saunders,6 Thornton,7 Borenstein,8 Levine,9 and Morrison and Winston10 cite CRS as one of several factors that give the airlines which own them an advantage over others. Unless other airlines can have their flights listed on the computer screens at nondiscriminatory fees and terms, airlines owning the reservation systems can create a competitive disadvantage. Of course, even if airlines owning the systems do not discriminate, they can exact a supra-competitive price for access to the reservation system if the market for the systems is not competitive.

Clearly, CRS bring both benefits and costs to society. Policy analysis, however, is complicated by the fact that CRS surely qualify as an exemplar of Schumpeterian “creative destruction”—a technology so revolutionary that few who decline to make use of it can afford to compete.11 A full analysis of CRS, therefore, faces the challenge of incorporating the effects of innovation and creativity. Theories of entrepreneurship and innovation can provide a framework for analyzing the full impact of CRS and evaluating alternative rules for dealing with them.

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9. Levine, supra note 1, at 416.


II. THE CRS INDUSTRY

Efforts toward developing CRS in the United States date from 1967 when 21 airlines signed a memorandum of understanding to jointly develop an industry-wide system. Antitrust challenges and financing difficulties doomed this and several other attempts. In 1976, United Air Lines and American Airlines announced plans to develop and market their own systems.\(^{12}\)

Today, there are five CRS, all of which are wholly or partially owned by airlines or airlines' parent companies. American Airlines who owns Sabre, is the industry leader. Covia Partnership, owned half by United Air Lines and half by six other airlines, owns the Apollo CRS. Texas Air owns System One, Delta owns Datas II, and Northwest and TWA jointly own Pars.\(^{13}\)

A CRS generates three principal streams of revenue:

- **Incremental Revenues.** Airlines owning the systems can use them to increase ticket sales at the expense of competitors. Initially, airlines biased screen displays to show their flights first, even when other airlines' flights may have been less expensive or more convenient. The Civil Aeronautics Board (CAB) banned such bias in 1984, but observers suspect that travel agents still give preference to flights offered by the airline that owns their reservation system. Complaints of other biases also abound.

- **Booking Fees.** All airlines pay the CRS's owner a fee for each flight segment booked on that system.\(^ {14}\)

- **Installation/Operation Fees.** Travel agents pay fees for installation and use of terminals and other equipment in their offices.

By many conventional criteria, CRS providers may appear to possess market power. Table 1 reveals that two systems, Sabre and Apollo, account for approximately 60% of the national market. Concentration is even more pronounced in many major city markets, as Table 2 shows. Furthermore, only 6.5% of travel agents subscribed to more than one computer reservation system in 1986, which means a passenger usually must switch travel agents if he wants to use a different reservation system.\(^ {15}\)

\(\text{\textsuperscript{12}}\) MCSHANE, COMPUTER RESERVATION SYSTEMS: A STUDY OF THEIR IMPACT ON COMPETITION IN THE UNITED STATES AIRLINE INDUSTRY, 15-16 (1987) (offers a concise history).

\(\text{\textsuperscript{13}}\) In February 1990, the Pars System, owned by Northwest Air Lines and TWA, and the Datas II system, owned by Delta, completed a merger. See DOT; AIRLINE MARKETING PRACTICES, 47 (1990).

\(\text{\textsuperscript{14}}\) Morrison and Winston, supra note 4, at 64-65, suggests, United Air Lines and American Airlines may be able to set such excessive access charges for their service as to discourage other carriers from participation in their systems, thus giving United Air Lines and American Airlines the legal authority to institute total bias against these carriers.

### TABLE 1: CRS MARKET SHARE, 1988

<table>
<thead>
<tr>
<th>CRS Vendor</th>
<th>% Agency Locations</th>
<th>% Flights Booked</th>
<th>% Terminals</th>
<th>% Revenues</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sabre</td>
<td>35.3</td>
<td>43.1</td>
<td>39.5</td>
<td>38.8</td>
</tr>
<tr>
<td>Apollo</td>
<td>23.8</td>
<td>27.9</td>
<td>21.3</td>
<td>27.6</td>
</tr>
<tr>
<td>SystemOne</td>
<td>21.7</td>
<td>13.9</td>
<td>19.5</td>
<td>16.6</td>
</tr>
<tr>
<td>Pars</td>
<td>11.6</td>
<td>9.4</td>
<td>11.4</td>
<td>11.1</td>
</tr>
<tr>
<td>Datas II</td>
<td>7.6</td>
<td>5.7</td>
<td>8.3</td>
<td>5.9</td>
</tr>
</tbody>
</table>

Source: DOT, supra note 13, at 51.

### TABLE 2: 1988 REGIONAL SHARES OF BOOKINGS

<table>
<thead>
<tr>
<th></th>
<th>Sabre</th>
<th>Apollo</th>
<th>SystemOne</th>
<th>Pars</th>
<th>Datas II</th>
</tr>
</thead>
<tbody>
<tr>
<td>Atlanta</td>
<td>21.7</td>
<td>16.7</td>
<td>26.1</td>
<td>0.1</td>
<td>35.4</td>
</tr>
<tr>
<td>Boston</td>
<td>59.6</td>
<td>15.6</td>
<td>11.4</td>
<td>8.8</td>
<td>4.5</td>
</tr>
<tr>
<td>Charlotte</td>
<td>25.2</td>
<td>15.5</td>
<td>54.2</td>
<td>0.1</td>
<td>5.0</td>
</tr>
<tr>
<td>Chicago</td>
<td>40.3</td>
<td>46.8</td>
<td>4.2</td>
<td>5.4</td>
<td>3.3</td>
</tr>
<tr>
<td>Cincinnati</td>
<td>67.5</td>
<td>5.0</td>
<td>0.8</td>
<td>2.9</td>
<td>23.7</td>
</tr>
<tr>
<td>Dallas</td>
<td>87.3</td>
<td>3.7</td>
<td>1.4</td>
<td>0.6</td>
<td>7.0</td>
</tr>
<tr>
<td>Dayton</td>
<td>34.2</td>
<td>21.3</td>
<td>0.8</td>
<td>16.4</td>
<td>27.3</td>
</tr>
<tr>
<td>Denver</td>
<td>21.2</td>
<td>56.9</td>
<td>17.2</td>
<td>2.7</td>
<td>1.9</td>
</tr>
<tr>
<td>Detroit</td>
<td>47.7</td>
<td>35.9</td>
<td>5.3</td>
<td>4.9</td>
<td>6.2</td>
</tr>
<tr>
<td>El Paso</td>
<td>89.1</td>
<td>1.5</td>
<td>2.5</td>
<td>0.8</td>
<td>6.1</td>
</tr>
<tr>
<td>Honolulu</td>
<td>34.6</td>
<td>60.4</td>
<td>3.4</td>
<td>0.8</td>
<td>0.8</td>
</tr>
<tr>
<td>Houston</td>
<td>42.0</td>
<td>10.6</td>
<td>41.6</td>
<td>2.3</td>
<td>3.5</td>
</tr>
<tr>
<td>Kansas City</td>
<td>14.4</td>
<td>13.9</td>
<td>30.6</td>
<td>39.6</td>
<td>1.5</td>
</tr>
<tr>
<td>Las Vegas</td>
<td>22.3</td>
<td>23.3</td>
<td>16.2</td>
<td>34.1</td>
<td>4.1</td>
</tr>
<tr>
<td>Los Angeles</td>
<td>42.2</td>
<td>38.0</td>
<td>3.9</td>
<td>13.7</td>
<td>2.2</td>
</tr>
<tr>
<td>Memphis</td>
<td>45.0</td>
<td>9.0</td>
<td>1.7</td>
<td>17.9</td>
<td>26.4</td>
</tr>
<tr>
<td>Miami</td>
<td>12.0</td>
<td>1.6</td>
<td>79.7</td>
<td>1.2</td>
<td>5.5</td>
</tr>
<tr>
<td>Minneapolis</td>
<td>48.7</td>
<td>15.5</td>
<td>14.1</td>
<td>20.3</td>
<td>1.4</td>
</tr>
<tr>
<td>Nashville</td>
<td>85.0</td>
<td>1.0</td>
<td>9.5</td>
<td>1.5</td>
<td>3.0</td>
</tr>
<tr>
<td>New York</td>
<td>54.6</td>
<td>13.0</td>
<td>19.7</td>
<td>10.7</td>
<td>2.0</td>
</tr>
<tr>
<td>Orlando</td>
<td>15.7</td>
<td>17.3</td>
<td>42.7</td>
<td>0.7</td>
<td>23.5</td>
</tr>
<tr>
<td>Philadelphia</td>
<td>20.7</td>
<td>44.9</td>
<td>20.0</td>
<td>13.0</td>
<td>1.4</td>
</tr>
<tr>
<td>Phoenix</td>
<td>58.5</td>
<td>15.6</td>
<td>10.8</td>
<td>12.2</td>
<td>2.9</td>
</tr>
<tr>
<td>Pittsburgh</td>
<td>17.7</td>
<td>40.1</td>
<td>15.5</td>
<td>24.0</td>
<td>2.7</td>
</tr>
<tr>
<td>Raleigh-Durham</td>
<td>37.5</td>
<td>26.8</td>
<td>23.6</td>
<td>0.5</td>
<td>11.7</td>
</tr>
<tr>
<td>Salt Lake City</td>
<td>23.2</td>
<td>37.4</td>
<td>4.0</td>
<td>3.9</td>
<td>31.5</td>
</tr>
<tr>
<td>San Diego</td>
<td>51.7</td>
<td>36.3</td>
<td>2.5</td>
<td>6.7</td>
<td>2.8</td>
</tr>
<tr>
<td>San Francisco</td>
<td>37.8</td>
<td>44.9</td>
<td>2.5</td>
<td>10.3</td>
<td>4.5</td>
</tr>
<tr>
<td>Seattle</td>
<td>24.8</td>
<td>60.1</td>
<td>7.2</td>
<td>3.3</td>
<td>4.6</td>
</tr>
<tr>
<td>St. Louis</td>
<td>25.3</td>
<td>3.2</td>
<td>4.2</td>
<td>66.1</td>
<td>1.2</td>
</tr>
<tr>
<td>Tampa</td>
<td>17.6</td>
<td>13.9</td>
<td>48.6</td>
<td>3.2</td>
<td>16.8</td>
</tr>
<tr>
<td>Washington</td>
<td>56.4</td>
<td>29.3</td>
<td>8.9</td>
<td>4.0</td>
<td>1.4</td>
</tr>
</tbody>
</table>

Source: DOT, supra note 13, at 99.
There is also evidence of barriers to entry. The costs of developing computer systems and software may be sunk, especially for a non-airline company, since such a company does not already have an internal computer system for tracking its own flights. Department of Transportation (DOT) also found evidence of economies of scale, economies of scope, and learning curve effects, although economists disagree on whether these phenomena constitute barriers to entry.16

In addition, travel agents and reservation system owners sign contracts for up to five years. Rollover contractual provisions have required travel agents to renew all of their contracts with a vendor whenever that vendor installs new equipment.17 Minimum-use provisions often require the travel agent to book 50% of its flights on a given CRS. The contracts also typically contain liquidated-damages provisions that discourage a travel agent from switching systems before the contract expires.18 Not only have these clauses generated a flood of litigation but many airlines and travel agents charge that rollover and minimum use provisions create exclusive dealing relationships. In addition, they argue that the liquidated damages provisions do far more than compensate reservation system vendors for losses incurred when travel agents break the contract.19

None of these contractual provisions would lead to monopolistic pricing if the contracting process itself is competitive, and Demsetz20 demonstrated as much in his discussion of contracting as an alternative to public utility regulation. However, the fairly small number of system vendors, coupled with the presence of sunk costs, suggests that system vendors may indeed possess some market power, allowing them to extract contract terms that deter economically efficient entry.

Critics of CRS usually point to fairly high profits to clinch the argument. A variety of private studies have disputed the profitability of reservation systems, but most of them have examined accounting profits.21

16. See id. at 24-27. For a discussion of whether these phenomena constitute barriers to entry, see G. Stigler, The Organization of Industry, 67-70 (1983); and Demsetz, Barriers to Entry, 72 Am. Econ. Rev. 47 (1982).

17. However, Covia Partnership, which owns the Apollo CRS, claims that it discontinued use of such rollovers in 1987, and it is not aware that any other CRS vendors still use them. DOT Comments of Covia Partnership, Doc. No. 46494 (Nov. 20, 1989).

18. An internal United Air Lines memo dated April 29, 1985 notes, "The liquidated damages provisions in all of the new contracts will make conversions of Apollo very unattractive to United's competitors." An AMR Corp. memo on "Account Retention," dated August 21, 1985, states, "The primary intent of the liquidated damages clause was to ensure subscribers do not easily convert to a competitive system." The memos can be found as attachments B and C to Comments of Delta Air Lines, DOT Doc. No. 46494 (Nov. 20, 1989).


21. See DOT, supra note 15, at 18-19, for citations and a review of these studies, most of which were sponsored by CRS vendors or their critics.
The DOT, on the other hand, estimated the systems' "internal" or "economic" rate of return—the discount rate which equates the present value of cash flows with the amount invested to create the system. Employing assumptions used in many industry-sponsored studies, DOT concluded that the three largest systems earn rates of return exceeding 100%.22

III. THE STATUS OF CRS POLICY

Despite this evidence, courts have declined to find CRS vendors guilty of antitrust violations. In United Air Lines v. Austin Travel Corp.,23 the court awarded United Air Lines $408,375 in liquidated damages when Austin Travel Corp., a Long Island travel agent, terminated its Apollo leases and installed Texas Air's SystemOne. Austin had countered United's suit by accusing United of monopolization, attempted monopolization, and unreasonable restraint of trade. The court found United innocent of monopolization because Apollo accounted for only 8% of revenues generated by CRS bookings in the Long Island area. It suggested that only Sabre, the leading system, might possess monopoly power. The court also declared that there was no evidence that Apollo might have succeeded in attempted monopolization. Finally, the court denied that Apollo's rollover, minimum use, and liquidated-damages provisions constituted unreasonable restraints of trade. In general, the court noted, "Austin relied upon inadmissable hearsay from irrelevant governmental publications, testimony of witnesses without first-hand knowledge of any facts relating to United's practices or to the relevant Long Island market, and speculative assertions unaccompanied by specific direct evidence."24

In a later set of cases, the same court essentially declared the CRS market competitive on the grounds that travel agents have alternatives to the dominant CRS. It stated, "The presence or absence of substitutes to which buyers may turn negates an inference of market power. This suggests that United cannot control price or exclude competition."25 In December 1989, a California jury decided that neither Sabre nor Apollo possesses monopoly power.26

At the same time, even though a particular practice may not consti-

tute an antitrust violation, Section 411 of the Federal Aviation Act gives the (CAB) and its successor in airline regulation, the DOT, authority to regulate such airline business practices. In 1984, the CAB issued regulations prohibiting CRS display bias, discriminatory booking fees, tie-ins, and exclusive use contracts. It also imposed a five-year limit on CRS contracts and required CRS vendors to make enhanced features available on a non-discriminatory basis. In upholding the regulations, Judge Richard Posner noted that Section 411 empowers the CAB to regulate "unfair and deceptive" business practices and "unfair" methods of competition. "We know from many decisions, under both that section [411] and its progenitor, section 5 of the Federal Trade Commission Act, that the Board can forbid anticompetitive practices before they become serious enough to violate the Sherman Act."28

The question of competition in the CRS market, therefore, is still very much a live policy issue. Since the CAB's 1984 regulations originally expired on December 31, 1990, DOT initiated a rulemaking to establish new regulations. Its notice of proposed rulemaking stated, "Commentors should be aware that the Department's position is that the CRS rules should be extended and that revisions related to further limiting the term of CRS contracts, prohibiting mandatory rollovers, and establishing a quantitative or qualitative standard on minimum use clauses may be warranted."29 DOT has since extended the original regulations through 1991 as it continues to grapple with the task of writing new regulations.

More extreme proposals also abound. One would force airlines to divest CRS, removing the system vendors' and travel agents' incentives to steer customers toward flights on reservation-system-owning airlines.30 Another would limit the booking fees that system vendors could charge.31 The Department of Justice (DOJ), meanwhile, has called for a rule requiring a direct pass-through of booking fees to travel agents or passengers,

27. 14 C.F.R. Parts 255, 256.
31. Northwest and TWA proposed submitting fee increases to arbitrators charged with fixing "fair and reasonable" fees. They also sought permission to assess discriminatorily high fees against airlines that raised their own CRS fees. See Comments of Northwest Airlines, Inc., and Trans World Airlines, Inc., DOT Doc. No. 46494, at 17-18 (Nov. 20, 1989). The Orient Airline Association called for a cap on fees at current levels, with increases permitted only if "justified." See Comments of the Orient Airline Association, DOT Doc. No. 46494 (Nov. 20, 1989), at 46. See also Midwest Express Airlines, Inc., Comments on the ANPR, DOT Doc. No. 46494, 8 (Nov. 22, 1989).
rather than having airlines pay the booking fees to the CRS vendors.32

What policy response, if any, is justified by economic analysis? A careful look at the peculiar nature of CRS reveals that Congress, courts, and regulatory agencies must first take into account the economics of entrepreneurship and innovation if they seek to design CRS rules that maximize consumer welfare.33

IV. COMPUTER RESERVATION SYSTEMS AS CREATIVE DESTRUCTION

CRS are a cost-reducing innovation that might also convey market power. As a result, CRS policymakers confront a conflict between two forms of economic efficiency: "allocative efficiency" and "productive efficiency."

Allocative efficiency occurs when each unit of each resource is employed in the use that consumers value most highly. When allocative efficiency is maximized, the result is "Pareto-efficient;" no re-allocation of resources can make one consumer better off without making someone else worse off. In such a state, business firms earn only "competitive" profits just sufficient to cover their cost of capital. As used by many economists, the term "economic efficiency" frequently refers only to allocative efficiency. Economists have demonstrated that under the stringent assumptions necessary for perfectly competitive equilibrium, an unhampered marketplace maximizes allocative efficiency.34 Critics of developments in deregulated transportation markets, in turn, have faulted deregulation precisely because it has not produced a perfectly competitive result.35

A public policy that seeks to prevent firms from earning above-competitive profits would not necessarily maximize consumer welfare because such a policy could hamper productive efficiency. Productive efficiency occurs when firms discover new ways to lower costs, produce new products that better satisfy consumer desires, and find better ways of informing consumers about the options available to them. Firms become efficient in a quest for profits—profits greater than those that they would earn if the market were in a continual state of perfect competition. A market in which firms are earning above-competitive profits by enhancing productive efficiency cannot simultaneously be a perfectly competitive

33. P. Dempsey, supra note 5, at 35-36, argues that regulation ought to serve goals other than economic efficiency. This article does not dispute that point. The argument here is merely that most previous discussions of CRS have offered an incomplete economic analysis.
35. See, e.g., P. DEMPSEY, supra note 5, at 35.
market in which allocative efficiency is maximized. Such logic stands behind Bork's observation that "A determined attempt to remake the American economy into a replica of the textbook model of [perfect] competition would have roughly the same effect on national wealth as several dozen strategically placed nuclear explosions." It also stands behind the realization among public utility analysts that rate-of-return regulation may actually harm consumer interests by stunting the regulated firm's incentives to innovate.

In striking a balance between allocative and productive efficiency, the "Williamson Tradeoff" might seem to be the most sensible way to evaluate CRS. Williamson developed the model to evaluate the welfare effects of a large merger which created market power while lowering costs, and Bork champions this model as a heuristic device for implementing antitrust policy. A look at Figure 1, however, suggests that this model may not be very appropriate for analyzing radical innovations.


37. For a recent symposium on alternatives to rate-of-return regulation, see 20 RAND J. OF ECON. (1989).


In the conventional Williamson framework, the initial cost curve under perfect competition is \( AC_1 \), and price-taking firms produce a total output of \( Q_1 \) to be sold at a competitive price \( P_1 \). A merger or other market change then occurs which lowers the cost curve to \( AC_2 \) but also allows a single firm to capture the entire market. Price rises to \( P_2 \), and quantity falls to \( Q_2 \). In deciding whether to challenge the merger or other practice, policymakers must weigh the rectangle-shaped increase in producer surplus against the triangle-shaped loss in consumer surplus.

In contrast to this model, CRS seem to have swept the travel industry not just because they increased airlines' profits, but also because they lowered the costs that CRS customers—travel agents and non-CRS-owning airlines—pay when they book passengers. Several pieces of evidence point in this direction.

First of all, a 1981 Harris survey indicates that the systems raised travel agents' productivity by an average of 41\%.\(^{40}\) In fact, "One travel agent estimated that his employees could make a reservation using a

CRS in one-third the time it would take to look up schedules in a book and make reservations over the telephone." United Air Lines estimates that the Apollo system's booking fee is less than the cost of making a reservation by calling the airline's own reservation staff.

Indeed, despite complaints about the way CRS have been managed, 95% of all travel agents now subscribe to at least one system, even though they have the option of returning to pre-automation technology. The fact that they do not suggests that reservation systems vendors are charging prices lower than the cost of alternative technologies, and so travel agents' costs are most likely lower with the systems than without them. When the CAB issued its CRS regulations in 1984, it "concluded that, because the systems were so much more efficient than other tools, almost all travel agents used CRS to determine what airline services and fares are available, to make bookings, and to issue tickets." Similarly, the DOJ has asserted, "For most carriers, alternative distribution methods are not acceptable substitutes for being listed in a CRS."

Finally, not even the most ardent critics propose to ban CRS; they seek only to regulate them. If the reservation systems raised ticket prices above what they would be if travel agents were not automated, one would expect critics to call for abolition of the systems themselves.

For these reasons CRS seem an ideal example of "Schumpeterian" innovation. Schumpeter stressed the importance of competition which "commands a decisive cost or quality advantage and which strikes not at the margins of the profits and the outputs of existing firms but at their foundations and their very lives." Figure 2 shows the effects of such an innovation. The cost curve for provision of reservation services falls from AC\(_1\) to AC\(_2\), a large enough drop that price falls and the quantity of reservation services purchased expands. Both consumer surplus and profits rise, even though the firm produces at point B, which is the "monopoly"

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41. Supra note 2, at 3.
43. DOT, supra note 15, at 10.
44. MORRISON AND WINSTON, supra note 4, at 70, suggest that travelers' welfare may also be higher with computer reservation systems than without them: "In some if not most cases, given travelers' lack of expertise in collecting flight information, even a biased CRS can be an improvement over independent search."
46. Comments of the United States Department of Justice, DOT Doc. No. 46494, 10 (Nov. 22, 1989).
47. A long assortment of CRS critics have called for divestiture, rate regulations or self help. See Levine, supra note 1; Midwest Express Airlines, Inc., and Wash. Post supra note 30; Comments of Northwest Airlines and Comments of the Orient Airline Assoc., supra note 31.
48. J. SCHUMPETER, supra note 11, at 84.
price and quantity, given the new cost curve.49

Figure 2: Schumpeterian Innovation

Clearly, the move from point A to point B is "Pareto-superior." Schumpeterian innovations, defined as in Figure 2, will always expand output. Therefore, they will always pass Posner's "output test," another proposed test for evaluating the effect of an industry practice on consumer welfare.50

All of this analysis will be of little comfort to anyone who observes point C in Figure 2. A relevant policy question is whether the firm could do even better. If the computer reservation service vendor were forced to

49. Such innovation has also been termed "drastic" by Arrow, Economic Welfare and the Allocation of Resources for Inventions, in THE RATE AND DIRECTION OF INVENTIVE ACTIVITY (R. Nelson ed., 1962) and "major" by M. Kamien and N. Schwartz, Market Structure and Innovation 38 (1982).

price its product competitively, quantity would expand still further to $Q_3$, and price would fall to $P_3$. Proposals to change CRS business practices are best understood as attempts to effect such a switch.

If moving to point C were costless, the choice would be clear. However, such a move may entail very real costs because the potential to employ seemingly monopolistic business practices no doubt provided airlines with a powerful incentive to develop CRS in the first place. It is possible that the systems would not have been developed had airlines known that display bias would be prohibited, contract lengths would be limited, and other contractual terms would be restricted. Judge Posner even speculated in 1985, "Maybe biasing of computerized reservation systems can be defended as a method by which airlines that spent hundreds of millions of dollars to develop computerized reservation systems, at considerable risk of failure, can recoup their investment with a profit commensurate with the amount of the investment, the length of time it has been outstanding, and the risk of loss."51 Posner’s remark echoes Schumpeter’s commentary on innovative firms that employ seemingly monopolistic practices to safeguard their innovations:

As we have seen, such concerns are aggressors by nature and wield the really effective weapon of competition. Their intrusion can only in the rarest of cases fail to improve total output. But these aggressors are so circumstanced as to require, for purposes of attack and defense, also pieces of armor other than price and quality of their produce which, moreover, must be strategically manipulated all along so that at any point in time they seem to be doing nothing but restricting their output and keeping prices high.52

In other words, even if various CRS business practices generate high rates of return, the high rates of return constitute monopoly rents only from the static perspective of one who observes the industry after the CRS has been invented and marketed. From the perspective of earlier periods, when the CRS was just an untested idea, the high profits are just a residual reward to the companies that first recognized the potential of CRS and aggressively developed and marketed them. Therefore, even if CRS vendors possess market power, it is not clear that eliminating such market power maximizes consumer welfare.53-54

51. United Air Lines, Inc. v. Civil Aeronautics Board, 766 F.2d at 1113.
52. J. Schumpeter supra note 11, at 89. See also M. Kamien and N. Schwartz, supra note 48.
53. This general theoretical argument can be found in I. Kirzner, Competition and Entrepreneurship, 133-34 (1973).
54. It is crucial to distinguish this discussion from the voluminous literature, largely inspired by Schumpeter, that examines the impact of market structure on innovation. This literature typically asks questions like, "Are monopolies or large firms more innovative than competitive or small firms?" The argument here is not that possession of market power encourages innovation, but that the prospective opportunity of possessing market power encourages innovation. M.
Of course, CRS will not disappear now if the government merely constrains their profits. In that sense, they are like a capital investment whose quasi-rents are ever available to be expropriated. But just as a public policy that expropriates quasi-rents discourages the investments that generate quasi-rents, so too do public policies that expropriate entrepreneurial rents discourage entrepreneurial discovery.\textsuperscript{55}

The economics literature on innovation contains extensive discussions of the importance of "appropriability"—the innovator's ability to capture rents from his innovation.\textsuperscript{56} Because imitation may erode these rents, the government awards patents, and innovative firms adopt an assortment of business strategies to differentiate their products and prevent imitation. In the CRS case, the policies at issue are ones that would actually impinge upon appropriability, rather than enhance it. Tighter regulation of CRS, therefore, could discourage further innovation in the CRS industry. It could also discourage innovation elsewhere in the economy if entrepreneurs in general assume that they too might have to forfeit their innovation-induced profits.

Kamien and Schwartz\textsuperscript{57} note that there currently exists no precise way to calculate the ideal departure from perfect competition that encourages the optimal amount of innovation. However, economic theories of entrepreneurship suggest general principles that can be applied to show how various policy proposals would affect incentives to innovate.

By its very nature, innovation involves dealing with the uncertain fu-
tire. An entrepreneur pays certain prices for resources in the hope that he can produce and later sell a product for a price that more than covers its cost. His residual profit contains "an element of calculation and an element of luck." CRS policy rules consistent with maximal incentives to innovate would, at a minimum, have to avoid confiscating those calculated profits that motivated airline entrepreneurs to undertake the innovation.

Of course, in practice, it is difficult if not impossible to ascertain precisely what level or probability distribution of anticipated profits motivated airlines to develop and introduce the CRS. Even if such a calculation were possible—for example, by examining internal documents that show how airlines decided the investment was worth the risk—it might miss an important aspect of the entrepreneurial process. Dosi argues that innovators face a form of "strong uncertainty" that prevents them from even listing all of the possible results of their innovations. An innovative firm may thus form some estimate of anticipated profits from an innovation, but it also expects that the innovation will generate additional profit opportunities whose precise magnitude and nature it cannot yet foresee. These vaguely-perceived profit opportunities can also encourage innovation. These profits are not simply outcomes to which the innovator assigned a low probability. They might more aptly be termed "pleasant surprises." The innovator expects that such surprises will occur, but he does not know enough about them to include them in his calculations of expected returns:

What switches on the entrepreneurial antennae appears to be the potential entrepreneur's awareness that the situation holds unknown possibilities unconstrained by known constraints. It is the entrepreneur's awareness of the open-endedness of the decision context that appears to stimulate the qualities of self-reliance, initiative, and discovery.

When an entrepreneur contemplates making an innovation, he may be able to imagine some set of possible outcomes and assign subjective probabilities to them. But in addition to these outcomes, there may also be a set of outcomes that the innovator is simply unaware of, or that he

58. F. Knight, Risk, Uncertainty, and Profit, at 277 (1921).
59. Dosi, supra note 55, at 1134. Dosi suggests, "In general, the uncertainty associated with innovative activities is much stronger than that with which familiar economic models deal. It involves not only lack of knowledge of the precise cost and outcomes of different alternatives, often also lack of knowledge of what the alternatives are. . . . In fact, let us distinguish between (a) the notion of uncertainty familiar to economic analysis defined in terms of imperfect information about the occurrence of a known list of events and (b) what we could call strong uncertainty whereby the list of possible events is unknown." Dosi's "strong uncertainty" is, of course, equivalent to Frank Knight's "true" uncertainty—a risk which is uninsurable "because there is no objective measure of the probability of gain or loss." Supra note 57, at 119-20. For a concise explication of Knight's theory, see Hébert and Link, The Entrepreneur, at 69-72 (1982).
has insufficient knowledge of to assign a subjective probability. Nevertheless, the dim realization that an innovation may be much more profitable than predicted is itself an important incentive. Therefore, preserving the "open-endedness of the decision context" may be as important as allowing the innovator to keep some amount of profit that he actually anticipated receiving.⁶¹

In the CRS context, this theory suggests that regulators should tread lightly when they seek to restrain CRS business practices, because any diminution of CRS profits may reduce incentives for innovation. In some cases, a reduction in such incentives may be worth bearing. For example, some of the profit the CRS owner with market power earns may stem from its ability to mislead travel agents or air passengers. As Judge Posner noted, the opportunity to deceive may indeed encourage innovation. Nevertheless, it is doubtful that the benefits of such incentives exceed the costs that deception imposes on society. Levine's comment seems persuasive: "It is difficult to defend as efficient those practices which reward undisciplined distortion of choices by agents at the externalized expense of principals."⁶² The agents, in Levine's view, are airline CRS owners who claim that their systems are unbiased, or fail to disclose the extent of the bias. The principals are the airline passengers who count on CRS as a source of unbiased information.

Focusing on the prevention of deception provides a clear-cut standard for evaluating CRS policy proposals. To the extent that a policy prevents deception, it offers a clear and visible benefit to balance against the diminution in entrepreneurial incentives. To the extent that a policy merely diminishes CRS profits without deterring deception, the effect on consumer welfare is much more problematic. Such a policy constrains entrepreneurial incentives in the hope that consumers will gain more from lower ticket prices than they lose in benefits from increased innovation.

V. POLICY OPTIONS

Major CRS policies and policy proposals generally regulate one of four things: bias, prices, other contract terms, and industry structure. Some of these policies control deception, while others merely control profits. Consider each category in turn.

⁶¹ Similarly, J. Schumpeter suggests, "Spectacular prizes much greater than would have been necessary to call forth the particular effort are thrown to a small minority of winners, thus propelling much more efficaciously than more equal and more "just" distribution would, the activity of that large majority of businessmen who receive in return very modest compensation or nothing or less than nothing, and yet do their utmost because they have the big prizes before their eyes and overrate their chances of doing equally well." Supra note 11, at 73-74. See also F. KNIGHT, supra note 57, at 283-84.

⁶² Levine, supra note 1, at 489.
A. Bias

CRS bias comes in several forms, and it is important to distinguish between them. The most obvious is display bias, which the CAB outlawed in 1984.

Initially, some airlines freely admitted that their CRS displays were biased. In particular, American Airlines’ 1982 annual report said that the Sabre system was profitable in part because it permitted American to give its flights preferential display.63 Richard Fahy, American’s associate general counsel, commented, “Vendors viewed display preference as nothing more than putting the vendors’ product on a higher shelf in the display so that it will be at eye level for the consumer. In the grocery business, such competition for shelf space is a normal part of the marketing game.”64 However, since most terminals are located in travel agents’ offices, only the travel agent, and not the customer, can see all of the shelves. Travel agents can take advantage of this fact by booking passengers on more expensive flights in order to collect incentive commissions from CRS-owning airlines.65

Some airlines, such as Delta, have claimed that their CRS’s are unbiased, but such claims are difficult for consumers to evaluate, given the complexity of the information involved. Others have simply failed to disclose the existence or extent of bias.66 Even if all such information is disclosed, consumers would have a hard time preventing bias. Given the high market shares of the top CRS vendor in many major cities, it may be difficult for consumers to shop travel agents using competing CRS’s, and the long-term contracts binding travel agents to specific CRS vendors make it difficult for newer, unbiased CRS vendors to enter the market. In short, display bias seems a prime candidate for regulation on the basis of preventing deception.

Since the CAB prohibited display bias, CRS-owning airlines have continued to earn substantial incremental revenues. The DOT’s 1988 study postulated that these revenues are the result of a “halo effect” that encourages travel agents to book flights on the CRS-owning airline.67 Some U.S. airlines claim that this effect results from “functional bias,” which occurs when a CRS contains less timely or less accurate information for some airlines than for others.68 Such bias may occur because the

63. AMERICAN AIRLINES INC. ANNUAL REPORT 13-14 (1982).
65. Levine, supra note 1, at 60.
CRS lets travel agents access the vendor's own internal computer system, while information on competing airlines' flights must be loaded into the CRS. American Airlines, on the other hand, claims that the halo effect is merely the result of good business relationships with travel agents.\textsuperscript{69} The DOT, meanwhile, has suggested that functional or "architectural" bias, to the extent that it exists, is mainly the result of the state of technology, and that it is diminishing over time.\textsuperscript{70}

This type of bias poses a more difficult problem, because current technology may simply make it less expensive to access information about the vendor airline in a timely manner. Regulation in this area might enhance consumer welfare, but this result would be certain only if regulation can be implemented without eliminating those economies of scope that stem simply from well-developed business relationships.

\textbf{B. PRICES}

In 1984, the CAB explicitly declined to impose ceilings on CRS booking fees. Its rationale fits well with the notion of the CRS as a Schumpeterian innovation, for the CAB stated that its refusal to set fees would help preserve "the legitimate competitive advantages the CRS vendors have gained because of their innovations."\textsuperscript{71} Nevertheless, the CAB did impose limited regulation on fees by prohibiting discrimination not justified by cost differences: "[W]e anticipate that the bargaining power of some participating carriers, combined with a non-discrimination requirement, will generally hold fees close to reasonable levels."\textsuperscript{72}

This decision is a good example of a regulation that ostensibly permits CRS vendors to cover their costs while simultaneously diminishing their entrepreneurial incentives. Under the anti-discrimination regulation, CRS vendors should be able to earn a profit, as long as they can cover their costs by charging all participating carriers the same fee.\textsuperscript{73} Nevertheless, the systems are less profitable than if price discrimination were permitted. While such a regulation is understandable in light of the well-established antitrust aversion to price discrimination, the elimination of discrimination is not costless, since that which diminishes profits diminishes entrepreneurial incentives.

\textsuperscript{70} DOT \textit{supra} note 13, at 70.
\textsuperscript{71} 54 Fed. Reg. at 32,542.
\textsuperscript{72} 54 Fed. Reg. at 32,552.
\textsuperscript{73} The regulation creates additional problems if CRS vendors can only cover their costs by practicing price discrimination. Given the profit records of CRS systems, it is doubtful that differential pricing is necessary, at least for the larger systems.
C. OTHER CONTRACT PROVISIONS

Other CRS contract provisions most clearly exemplify the types of "armor" that Schumpeter suggested innovative firms may need when taking entrepreneurial risks. Indeed, since Schumpeter, it is a well-established point in the scholarly economics literature that long-term contracts, liquidated damages provisions, minimum-use requirements, and similar restrictions can all encourage businesses to invest in sunk capital assets with low resale value.\textsuperscript{74}

When the CAB decided to limit contracts to five years, it essentially ignored this point. The CAB justified the limit by stating, "we will intervene to eliminate only those contract terms clearly designed to prevent travel agents from switching systems. We have found no other business justification for the lengthy contracts."\textsuperscript{75} In fact, the CAB agreed to five years, rather than a shorter period, only because American Airlines argued that shorter contract terms would prevent airlines from taking advantage of investment tax credits. There is no doubt that long-term contracts discourage travel agents from switching to another CRS; that is the purpose of a long-term contract. In limiting contract terms, the CAB either assumed away the problem of sunk costs, or it assumed, without offering proof, that airlines can recover their sunk investments within five years.

The CAB's decision not to regulate liquidated damages displays a greater appreciation of their potentially efficiency-enhancing role. The agency left adjudication of liquidated damages to the courts, "because they can tailor a decree to the particular circumstances."\textsuperscript{76} Courts, meanwhile, have generally upheld liquidated damages clauses as a reasonable way for CRS owners to protect their investment.\textsuperscript{77}

Finally, such practices as automatic rollovers, which renew the travel agent's contract for all of its CRS equipment when it receives one new piece of equipment, and tie-in sales are less defensible as means of protecting sunk capital. Nevertheless, since they are non-deceptive means of expanding CRS profits, Schumpeterian analysis suggests that prohibiting them may well make consumers worse off by diminishing the incentives to innovate.

D. STRUCTURE

The CAB and DOT have declined to call for divestiture of airline-

\textsuperscript{74} See, e.g., O. Williamson, The Economic Institutions of Capitalism (1985).
\textsuperscript{75} 49 Fed. Reg. at 32,556.
\textsuperscript{76} 49 Fed. Reg. at 32,556.
\textsuperscript{77} United Air Lines, Inc. v. Austin Travel Corp., 867 F.2d at 740.
owned CRS's, but others have felt free to champion divestiture. Levine makes the case for divestiture in a careful and straightforward manner. In his view, airlines owning CRS's have an incentive to bias their CRS operations against competitors. The mere outlawing of display bias is not a sufficient remedy, as the persistence of substantial incremental revenues shows. Therefore, divestiture is the only effective way to prevent bias.

It is important to note that this argument does not claim that divestiture would completely eliminate market power. After all, if ownership of a CRS can generate a stream of monopoly profits, the airline can capture those profits in the sale price of the CRS. However, the airline could not capture bias-induced incremental revenues by selling its CRS to a non-airline company, because a non-airline has no way of using the CRS to earn incremental revenues. Therefore, while divestiture may not eliminate market power, it can eliminate bias.

A significant problem with this solution is that in the absence of display bias, observed incremental revenues may be due either to other forms of bias or to the existence of good business relationships. Divestiture would certainly eliminate incentives to develop new, hidden forms of bias, but it would also diminish CRS-owning airlines' incentives to invest in developing good business relationships. The wisdom of divestiture on this count will have to await further empirical research on the origins of remaining incremental revenues.

Of course, divestiture creates another, more obvious threat to entrepreneurial incentives; it would prevent airlines from exploiting economies of scope in the joint provision of air travel and CRS services. To the extent that innovators are motivated by a desire to capture economies of scope, divestiture would quash this incentive. The CAB made essentially this point in rejecting divestiture.

VI. CONCLUSION

The legal and economic debate over CRS has frequently overlooked the peculiar economics of innovation and entrepreneurship. In so doing, scholars and regulators have spotlighted the benefits of certain forms of regulation without adequately considering the costs. Incorporating a Schumpeterian theory of innovation into CRS analysis makes existing and proposed regulation of prices, contract terms, and industry structure much less attractive from the perspective of consumer welfare. Regulation designed to prevent bias, however, still seems to be efficiency-en-

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78. Levine, supra note 1.
79. Unless, of course, the non-airline company were a car rental firm or other company that also has its products listed on the CRS.
hancing because the reduction in entrepreneurial incentives is balanced by the benefits of preventing deception.

Interestingly, this approach to the CRS problem finds a close parallel in Judge Posner's economic analysis of the CAB's 1984 regulations. Posner's decision upholding the regulations notes that prevention of bias clearly stems from the CAB's mandate to prevent "unfair and deceptive" practices. However, he questioned the CAB's finding that CRS vendors possess market power. Ultimately, the court upheld the CAB's ban on price discrimination only because Section 411 of the Federal Aviation Act gave the CAB power to regulate competitive practices even when they do not constitute antitrust violations.81

Given this analysis, an important caveat from Schumpeter himself is in order. After defending many monopolistic practices on the grounds that they encourage innovation, he notes, "our argument does not amount to a case against state regulation. It does show that there is no general case for . . . the prosecution of everything that qualifies as a restraint of trade."82 The possibility of employing various non-fraudulent but currently controversial CRS business practices may have motivated airlines to develop and market these systems. Consumers may, however, be willing to give up some degree of innovation in exchange for a degree of protection from the innovator's market power. Nevertheless, before policymakers can make such a tradeoff in the CRS industry, they must first recognize that it exists. Thus far, few have.

81. See United Air Lines, Inc. v. Civil Aeronautics Board, 766 F.2d at 1107.
82. D.O.T. supra note 13, at 89.
The Civil Rights of the Handicapped in Transportation: The Americans With Disabilities Act and Related Legislation

PAUL STEPHEN DEMPSEY*

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Described as the most sweeping civil rights legislation in a quarter century, the Americans With Disabilities Act of 1990 [ADA] seeks to eliminate bias by private and public enterprises in areas of employment, public accommodations, transportation and telecommunications. The legislation creates federally mandated rights and responsibilities for a class of beneficiaries unparalleled since the 1960s.

Although much of the new legislation is devoted to issues of employment discrimination, its transportation provisions are also quite important. The fundamental thrust of the ADA is to integrate the disabled into the mainstream of the nation. As one Congressman put it, the purpose of the ADA is to "open up mainline transportation systems to people with disabilities. It is designed to make the America of the future accessible to all our citizens." 

Another Congressman proclaimed that the ADA "represents a major breakthrough in ensuring that citizens who have been robbed of their mobility by disabilities or accidents can get to work, can pursue their interests, and broaden their lives with the access our nation’s public transportation facilities offer." Still another observed:

All of us recognize the crucial role transportation plays in our lives. It is the veritable lifeline which enables all persons to enjoy the full economic and social benefits which our country offers. To be denied effective transportation is to be denied the full benefits of employment, public and private services, and other basic opportunities.

While many Americans take transportation access for granted, those who have lost it understand the crucial role it plays in everything we do, both professionally and socially.

The transportation provisions of the ADA were among the most hotly contested, primarily because of the cost of compliance. In a nutshell, the

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5. Tucker, The Americans With Disabilities Act: An Overview, 1989 U. ILL. L. REV. 923, 932 (1989) [hereinafter Overview]. For example, Greyhound Corporation argued that compliance with the ADA would cost $40 million a year, "a sum that dwarfs its expected 1989 profit of $8.5 million." Disabled rights advocates, however, have contended that the cost estimates cited by the transportation companies are unrealistic. For example, during congressional hearings on the ADA, Greyhound alleged that it costs $35,000 to purchase one lift for an over-the-road bus, while others indicated that lifts could be purchased for less than $8,000.
ADA requires that all new vehicles purchased by public and private transportation firms be equipped with lifts and other facilities for the handicapped. In three years, telephone companies must provide special equipment enabling the hearing or speech impaired to communicate with people using ordinary telephones. This bit of social engineering is designed to eradicate the problems of discrimination against the handicapped.

The ADA is the most recent in a series of acts intended to eradicate the disadvantages of the handicapped in transportation going back to 1970. With the graying of America, more of its citizens find themselves immobile and requiring federal legislative assistance to move about. This article reviews all the major legislative and regulatory attempts to enhance the mobility of the disabled.

II. THE PROBLEM

People with disabilities are "substantially worse off on almost any indicator of well-being than are the non-disabled." Less than 25% of disabled men and 13% of disabled women hold jobs. Their earnings are but two-thirds of all workers. In 1984, half the disabled people over the age of 16 had household incomes of $15,000 or less, compared with only 25% of non-disabled.

6. A Law for Every American, N.Y. Times, July 27, 1990, § A, at 26, col. 1 [hereinafter Every American]. The original Senate bill, passed last September, was vague in its instructions to employers. More precise language has since been added and, partly as a result of adjustments made by the House, employers will have time to get ready. Businesses with more than 25 employees will have 18 months to meet the public accommodations rules and two years to meet the employment revisions. Small businesses would be given more time to comply. The three-year time limit may be extended by the Secretary of Transportation for up to twenty years for "extraordinarily expensive structural changes." See 135 CONG. REC. S10,954, S10,957 (daily ed. Sept. 12, 1989).

7. BURKHAUSER & HAVEMAN, UNITED STATES POLICY TOWARD THE DISABLED AND EMPLOYMENT HANDICAPPED 15 (International Institute of Management/Labor Market Policy Discussion Paper No. 84-4a, 1984), quoted in McCluskey, Rethinking Equality and Difference, 97 YALE L.J. 863, 863-64 (1988) [hereinafter Rethinking Equality]. People with physical disabilities in the United States face, and continue to struggle against, many social and economic disadvantages. Over the years, laws have explicitly excluded people with disabilities from holding public office, serving on juries, marrying, working in certain occupations, bearing children, attending school, and even from being seen on public streets. Even today, people with disabilities are "substantially worse off in almost any indicator of well-being (including education, employment, and earnings) than are the non-disabled."

8. Every American, supra note 6, at 26. The Federal Government now spends $57 billion every year on benefits for the disabled. That figure will undoubtedly decline if the disabled have greater access to jobs.

9. Rethinking Equality, supra note 7, at 864. To alleviate some of the problems confronted by people with disabilities, Congress enacted section 504 of the Rehabilitation Act of 1973, which prohibits discrimination on the basis of disability in federally funded programs. Congress modeled section 504 on civil rights legislation that prohibits race and sex discrimination.
Slightly "more than half of the population of the United States expresses slightly positive attitudes toward the disabled. The rest openly admit to negative attitudes. They see the handicapped as different and in some ways inferior to normal people." 10

However, Professor James Frierson has observed that during the 1990's three trends will converge that should encourage employers to employ disabled employees. First, the number of young entry-level employees is declining to such an extent that many businesses are having difficulty filling positions. Second, the Education for the Handicapped Act of 1975, which required the mainstreaming of disabled students into regular schools, created the first generation of severely disabled individuals with an adequate educational background and training. Third, as the United States evolves toward an informational society, disabled persons' skills in office work, computer operation and other brain-power jobs will increasingly become more valuable. 11

Professor Frierson has also enumerated several myths which must be dispelled in order to achieve successful compliance with the ADA:12

Myth #1. Disabled employees have higher than average absenteeism. A survey by the U.S. Office of Vocational Rehabilitation shows that 55% of disabled workers have a better than average attendance rate, while only 5% have worse than average absenteeism.

Myth #2. Disabled employees have high turnover rates. The study cited above found that 88% of disabled employees have lower than average turnover rates.

Myth #3. Job performance and productivity of disabled employees is low. Ninety-one percent of disabled workers have average to higher than average productivity.

Myth #4. Disabled workers create a safety risk. Only 2% of disabled employees have a worse than average safety record, while 57% have higher than average safety records.

Myth #5. Making accommodations for disabled workers is too expensive. Surveys have shown that over 50% of all accommodations are cost free, while another 30% cost under $500. 13 In many cases all that is needed is rearrangement of office furniture, minor adjustments in employee break time,

10. Id. at 869. Despite the similarity of section 504 to race and sex discrimination legislation, and despite the similar problems addressed by these laws, courts and lawmakers interpreting section 504 have often departed from the race and sex discrimination model. In contrast to the race and sex discrimination doctrine, disability discrimination law generally assumes that physical difference, not prejudice, is the primary problem.


12. Much of this material is taken from two articles: Lester & Caudill, The Handicapped Worker: Seven Myths, TRAINING & DEVELOPING JOURNAL, August, 1987, at 50-51 [hereinafter Seven Myths]; and Stevens, Exploding the Myths About Hiring the Handicapped," PERSONNEL, December 1986, at 57-60 [hereinafter Exploding Myths].

13. Id. at 57-60.
or the installation of inexpensive equipment such as a $50 telephone amplifier.

Myth #6. Insurance rates will skyrocket if the company hires disabled employees. A U.S. Chamber of Commerce survey of 279 companies found that 90% did not incur added insurance costs by hiring disabled persons. Other surveys have shown that disabled persons create fewer accidents on the job than the average employee, thus lowering workers compensation costs and liability claims. Although many companies—especially small companies—worry about increased health, disability or life insurance claims that may result from hiring disabled employees, their concern is misplaced. Many types of disabilities do not cause continuing health problems. For example, most people in wheelchairs are in a completely stable medical condition that does not require future medical treatment, nor does it increase the chance of contracting illnesses or causing death.

Although it is true that other disabilities will cause future medical bills and may lead to an early total disability or death, i.e., AIDS, uncured cancer, diabetes, etc., the ADA allows employers and insurance companies to continue to use a pre-existing conditions clause whereby coverage of specific medical conditions diagnosed before an individual is first employed may be limited or excluded. The ADA is very clear in stating that nothing in the new law should be interpreted as changing the customary methods of underwriting employer-provided insurance coverage of employees.14

The disabled have also been subjected to indignities. For example, "an airline employee who resented having to help a 66-year old double amputee board a plane instead threw him onto a baggage dolly."15 Seventeen states prohibit people with epilepsy from marrying, and four states authorized the sterilization of people with epilepsy.16 Until 1973, a Chicago ordinance prohibited people who were "diseased" or "deformed" or an "unsightly or disgusting object" from exposing themselves to public view on the streets or in other public places.17 Thus, the Elephant Man would be exiled to the back alleys and dark corners of Chicago.

The ADA finds that "individuals with disabilities are a discrete and insular minority who have been faced with restrictions and limitations, subjected to a history of purposeful unequal treatment and relegated to a position of political powerlessness . . . ."18

A poll of the disabled reveals that half viewed employment discrimination as the cause of their unemployment, and 28% blame transporta-

16. Rethinking Equality, supra note 7, at 864. As recently as 1980, four states, Delaware, Mississippi, Oklahoma, and South Carolina had statutes authorizing the sterilization of persons with epilepsy.
17. Id.
tion barriers. Over half of those with severe disabilities identified transportation barriers as limiting their social activity.\textsuperscript{19} Transportation access is essential for many of the human activities the non-disabled take for granted: employment, education, shopping, recreation and political participation.\textsuperscript{20}

III. HISTORY OF THE LAW OF THE HANDICAPPED IN TRANSPORTATION: THE LONG AND WINDING ROAD

The Urban Mass Transportation Assistance Act of 1970 declared it national policy that elderly and handicapped people have the same right as other people to use mass transportation facilities and services; and that special efforts should be made in the planning and design of mass transit facilities and services to that its availability to the elderly and handicapped services will be assured.\textsuperscript{21} Of federal money appropriated for mass transit, 3.5 percent may be designated to benefit access for the elderly and handicapped.\textsuperscript{22} The National Mass Transportation Assistance Act of 1974 assured that fares for the elderly and handicapped not exceed half the general rate for peak hours.\textsuperscript{23}

But in the ensuing years, handicapped plaintiffs were unsuccessful in arguing that they had a fundamental right to public transportation which requires transit authorities to purchase buses accessible to wheelchairs.\textsuperscript{24} In 1976, section 165 was added to the Federal-Aid Highway Act of 1973 authorizing the Secretary of Transportation to require that a mass transit system, aided by grants from highway funds "be planned, designed, constructed, and operated to allow effective utilization by elderly or handicapped persons."\textsuperscript{25}

Section 504 of the Rehabilitation act of 1973, commonly known as the civil rights bill of the disabled, provides that

No otherwise qualified individual with handicaps in the United States . . . shall, solely by reason of her or his handicap, be excluded from the participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance.\textsuperscript{26}

\textsuperscript{19} 134 CONG. REC. S5106, S5115 (daily ed. April 28, 1988) (statement of Sen. Simon). The 1980 census revealed that 20\% of our citizens have a disability. Even the number with severe disabilities constitutes a sizable minority. Six million Americans have mobility problems sufficiently severe to require a mobility aid such as a wheelchair, a walker, crutches, or a prosthesis.

\textsuperscript{20} Rethinking Equality, supra note 7, at 864.

\textsuperscript{21} 49 U.S.C. § 1612(a) (1982).


\textsuperscript{23} Id. at 327.

\textsuperscript{24} Id. at 328.


\textsuperscript{26} 29 U.S.C. § 794(a) (1973).
Acting under this bill and section 16 of the Urban Mass Transportation Act, the Urban Mass Transit Administration [UMTA] (a DOT subsidiary) adopted regulations in 1976 which required local transit agencies receiving federal funds to make "special efforts" to accommodate the needs of the disabled, but largely left to the local agencies the responsibility to determine how to implement these requirements. Many devoted resources to purchasing new buses with wheelchair lifts. Others, finding that alternative too costly, provided paratransit or "dial-a-ride" services, whereby a van would be dispatched to pick up the handicapped and take them to their destinations.

In 1978, the U.S. Department of Health Education and Welfare issued guidelines which required that federally funded programs be accessible, as a whole, to the disabled, essentially requiring them to "mainstream" the handicapped. The guidelines specifically required retrofitting of subways and buses to make them fully accessible to the handicapped. But HEW acknowledged that its guidelines did not "preclude in all circumstances the provision of specialized services as a substitute for, or supplement to, totally accessible services."

In response, UMTA promulgated new rules in 1979 which adopted an equal access, embracing the assumption that mass transit should be available both to people with disabilities and those free from them. This required that all new fixed route buses be made accessible to the handicapped (including those confined to wheelchairs), and that rail transit facilities be retrofitted for accessibility. One half of peak-hour buses would have to be accessible within three years (ten years for modification

27. Rethinking Equality, supra note 7, at 873; 55 Fed. Reg. 40,762 (1990); Economic Policy, supra note 22, at 329-30. Three examples of satisfactory "special efforts" with respect to people using wheelchairs are: (1) spending a minimum proportion of federal aid on wheelchair accessible service, (2) buying only wheelchair accessible buses until one-half of the vehicles in the system were accessible, or providing a comparable substitute service for wheelchair users, (3) establishing a system of individual subsidies so that every wheelchair user could purchase ten round trips per week from any accessible service at prices equal to "regular fares."


29. 45 C.F.R. §§ 85.57(b), 85.58 (1978).


31. Rethinking Equality, supra note 7, at 873. The DOT made this change in adopting an equal access approach in the new rules in response to rules issued in 1978 by the Department of Health, Education, and Welfare (HEW), which had authority to coordinate other agencies' implementation of section 504. The HEW guidelines required federal funded programs to be accessible, as a whole, to people with disabilities. Following HEW's guidelines, DOT's 1979 rules required all new fixed route buses to be accessible to people with disabilities, including those using wheelchairs. Within three years, or ten years for modifying existing vehicles or facilities or making expensive structural changes, transit systems had to make at least one half of peak-hour bus service accessible.

of existing vehicles or facilities requiring extensive structural changes).\textsuperscript{33} A waiver provision existed for commuter rail, subway and streetcar systems.\textsuperscript{34}

These rules were struck down in 1981 as beyond the scope of DOT's authority because of their requirement of extensive structural changes which imposed undue financial burdens on transit authorities.\textsuperscript{35} In response, DOT withdrew the challenged regulations, and substituted interim rules similar to the "special efforts" regulations it had adopted in 1977.\textsuperscript{36}

Congress responded by promulgating the Surface Transportation Assistance Act of 1982\textsuperscript{37} which required that DOT issue a new rule identifying minimum service criteria for the disabled. The legislation did not, however, require equal access or comparable service for the handicapped.\textsuperscript{38}

DOT issued final rules in 1986 which gave local transit agencies the option of (1) requiring installation of wheelchair lifts in buses, (2) establishing a "special service" or paratransit system, or (3) establishing a mixed system of accessible buses and paratransit as an option for mak-

\textsuperscript{33} Rethinking Equality, supra note 7, at 873.
\textsuperscript{34} Economic Policy, supra note 22, at 330.
\textsuperscript{35} American Public Transit Ass'n v. Lewis, 655 F.2d 1272 (D.C. Cir. 1981); 55 Fed. Reg. 40,762 (1990); Economic Policy, supra note 22, at 331. American Public Transit Association v. Lewis held that a section of the rules governing specific requirements for mass transit was beyond the scope of DOT's authority under section 504 because it mandated expensive structural changes. The D.C. Circuit based its decision in this case on Southeastern Community College v. Davis, the U.S. Supreme Court's first decision interpreting section 504's substantive requirements. Davis upheld a nursing program's rejection of an applicant with impaired hearing, holding that section 504 does not require substantial modifications of programs to accommodate people with disabilities. The Court did not define "substantial modification," but held that section 504 does not require a fundamental alteration in the nature of a program, such as eliminating clinical courses for a nursing student.
\textsuperscript{36} Rethinking Equality, supra note 7, at 875. Believing that these rules would not result in sufficient access, Congress promulgated a statute requiring DOT promptly to issue final rules that would establish clear minimum standards for accessible transportation service. Before DOT issued these final rules, the U.S. Supreme Court again considered the extent of accommodations required by section 504. In Alexander v. Choate, 469 U.S. 287 (1985), the Court refused to limit section 504 to a simple equal treatment, but left unanswered questions about when section 504 would forbid unequal effects. The Court assumed that section 504 may in some situations require accommodations to eliminate disparate impacts. The Court assumed that section 504 may in some situations require accommodations to eliminate disparate impacts. The Court concluded that policies with harmful effects on people with disabilities may be lawful if "meaningful and equal access" still exists. The Court feared that "because the handicapped typically are not similarly situated to the nonhandicapped," the disparate impact approach in some situations could lead to "a wholly unwieldy administrative and adjudicative burden."
\textsuperscript{37} 49 U.S.C. §§ 1601, 1612(d). The statute added section 1612(d) to the Urban Mass Transit Act.
\textsuperscript{38} 55 Fed. Reg. 40,762 (1990). The new section required the Department to issue a new rule containing minimum service criteria for service to disabled passengers.
The transit agencies shall meet these minimum service requirements as soon as reasonably feasible, as determined by UMTA, but in any case within six years of the initial determination by UMTA concerning the approval of its program. The rules establish minimum service requirements governing fares, area and time of service, restrictions on eligibility and trip purpose, and waiting periods. Under these rules, service for people with disabilities must generally be "comparable" to service for nondisabled people, but can still be somewhat inferior.

Service for the handicapped, although it could be segregated, would have to be "comparable." In order to avoid the "undue burdens" problems which had scuttled the 1977 rules, the 1986 rules also allowed a local transit agency to limit its expenditure on transportation for the handicapped to 3% of its annual operating budget, even if it failed to meet the rule's service criteria. Although holding that the DOT could take costs into account in formulating a rule, a federal court deemed this 3% "cost cap" arbitrary and capricious in 1988. Nevertheless, the DOT's decision not to implement mainstreaming, but to allow local transit authorities to use accessible buses, paratransit or mixed systems, was upheld as reasonable. Mainstreaming was not required under the legislation that then existed, for there was no right, legislative or constitutional, of equal access.

With two steps forward and one step back, progress was made, albeit gradually. The percentage of new bus purchases accessible to those in wheelchairs grew to more than 50% annually. By 1990, 35% of the nation's public transit buses were accessible to the disabled.

IV. AIR TRANSPORTATION

A. AIRLINES

Airlines were specifically excluded from the application of the ADA because Congress had already promulgated legislation, the Air Carrier

39. 51 Fed. Reg. 18,994 (1986). 49 C.F.R. § 27.95 (1987). Rethinking Equality, supra note 7, at 876. The transit agencies shall meet these minimum service requirements as soon as reasonably feasible, as determined by UMTA, but in any case within six years of the initial determination by UMTA concerning the approval of its program. The rules establish minimum service requirements governing fares, area and time of service, restrictions on eligibility and trip purpose, and waiting periods. Under these rules, service for people with disabilities must generally be "comparable" to service for nondisabled people, but can still be somewhat inferior.

40. 49 C.F.R. § 27.95 (1987).

41. Rethinking Equality, supra note 7, at 877. The DOT claims that this cost limit on required accommodations will prevent undue burdens that are beyond its authority of impose under section 504, particularly in light of APTA, while still requiring improved service for people with disabilities.


43. ADAPT, 881 F.2d at 1198.

44. Id.

Access Act of 1986 [ACAA]. to deal with the problem. The ACAA succinctly provides that "No air carrier may discriminate against any other­wise qualified handicapped individual, by reason of such handicap, in the provision of air transportation." The principal sponsor of the bill, Senator Robert Dole, said, "there should be no restrictions placed upon air travel by handicapped persons. Any restrictions that the procedures may impose must be only for safety reasons found necessary by the Federal Aviation Administration [FAA]."

Even before enactment of the Air Carrier Access Act, in 1982 the now defunct Civil Aeronautics Board, acting under the authority of section 504 of the Rehabilitation Act of 1973 (discussed above) and sections 404(a) and 404(b) of the Federal Aviation Act of 1958 (which require safe and adequate transportation and prohibited unjust discrimination in trans­portation, respectively), promulgated regulations attempting to prohibit discrimination in the airlines.

In 1990, the DOT (which took the jurisdictional reins from the CAB upon it demise in 1985), promulgated regulations which required that new aircraft (of thirty seats or more) purchased by domestic airlines be equipped with folding armrests on half the aisles. Widebodied aircraft must have lavatories accessible to the handicapped. Planes with 100 or more seats must have priority space for storing a wheelchair in the cabin. In fact, wheelchairs and other handicap assistance devices (such as canes or crutches) have priority for in-cabin and baggage compartments over other passengers' baggage. Airlines also cannot prohibit the handicapped from bringing their personal ventilators and respirators as well as non-spillable batteries and seeing-eye dogs aboard the aircraft. Planes with sixty or more seats with an accessible lavatory must also have an on-board wheelchair in the cabin. Retrofitting existing aircraft is not required, unless the airline replaces the cabin interior or lavatories.

49. 14 C.F.R. § 382 (1990). A U.S. Supreme Court decision, Department of Transportation v. Paralyzed Veterans of America, 477 U.S. 597 (1986), held that non-subsidized airlines did not receive Federal financial assistance and were therefore not covered by section 504 of the Rehabilitation Act of 1973. This case served as the catalyst for the Air Carrier Access Act of 1986.
50. 55 Fed. Reg. 8048 (1990) (to be codified at 14 C.F.R. § 382.21(a)(1)).
51. ld. at § 382.21(a)(3).
52. ld. at § 382.21(a)(2).
54. ld. at §§ 382.39(b), 382.55(a).
55. 55 Fed. Reg. 8048 (1990) (to be codified at 14 C.F.R. § 382.21(a)(4)).
56. ld. at § 382.21(b)(1), (c). However, an on-board wheelchair must be available within two years. ld. § 382.21(b)(2).
As to the practices of airlines, no airline can refuse transportation to an individual based on his or her handicap unless allowing the person on the plane would be inimical to the safety of the flight. If the carrier excludes a passenger on such grounds, it must provide him with a written explanation. The airline may, however, exclude or require a medical certificate from those with a communicable disease determined by federal authorities to be likely to be spread to other passengers. It may also require a medical certificate from those traveling in stretchers, those needing medical oxygen or those whose condition raises a reasonable doubt whether they can complete the flight safely.

Airlines may not require advance notice that a handicapped person will be traveling, although they may require up to forty-eight hours notice in circumstances where certain preparations need to be made to accommodate the handicapped passenger. Airlines may not charge handicapped people for the amenities required by DOT regulations.

However, the airline may require that an attendant accompany a person traveling in a stretcher or incubator, or who because of a mental disability, is unable to comprehend or respond to safety instructions, or who has a mobility impairment so severe that he is unable to evacuate the aircraft, or who has such severe vision and hearing impairments that he is unable to communicate with airline personnel. But if the handicapped person disagrees with the airline as to the necessity of an attendant, the airline shall not charge for the transportation of the attendant.

57. 55 Fed. Reg. 8049 (1990) (to be codified at 14 C.F.R. § 382.31). This is consistent with Adamsons v. American Airlines, 58 N.Y.2d 42, 444 N.E.2d 21 (1982), in which the court upheld the airline’s refusal to board a passenger paralyzed from the waist down who was crying from the severe pain and was using a catheter and disposal bag. Under 49 U.S.C. § 1511, the airline lawfully excluded the passenger on grounds that such transportation would be inimical to the safety of the flight. An airline specifically may not limit the number of seats dedicated to a handicapped person “solely because the person’s handicap results in appearance or involuntary behavior that may offend, annoy, or inconvenience crew members or other passengers.” 55 Fed. Reg. 8,049 (1990) (to be codified at 14 C.F.R. § 382.31(b)).

58. Id. at § 382.31(e).

59. 55 Fed. Reg. 8052 (1990) (to be codified at 14 C.F.R. § 382.51(b)).

60. Id. at § 382.53(b). In the medical certificate, the physician must specify that the passenger is capable of completing a flight safely, “without requiring extraordinary medical assistance during the flight.” Id.

61. 55 Fed. Reg. 8049 (1990) (to be codified at 14 C.F.R. § 382.33). Among the special services for which advance notification may be required are medical oxygen, an incubator, an electrical hook-up for a respirator, a stretcher, an electrical wheelchair (on a plane seating fewer than 60 passengers), hazardous material packaging for a battery, ten or more handicapped passengers traveling as a group, and an on-board wheelchair on an aircraft that does not have an accessible lavatory. Id. at § 382.33(b).


63. 55 Fed. Reg. 8029 (1990) (to be codified at 14 C.F.R. § 382.35(b)).

64. Id. at § 382.35(c).
Airlines which operate aircraft of more than 19 seats are obliged to train their personnel in the requirements of the DOT regulations regarding the handicapped. Airline employees must provide the handicapped with assistance in enplaning and deplaning, and in making flight connections and providing transportation between gates. The airlines must also make special accommodations for passengers with hearing impairments, including providing a telecommunications device for the deaf, without imposing additional charges for the service.

Carriers may place only able bodied persons capable of performing functions necessary for an emergency evacuation in exit rows. Airline employees need not carry a handicapped person on a small plane (carrying fewer than 30 passengers) for which a lift or other device is unavailable. However, once in the aircraft, the handicapped passenger is entitled to special assistance, including help in moving between seats in enplaning and deplaning, preparation for eating, use of the on-board wheelchair, moving to the lavatory, and loading and retrieving carry-on items.

The airlines must make a complaints resolution official available at each airport they serve to receive and resolve complaints of violations of the DOT rules. DOT anticipates that the cost to the airline industry of compliance for its regulations, including accessible lavatories, on-board wheelchairs, moveable armrests and training is approximately $400 million, or about ten cents a ticket.

B. AIRPORTS

Discrimination in airports was implicitly addressed by Congress in the Rehabilitation Act of 1973 (discussed above) and the Rehabilitation,

| 66. | 55 Fed. Reg. 8050 (1990) (to be codified at 14 C.F.R. § 382.39(a)). Airlines must provide the handicapped with ground wheelchairs at the airport, and may not leave a handicapped passenger in a wheelchair unattended for more than 30 minutes. Id. at §§ 382.39(a)(1), (3). |
| 68. | 14 C.F.R. §§ 121, 135 (1990). This requirement is consistent with Anderson v. USAir, 619 F. Supp. 1191 (D.D.C. 1985), aff’d on other grounds, 818 F.2d 49 (D.C. Cir. 1987), which held that an airline could lawfully evict a blind passenger from an exit row. |
| 70. | Id. at § 382.39(b). However, the airline is not obliged to assist the handicapped passenger in actual eating, or assist him in the restroom, or provide medical services. Id. at § 382.39(c). |
Comprehensive Services, and Developmental Disabilities Act of 1978, which prohibit discrimination in any program or activity receiving federal financial assistance.\footnote{73. 29 U.S.C. § 794(a) (1988).} In promulgating regulations thereunder, the DOT prohibited discrimination against the handicapped in most airports, except those served by smaller aircraft.\footnote{74. Airports subject to the regulations include those served by airlines flying aircraft seating more than 55 people or having a cargo payload of more than 18,000 pounds. But if federal funds are made available for the airport's terminal facilities, they are subject to the rules anyway. 49 C.F.R. § 27.5 (1990).}

Essentially, the regulations require equality of treatment for qualified handicapped people in terms of employment, access, or utilization of airports.\footnote{75. 49 C.F.R. § 27.7 (1990).} Structural changes in facilities necessary to permit access by the handicapped were required.\footnote{76. 49 C.F.R. § 27.65 (1990).} Specifically, airport terminals “shall permit efficient entrance and movement of handicapped persons while at the same time giving consideration to their convenience, comfort, and safety.”\footnote{77. 49 C.F.R. § 27.71 (a)(2)(i) (1990). The basic terminal design shall permit efficient entrance and movement of handicapped persons while at the same time giving consideration to their convenience, comfort, and safety. It is also essential that the design, especially concerning the location of elevators, escalators, and similar devices, minimize any extra distance that wheelchair users must travel compared to nonhandicapped persons, to reach ticket counters, waiting areas, baggage handling areas, and boarding locations. 49 C.F.R. § 27.71 (1990).} Ticketing, baggage check-in and retrieval, boarding, telephones, teletypewriters, vehicular loading and unloading, parking, waiting areas, airport terminal information, and other public services (e.g., drinking fountains and rest rooms) all must be made accessible to the handicapped.\footnote{78. 49 C.F.R. § 27.71 (1990).} Many of these requirements have also been imposed upon airlines which own, lease or operate airport terminal facilities.\footnote{79. 55 Fed. Reg. 8023 (1990) (to be codified at 14 C.F.R. § 382.23).}

V. SURFACE TRANSPORTATION

A. THE DISABLED

The Americans with Disabilities Act of 1990 begins with a Congressional finding that 43 million Americans “have one or more physical or mental disabilities.”\footnote{80. A.D.A., supra note 18, at § 2(a).} This is quite a remarkable number of people. Nearly one in five of all Americans, according to Congress, are disabled. The ADA defines a disability as any physical or mental impairment that “substantially limits a major life activity.”\footnote{81. Will Disabilities Law Produce Litigation, NAT’L L.J., Aug. 13, 1990, at 3.}
1973\textsuperscript{82} have construed the term "handicapped" as including transsexuals and compulsive gamblers, the ADA specifically excludes them.\textsuperscript{83} In fact the act excludes a number of categories of human condition, including those afflicted with "homosexuality or bisexuality; transvestism, transsexualism, or other sexual disorders; compulsive gambling, kleptomania, or pyromania; or psychoactive substantive use disorders resulting from current use of illegal drugs."\textsuperscript{84} As to drugs, the ADA allows an employer to prohibit the illegal use of drugs and alcohol in the workplace.\textsuperscript{85}

The DOT regulations define a disability as a "permanent or temporary physical or mental impairment that substantially limits one or more major life functions . . . .\textsuperscript{86} A physical or mental impairment is defined to include the following:

(1) Any physiological disorder or condition, cosmetic disfigurement, or anatomical loss affecting one or more of the following body systems: neurological, musculoskeletal, special sense organs, respiratory including speech organs, cardiovascular, reproductive, digestive, genito-urinary, hemic and lymphatic, skin or endocrine; or

(2) Any mental or psychological disorder, such as mental retardation, organic brain syndrome, emotional or mental illness, and specific learning disabilities. The term "physical or mental impairment" includes, but is not limited to such diseases and conditions as orthopedic, visual, speech, and hearing impairments, cerebral palsy, epilepsy, muscular dystrophy, multiple sclerosis, cancer, heart disease, diabetes, mental retardation, emotional illness, drug addiction (but not including the current use of illegal drugs) and alcoholism. "Major life activities" means functions such as caring for one's self, performing manual tasks, walking, seeing, hearing, speaking, breathing, learning, and working . . . .\textsuperscript{87}

Both the Senate and House of Representatives Committee Reports on the ADA specify that the new legislation covers persons with AIDS or the HIV-Virus.


\textsuperscript{85} W. Kenworthy, Legislative Update (address before the Transportation Law Institute, Washington, D.C., November 5, 1990), at 12 [hereinafter Legislative Update].

\textsuperscript{86} 49 C.F.R. § 37.5 (1990).

\textsuperscript{87} 49 C.F.R. § 37.5(a) (1990).
The ADA affects transportation firms both as employers (as are all employers) and as providers of transportation services. Transportation firms would be well advised to specify the physical characteristics which require able bodied employees for safety reasons in the job descriptions therefore. But it is the requirements of transportation companies as providers of transport services with which the instant discussion is focused.

The ADA divides transportation firms into two categories: public and private. Let us first examine the ADA's requirements with respect to public transport.

B. DISCRIMINATION BY PUBLIC ENTITIES

The ADA provides that "no qualified individual with a disability shall, by reason of such disability, be excluded from participation in or be denied the benefits of the services, programs, or activities of a public entity, or be subjected to discrimination by any such entity." A public entity is defined to include a state or local government or its agencies (meaning essentially public, and mostly urban, bus and rail transit systems) and Amtrak. Both public school transport and aviation are excluded from the definition of public transportation, in the latter case because the Air Carrier Access Act (discussed above) prohibits discrimination in air travel.

The ADA requires that new vehicles (e.g., buses and light and rapid rail cars) purchased and new facilities constructed by these entities which operate fixed route systems must be accessible to the disabled, including those who use wheelchairs. New public buses and rail cars must be fitted with lifts or ramps and fold-up seats or secured spaces in order to accommodate wheelchairs. Public entities must also plan for and implement paratransit service for those unable to use the normal fixed route system.

89. Legislative Update, supra note 85, at 10.
91. Id. at § 201(1).
92. Id. at § 221(2). The term "designated public transportation" means transportation (other than public school transportation) by bus, rail, or any other conveyance (other than transportation by aircraft or intercity or commuter rail transportation (as defined in section 241)) that provides the general public with general or special service (including charter service) on a regular and continuing basis.
94. Overview, supra note 5, at 931.
95. Legislative Update, supra note 85, at 10.
The 500 existing intercity rail (Amtrak) stations shall be made accessible to the disabled in not less than 20 years.96 In remodeling existing facilities, those areas renovated must be accessible to the handicapped.97 Transit authorities have three years in which to insure their key rapid and light rail stations are accessible to the handicapped, unless structural changes are extraordinarily expensive, in which case they may receive extensions up to 20 years.98 They also have five years to provide at least one commuter, light or rapid rail car per train which is accessible to the disabled, unless it would significantly alter the historical character of the vehicle.99

In buying or leasing used vehicles, public entities must also make a good faith effort to find used vehicles accessible to the disabled.100 Vehicles remanufactured to extend their life for five years or more (or ten years, in the case of rail cars) shall, "to the maximum extent feasible," be made accessible to the disabled.101 Exceptions are again made for historical vehicles.102 The House Report states that "remanufactured vehicles need only be modified to make them accessible to the extent that the modifications do not affect the structural integrity of the vehicle in a significant way."103

The ADA also requires that public entities providing fixed route systems operate nondiscriminatory paratransit services, comparable in both the level of service and response time, as are provided individuals without disabilities, unless such services would impose an undue financial burden on the public entity.104

The rules promulgated by DOT to implement the ADA prohibit discrimination by public and private entities against individuals with disabilities. They forbid denial of the opportunity to use the transportation system if the person is capable of using it. They require that vehicles and equipment be capable of accommodating all users, and that personnel be trained and supervised so that they "treat individuals with disabilities who use the service in a courteous and respectful way."105

The new rules also delete the 3% "cost cap," discussed above.106

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96. See, A.D.A., supra note 18, at § 242(e).
97. Id. at § 227(a).
98. Id. at §§ 227(b), 242(e).
99. Id. at §§ 228(b), 242(a), 242(b).
100. Id. at §§ 222(b), 242(c).
101. Id. at §§ 222(c)(1), 242(d).
102. Id. at § 222(c)(2).
104. A.D.A., supra note 18, at § 223. Overview, supra note 5, at 931.
105. 49 C.F.R. § 37.7 (1990).
106. 55 Fed. Reg. 40,762 (1990). This new final rule deletes the three percent "cost cap," the provision of the rule which the courts invalidated. The effect of this amendment will be to
Compliance with the regulations is a condition of receiving federal financial assistance from DOT. The rules also make clear that any private entity which contracts with public entities for the provision of public transit, "stands in the shoes of the public entity for purposes of determining the application of ADA requirements." The rules also allow a temporary waiver for the purchase of new lift-equipped buses if they are unavailable, provided several conditions are met. In buying or leasing used vehicles, the ADA requires that transit authorities make a demonstrated good faith effort to find vehicles which are accessible to the handicapped. Under the DOT rules, this requires that the public entity specify accessibility in bid solicitations, conduct a nationwide search, advertise in trade periodicals, and contact trade associations. However, unlike the new vehicle rules, no formal waiver need be requested from DOT.

In remanufacturing used vehicles to extend their life for five years or more, the ADA requires they be made accessible to the handicapped. While they need not be modified in a way which adversely affects their structural integrity, the cost of modification is not a legitimate consideration.

Historical vehicles need not be made accessible if they operate on a require any UMTA recipient electing to meet its part 27 obligations through a special service system to meet all service criteria.

109. 55 Fed. Reg. 40,770 (1990); 49 C.F.R. §§ 37.21(b)-(g) (1990). The definition of "operates" in the ADA makes it clear that a private entity which contracts with a public entity stands in the shoes of the public entity for purposes of determining the application of ADA requirements.
110. 55 Fed. Reg. 40,771 (1990); 49 C.F.R. § 37.23 (1990). The purpose of the waiver provision in the ADA, as the Department construes it, is to address a situation in which, because of a potentially sudden increase in demand for lifts, lift manufacturers are unable to produce enough units to meet the demand in a timely fashion. This is, as the title of the ADA provision involved suggests, a temporary situation calling for "temporary relief." A waiver should allow a transit provider meeting the statutory standards to being vehicles into service without lifts. But there is not reason related to the purpose of this provision of the ADA why the vehicle should remain inaccessible throughout its life. A lift should be installed as soon as it becomes available.
112. 55 Fed. Reg. 40,772 (1990); 49 C.F.R. § 37.25 (1990). The House Committee on Transportation and Public Works reports uses the language: "remanufactured vehicles need only be modified to make them accessible to the extent that the modifications do not effect the structural integrity of the vehicle in a significant way." Based on these statements and on the comments to the NPRM, the final rule provides that it is considered feasible to remanufacture a vehicle to be accessible, unless an engineering analysis indicates that specified accessibility features would have a significant adverse effect on the structural integrity of the vehicle. That it may not be economically advantageous to remanufacture a bus with accessibility modifications does not mean it is unfeasible to do so, in the engineering sense which Congress intended. Accordingly, the rule does not include economic factors among those which may be considered in determining feasibility.
fixed route which is on the National Register of Historic Places, and making the vehicle accessible would significantly alter its historic character.\textsuperscript{113} Thus, the San Francisco cable cars and the New Orleans streetcar named Desire need not be modified for wheelchair access, even if they are rehabilitated to extend their life for five years.

The rules governing acquisition of new, used and remanufactured rapid and light rail vehicles parallel those for the purchase of buses and vans, except that the remanufacturing trigger for modification of intercity and commuter rail vehicles is for extension of its life for ten (as opposed to five) years.\textsuperscript{114}

Some small cities and rural communities provide demand-responsive systems. In general, such transit authorities must purchase accessible new equipment.\textsuperscript{115} But they need not if their systems, when viewed in their entirety, provide equivalent levels of service both to the handicapped and to those without handicaps.\textsuperscript{116} Thus, the delays from the moment service is requested to the time it is provided must be equivalent for handicapped and non-handicapped passengers.\textsuperscript{117}

\textbf{C. DISCRIMINATION BY PRIVATE ENTITIES}

The ADA includes a blanket antidiscrimination provision: "No individual shall be discriminated against on the basis of disability in the full and equal enjoyment of the goods, services, facilities, privileges, advantages, or accommodations of any place of public accommodation . . . ."\textsuperscript{118} A "public accommodation" is defined to include "a terminal, depot, or other station used for specified public transportation . . . ."\textsuperscript{119} Included among the prescribed conduct is denial of the opportunity, unequal, different or separate opportunity "to participate in or benefit from the goods, services, facilities, privileges, or accommodation . . . ."\textsuperscript{120}

Among the specific prohibitions of the ADA are: "a failure to remove architectural barriers, and communication barriers that are structural in nature, in existing facilities, and transportation barriers in existing vehicles and rail passenger cars used by an establishment for transporting individuals (not including barriers that can only be removed through the retrofit-

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\textsuperscript{115} A.D.A., supra note 18, at § 224.
\textsuperscript{117} Fed. Reg. 40,773 (1990); see, 49 C.F.R. § 37.7(f) (1990). For example, the time delay between a phone call to access the demand responsive system and pick up the individual is not to be greater because the individual needs a lift or ramp or other accommodation to access the vehicle.
\textsuperscript{118} A.D.A., supra note 18, at § 302(a).
\textsuperscript{119} id. at § 301(7).
\textsuperscript{120} id. at § 302(b).
\end{flushleft}
ting of vehicles or rail passenger cars by the installation of a hydraulic or other lift), where such removal is readily achievable."121

What is readily achievable? The ADA defines it as "easily accomplishable and able to be carried out without much difficulty or expense," taking into account the nature and cost of the change and the overall financial resources of the enterprise. Thus, the legislation requires some retrofitting to be accomplished immediately.122

Changes in physical structure, design layout and equipment in existing buildings must be made only if they are reasonable accommodations designed to satisfy the needs of disabled job applicants and employees. However, any sections of the business open to customers or the general public must be made accessible if the cost is minor.

The ADA imposes more stringent accessibility requirements when a "commercial facility" is renovated or newly-built. These rules apply to all businesses, regardless of size. Major renovations of commercial facilities must, to the maximum extent feasible, be made accessible to the disabled.

The most stringent rules dealing with physical accessibility apply to the construction of new commercial facilities whose first occupancy occurs on or after January 26, 1993.123

Further, the ADA prohibits discrimination "on the basis of disability in the full and equal enjoyment of specified public transportation services provided by a private entity that is primarily engaged in the business of transporting people . . . ."124

Such enterprise may not purchase a new vehicle (other than an automobile or van seating fewer than eight passengers) which is not readily accessible to individuals with disabilities, unless it is used in a demand responsive system and such system provides service equivalent to that provided the general public.125 Thus, taxi cabs are exempt.

Similar requirements are imposed for the purchase of new rail cars, and the remanufacture of such cars so as to extend the life thereof for ten or more years.126 Certain historical or antiquated rail cars more than 30 years in age and whose manufacturer is no longer in the business are exempt.127

Private companies operating "fixed route systems" (operating vehicles along a prescribed route according to a fixed schedule), must

121. Id. at § 302(b)(2)(A)(iv).
122. Id. at § 301(9).
123. Major Changes, supra note 11, at 15-16.
124. A.D.A., supra note 18, at § 304(a).
125. Id. at § 304(b)(3).
126. Id. at § 304(b) (6)-(7).
127. Id. at § 304(c).
purchase or lease new vehicles (seating 16 passengers or more) which are accessible to individuals with disabilities, including those using wheelchairs.\textsuperscript{128} If they do purchase a vehicle inaccessible to the handicapped, it shall be considered discrimination for them to fail to operate their systems so that, when viewed in their entirety, the system provides a level of service to individuals with disabilities which is equivalent to the level of service provided to those without disabilities.\textsuperscript{129}

However, retail and service businesses which are not in the principal business of transporting people, but do offer transportation, must also comply with several provisions of the ADA. Examples of such organizations are hotels and motels that offer airport pick-up services.

In purchasing new vehicles seating more than 16 people, private entities not primarily engaged in transportation (e.g., airport shuttles operated by hotels, rent-a-car companies, or ski resorts) must acquire vehicles accessible to the handicapped, including those in wheelchairs, unless the system, when viewed in their entirety, provide equivalent service to the handicapped and non-handicapped.\textsuperscript{130} Thus, a firm need not equip all of its vehicles with wheelchair lifts if its system will accommodate them adequately as a whole.

Finally, the U.S. Office of Technology Assessment is commissioned by the ADA to undertake a three year study of the most cost-effective means of achieving access in over-the-road buses (Greyhound-type buses with an elevated passenger deck over a baggage compartment), and to recommend legislation.\textsuperscript{131} Within a year after the study is completed, DOT shall promulgate regulations identifying how over-the-road buses shall comply with the ADA.\textsuperscript{132} Compliance is targeted for seven years for small providers and six years for others.\textsuperscript{133} In the interim, DOT may not require retrofitting—structural changes to existing over-the-road buses—in order to obtain access for the disabled.\textsuperscript{134} Such regulations also shall not require installation of accessible restrooms in the buses if that would result in a loss of seating capacity.\textsuperscript{135}

\textbf{D. REGULATORY IMPLEMENTATION}

The ADA requires the Architectural and Transportation Barriers Com-

\textsuperscript{128} 42 U.S.C. § 12181(4).
\textsuperscript{129} 42 U.S.C. § 12181(b)(2)(B)(i).
\textsuperscript{130} A.D.A., supra note 18, at §§ 302(b)(2)(B) & (D); 55 Fed. Reg. 40,774 (1990); 49 C.F.R. § 37.29 (1990).
\textsuperscript{131} A.D.A., supra note 18, at § 305.
\textsuperscript{132} Id. at § 306(a)(2)(B).
\textsuperscript{134} Id.
\textsuperscript{135} A.D.A., supra note 18, at § 306(a)(2)(C).
pliance Board to supplement its Minimum Guidelines and Requirements for Accessible Design by April 26, 1991, to insure that public buildings, facilities and vehicles covered by the act are accessible in terms of architecture, design and transportation to the disabled.\(^{136}\) The DOT must issue regulations to implement the public and private transportation provisions by July 26, 1991 (several of these have been issued, and are discussed above). The Department of Justice must issue its regulations by then as well.\(^{137}\)

### E. UNRESOLVED ISSUES

Several issues remain unresolved as of the date of this writing. One is, how shall a blind person be accommodated in bus service since he can neither read the destination on the front of the bus, nor see his destination when he arrives at it? The blind could be issued color coded cards to signal the driver of their destination, and the driver could call out each stop as he arrives at it.\(^{138}\) Another is, how should transit authorities deal with access by non-traditional mobility devices, such as three-wheel scooters, some of which are excessively heavy (600-700 pounds) for some lifts?\(^{139}\) Still another is whether it is discriminatory to require securement for mobility device users while other users are not secured?\(^{140}\) The resolution of these issues was left for another day.

### F. REMEDIES

The ADA also provides the remedies available under section 505 of the Rehabilitation Act of 1973 (which incorporates those available under Title VII of the Civil Rights Act, including back pay, damages, attorney's fees and injunctions).\(^{141}\)

It gives the disabled the remedies and procedures already available under Title VII of the Civil Rights Act of 1964 to those suffering racial discrimination.\(^{142}\) Title VII outlaws discrimination based upon race, color, religion, sex or national origin. Job applicants or employees can file complaints with the Equal Employment Opportunity Commission (EEOC),

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\(^{136}\) Id. at § 504. See also, 29 U.S.C. § 792 (1986).


\(^{139}\) 55 Fed. Reg. 40,767-68 (1990). A number of transit authorities either refuse to carry scooters and other non-standard devices or carry scooters and other non-standard devices or carry the devices but require the passenger to transfer out of his or her own device to a vehicle seat. This latter requirement typically is imposed when the transit provider believes it can successfully secure the mobility device but not the passenger while sitting in the device.


which can investigate and file charges. If the EEOC does not file charges, the individual who complained is permitted to file a lawsuit. Back pay, reinstatement, court-ordered accommodations and attorneys’ fees may be granted. Thus, violations of the physical accessibility rules may be handled by EEOC complaint, private lawsuit, or action by the U.S. Attorney General. 143

One question raised at the time the ADA was passed was whether Title VII would be expanded to include jury trials and punitive damages as proposed under the then-pending civil rights bill before Congress. 144 The issue became moot for the time being, as President Bush vetoed the civil rights legislation.

Injunctive relief is also available. 145 Moreover, the U.S. Attorney General is obligated to investigate alleged violations of the ADA. 146 A court may assess civil penalties up to $50,000 for the first violation, and up to $100,000 for any subsequent violation, plus damages. 147 However, punitive damages are specifically excluded. 148

VI. CONCLUSION

One criticism of the new legislation was that neither Congress nor the Administration made a responsible effort to determine the public or private costs of compliance. 149 Many businesses lobbied against the ADA, arguing that it would be expensive.

Some maintained that the new legislation would foster another "lawyer cottage industry." One attorney acknowledged the possibility of a "nuclear litigation explosion in the next decade. . . ." 150 Yet another hoped that the ADA would be implemented with a "minimum amount of litigation," but feared that "because it is such a sweeping law . . . there will be a substantial amount." 151 Another predicted that "without a battery of lawyers at their disposal, it will leave small employers playing a

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143. Major Changes, supra note 11, at 16.
144. Disabilities Law, supra note 1, at 3.
145. A.D.A., supra note 18, at § 308(a)(2). In the case of violations of section 302(b)(2)(A)(iv) and section 303(a), injunctive relief shall include an order to alter facilities to make such facilities readily accessible to and usable by individuals with disabilities to the extent required by this title. Where appropriate, injunctive relief shall also include requiring the provision of an auxiliary aid or service, modification of a policy, or provision of alternative methods, to the extent required by this title.
146. ld. at § 308(b)(1)(A).
147. ld. at § 308(b)(2)(B)-(C).
148. ld. at § 308(b)(4).
149. Every American, supra note 6, at 26.
150. Disabilities Law, supra note 1, at 3.
151. ld.
highstakes lawsuit. Among the potential areas for litigation in transportation is accident suits brought, for example, by those injured when bus lifts do not function properly, or when wheelchairs roll off them.

The bus industry also objected to the high cost of compliance imposed by the new legislation. For example, Greyhound argued that compliance would cost it $40 million a year, "a sum that dwarfs its 1989 profit of $8.5 million." Greyhound also alleged that the cost of each lift would be $35,000 per bus; others insisted that lifts could be purchased for less than $8,000.

With its very survival in question, Greyhound, which underwent a $350 million leveraged buy-out in 1986, purchased Trailways for $80 million in 1987, and suffered a strike in 1990, may be ill-equipped to endure even a modest additional financial burden. It is saddled with more than $340 million in long-term debt and has been unable to meet recent interest payments. Greyhound ordinarily serves approximately 9,500 of the 10,000 communities which receive bus service. In contrast, Amtrak serves 498 communities, and all airlines serve 477.

Not only Greyhound, but a number of bus companies are faced with a close-to-being unbearable squeeze on their profits. Even without a wheelchair lift, a new bus costs about $300,000. Handicapped access could increase new equipment costs by more than 10%. As one source noted, "Bus operators are concerned that the costs of compliance will be so high that bus passengers will have to pay higher fares and carrier profit margins will be further eroded."

The ravages of destructive competition unleashed by deregulation have already forced bus companies to discontinue service to more than 4,500 communities, leading to the isolation of large pockets rural

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152. Id.
154. Overview, supra note 5, at 932.
155. Id. As a result of the current confusion, the ADA provides that the Office of Technology Assessment must undertake a study to determine, inter alia, "the most cost effective methods for making over-the-road buses readily accessible to and usable by individuals with disabilities, particularly individuals in wheelchairs." The study, which is to include any policy options for legislative action," must be completed within three years of the enactment of the Act.
156. See Dempsey, Thoms & Clapp, Canadian Transport Liberalization: Planes, Trains, Trucks and Buses Rolling Across the Great White North, 19 TRANSP. L.J. 113 (1990) [hereinafter Planes, Trains].
158. Kahn, Stopping By the Bus Terminal on a Dark and Stormy Night: The U.S. Bus Industry Seven Years After Deregulation, 18 TRANSP. L.J. 255, 271 n. 48 (1990) [hereinafter Stormy Night].
159. Id. at 267.
160. Id.
161. Intercity Bus, supra note 157, at 363.
America. In 1977, the last year in which the U.S. Department of Commerce performed a travel survey, 30% of all intercity bus passenger miles were consumed by individuals living in rural areas, compared to trains (20%), and airlines (15%); families earning less than $10,000 a year accounted for 45% of intercity bus miles, compared to trains (25%), automobiles (18%), and airlines (15%); people under the age of 18 or over the age of 64 accounted for half of intercity bus passengers, compared to automobiles (33%), railroads (25%), and airlines (17%).

Access for the poor, the elderly, and the disabled means nothing if the bus no longer stops in your town. Congress needs to come to grips with the failure of deregulation and provide subsidies for small town service and handicapped access, or federalize the system into an "Ambus," like its successful sibling, Amtrak. Amtrak's cost of compliance will be largely paid by the federal government and the "one car per train" rule will significantly temper those costs.

Undoubtedly, users and taxpayers will pay the price of additional access for the disabled. This is particularly troublesome in light of the efforts of recent Administrations to phase out federal operating assistance for public transit driven by unwieldy budget deficits. Subway systems, in particular, are extremely expensive to construct. For example, it would have been cheaper to buy each Metro rider in the Washington, D.C. area two Mercedez Benzes than to have constructed the Metro subway system.

Higher fares will discourage ridership, exacerbating urban highway congestion and automobile pollution. One commentator objected to the cost of urban transit even before promulgation of the ADA, saying:

In the past Federal regulations have been enacted which would require all mass transit systems to retrofit their facilities and equipment to accommodate the handicapped. The costs of this policy are prohibitive (especially to older systems such as Chicago) and would benefit relatively few members of society. Many alternatives are available by which mass transit systems could provide the same, if not improved, services to the elderly and handicapped at a significantly lower cost. These include para-transit services, "dial-a-ride" services, and contractual agreements with private taxi companies.

Many public transit systems had adopted dial-a-ride systems for the

163. Planes, Trains, supra note 156, at 113.
disabled. In theory, such systems are not only cost-efficient, but they provide a superior level of service. If given the choice of standing at a cold, wet bus stop waiting for a crowded, late bus, only to transfer at another cold, wet stop to another crowded, late bus, or instead calling a van to pick you up at your home or apartment and deliver you to your destination, who wouldn't prefer the individualized service, whether one is handicapped or not?

Unfortunately, theory is not reality. In many cities paratransit and dial-a-ride services have a number of significant, and sometimes onerous, restrictions, such as a 24, 48 or 72 hour notification rule; priority given to medical and work trips (in that order); lengthy delays attributable to grouping pick-ups in order to reduce costs; and limitations on availability from 9:00 a.m. to 5:00 p.m. The cost of a truly demand-responsive system would be prohibitive.\footnote{167}

The ADA abhors "separate but equal" as almost a badge of slavery, preferring integration into the mainstream and equality for all. Senator Paul Simon summed up the benefits of the legislation by pointing out that, without it, the disabled suffer

continued unnecessary deprivation, isolation, and deterioration in the lives of millions of Americans. What will be the consequences if we enact this law? Strengthened communities, greater integration, lower medical and institutional costs, and a substantial increase in this country's productivity. Most importantly, we will be ensuring the opportunity for all Americans with disabilities to lead lives of independence, dignity, and full participation as citizens of this nation.

It is unconscionable to imagine an able work force languishing at home because there is no access to public transportation.

Today the technology exists to fashion the existing transit systems with appropriate light and seating to accommodate those who need it. Trains and buses, particularly newly purchased models, are easily equipped.\footnote{168} As new buses and trains are purchased they are equipped with lifts. The added costs are relatively small in comparison to the actual gains that are made through employment and more importantly through independence.

The U.S. government presently spends $57 billion each year on benefits for the disabled. That figure may be reduced if significant numbers of disabled Americans acquire access to employment.\footnote{169} Transportation is an important means to that end.

\footnote{167} Letter from Patricia Yeager to Paul Dempsey (Nov. 12, 1990).
\footnote{169} Every American, supra note 6, at 26.
Federal Preemption of State Laws Regulating For-Hire Motor Carriers Transporting Property (Including Baggage) as Part of an Intrastate Air/Truck Shipment*

ARCIE IZQUIERDO JORDAN
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In some states, a motor carrier may be required to obtain intrastate operating authority when it is transporting property (including baggage)1.

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1. For purposes of this paper, the focus is on intermodal movements of property, not passengers. While some references to passenger transportation do appear in the following discussion, an in-depth analysis of federal preemption relative to passenger movements has not been attempted.
subsequent to its movement by an air carrier, in intrastate commerce. Defending the integrity of their motor carrier regulation from further encroachment by the federal government, those states discern no federal preemption of state motor carrier regulation when the entire movement, including the air portion, occurs wholly within the boundaries of one state. They argue they are free to impose different forms of economic regulation on the involved motor carriers.\(^2\) There is little doubt, however, that economic regulation by the individual states is federally preempted under certain circumstances even in the context of wholly intrastate movements. Resting on the premise that motor vehicle service which is rendered under certain circumstances constitutes the service of an air carrier, not the independent service of a motor carrier, federal preemption reaches services rendered in connection with movements that do not cross a state’s boundary. The parameters within which such preemption occurs are the focus of this paper.

**Statutory Framework**

The preemption provision of the Federal Aviation Act (also referred to as the Airline Deregulation Act) contained in Section 1305(a) provides:

\(1\) Except as provided in paragraph \(2\) of this subsection, no State or political subdivision thereof and no interstate agency or other political agency of two or more States shall enact or enforce any law, rule, regulation, standard, or other provision having the force and effect of law relating to rates, routes, or services of any air carrier having authority under subchapter IV of this chapter to provide air transportation.\(^3\)

Application of this provision revolves around three criteria: (1) the nature of the air carrier involved; (2) the relationship between the state regulation and an air carrier’s rates, routes or services; and (3) the characterization of the activities which would be affected by the state regulation as “air carrier services.”

Section 10526(a)(8) of the Interstate Commerce Act\(^4\) exempts from the jurisdiction of the Interstate Commerce Commission (ICC) certain motor vehicle movements (i.e. motor carrier operations) which are performed in connection with air movements. Generally referred to as the “Incidental to Air” exemption, Section 10526(a)(3) provides in pertinent part:

\(a\) The Interstate Commerce Commission does not have jurisdiction under this chapter over...\(\ldots\)

\(8\)(B) transportation of property (including baggage) by motor vehicle as part of a continuous movement which, prior or subsequent to such part of the

\(^2\) An examination of each state’s regulatory scheme is beyond the scope of this paper.


continuous movement, has been or will be transported by an air carrier.\textsuperscript{5}

The pertinent legislative history of this provision, as well as decisions of the ICC and the federal and state judiciaries which have considered this statutory enactment and its predecessor,\textsuperscript{6} are helpful in determining the extent to which motor carrier services in the context of an intermodal air/truck movement should be viewed as air carrier services rather than the independent services of a motor carrier.

ARE WHOLLY INTRASTATE ACTIVITIES WITHIN THE SCOPE OF THE SECTION 1305 PREEMPTION?

Section 1305(a)(1) is not expressly limited to transportation which moves across a state boundary. The only limitations apparent from the express terms of the provision relate to the nature of the air carrier which must be involved and the nature of the activities which must be affected by the state regulation. With regard to the nature of the air carrier, Section 1305(a)(1) refers to an air carrier having authority under Subchapter IV [of the Federal Aviation Act] to provide air transportation. An examination of the Aviation Act's definitions of an air carrier\textsuperscript{7} and air transportation\textsuperscript{8} in conjunction with the licensing requirements of Section 1371 (Subchapter IV) demonstrate that Section 1305(a)(1) applies to any air carrier which undertakes to provide interstate, overseas or foreign air transportation and has either received authority from the Civil Aeronautics Board\textsuperscript{9} (CAB) or been exempted from certification requirements.\textsuperscript{10} By the plain language of the statute, Section 1305(a)(1) applies to any state law which relates to the rates, routes, or services of air carriers engaged in interstate commerce. It is not limited in application only to the interstate rates, routes, or services of an air carrier.\textsuperscript{11} Any doubts which might exist in this regard are dispelled upon examination of the legislative history of Section 1305.

The language of Section 1305(a)(1) was originally passed by the

\textsuperscript{5} ld. (emphasis added).
\textsuperscript{6} 49 U.S.C. § 1303(b)(7a).
\textsuperscript{7} 49 U.S.C. app. § 1301(3).
\textsuperscript{8} 49 U.S.C. app. § 1301(10).
\textsuperscript{9} All functions, powers, and duties of the Civil Aeronautics Board were terminated or transferred by Pub. L. No. 95-504, § 40(a), 92 Stat. 1744, (1978) effective on or before January 1, 1985. The function of issuing certificates of authority pursuant to §§ 1371(a)-(c) was transferred to the Department of Transportation. \textit{See} 49 U.S.C. §§ 1551(a), (b).
\textsuperscript{10} \textit{See} Hughes Air Corp. v. PUC of Calif., 644 F.2d 1334, 1337-1339 (9th Cir. 1981) holding that Congress intended to include carriers exempted from CAB certification pursuant to [49 U.S.C. § 1386(b)(1)] within the scope of the preemption provision.
\textsuperscript{11} \textit{See} Hughes at 1339-1341 holding, \textit{inter alia}, that Section 1305(a)(1) preempts state regulation of the intrastate services of CAB-certificated carriers.
House as an amendment to the Airline Deregulation Act of 1978.\textsuperscript{12} With a minor change relating to shipments between points in Alaska\textsuperscript{13}, which will be discussed below, the House version of the preemption provision survived the Conference Committee and was enacted as part of the Act in 1978.\textsuperscript{14}

Notably, the original preemption provision as proposed by the Senate would have allowed the individual states to continue regulating an interstate carrier as long as such carrier was generating at least fifty percent of its revenues from intrastate operations and the state had issued intrastate authority to such carrier prior to January 1, 1979.\textsuperscript{15} Further, it contemplated that as soon as such a carrier derived more than fifty percent of its revenues from its interstate operations, all of its operations would become subject to the CAB’s jurisdiction.\textsuperscript{16}

Rejecting the Senate’s scheme in this regard, the House Committee on Public Works and Transportation noted that:

\textbf{[E]xisting law contains no specific provision on the jurisdiction of the States and the Federal Government over airlines which provide both intrastate and interstate service.} The lack of specific provisions has created uncertainties and conflicts. . . . [Section 1305(a)(1)] will prevent conflicts and inconsistent regulations by providing that \textit{when a carrier operates under authority granted pursuant to title IV of the Federal Aviation Act, no State may regulate that carrier’s routes, rates or services}.\textsuperscript{17}

One area in which the uncertainties and conflicts arose due to such lack of specific provisions related to situations in which carriers had been required to charge different fares for passengers traveling between two cities depending on whether they were interstate or intrastate passengers.\textsuperscript{18} The Committee noted that an interstate carrier may carry intrastate passengers whose entire journey is between two cities in a single state and interstate passengers who are traveling between the same two cities in a single state then connecting to another airline to complete an out-of-state journey.\textsuperscript{19} Under the existing law, the Committee noted the interstate passengers fares would be regulated by the CAB while the intrastate fares would be regulated by a state.\textsuperscript{20} It was this dichotomy


\textsuperscript{13} Now contained in 49 U.S.C. app. § 1305(a)(2).

\textsuperscript{14} S. 2493, 95th Cong., 2d Sess. (1978).


\textsuperscript{16} \textit{id.}


\textsuperscript{18} \textit{id.}

\textsuperscript{19} \textit{id. at} 16 n.1.

\textsuperscript{20} \textit{id. at} 16.
which the House intended to eliminate by proposing its version of preemption.

The only amendment made by the Conference Committee to the House version of preemption related to certain transportation between points in Alaska. In the case of such transportation, the amendment limited federal preemption pursuant to Section 1305(a)(1) to air transportation provided under a Section 1371 certificate of public convenience and necessity.\footnote{21} Thus, in Alaska's case, the preemption is governed by the characterization of the transportation as regulated interstate traffic, as opposed to the focus in all other states which is the involvement of a carrier operating pursuant to authority under Subchapter IV of the Federal Aviation Act. The Conference Committee noted that the limitation on federal preemption in the case of Alaska was necessitated by the special circumstances present there with regard to cargo. It stated that "[d]ue to geographic and climatic conditions a great deal of cargo is shipped to and consolidated in southern points in Alaska and is subsequently distributed to points throughout the State. Where such shipments occur, the confer­ees intend that the subsequent shipments by air between points in Alaska be subject only to State economic regulation."\footnote{22} Obviously, there would have been no need to exempt from preemption intrastate transportation within the State of Alaska if the framers of the legislation had not intended that the preemption language of subparagraph (a)(1) would apply to operations conducted by an interstate air carrier wholly within a single state.\footnote{23}

Federal preemption under Section 1305(a)(1) in the context of wholly intrastate transportation by air has been recognized by some of the very states that presently seek to regulate the truck portion of intrastate air/truck movements. In 1981, the Texas legislature amended the Texas Aeronautics Act. The Texas Aeronautics Act, as amended, defines an air carrier as "every person owning, controlling, operating or managing any air craft as a common carrier in the transportation of persons or property for compensation or hire which conducts all or part of its operation in the State of Texas."\footnote{24} However, it excludes from the definition "air carriers carrying passengers or property as common carriers for compensation or hire in commerce between a place in [Texas] and a place outside

\footnote{21. See H.R. REP. No. 1779, 95th Cong., 2d Sess. 95, reprint ed in 1978 U.S. CODE CONG. & ADMIN. NEWS 3773, 3805 (emphasis added).}
\footnote{22. Id.}
\footnote{23. See also discussion of Section 1305(a)'s legislative history, in Trans World Airlines, Inc. v. Mattox, 897 F.2d 773, 780 (5th Cir. 1990), holding that Section 1305(a)(1) preempts state regulations of advertising activities conducted within the State of Texas by an interstate air carrier.}
Pursuant to these provisions, the Texas Aeronautics Commission considered regulating interstate air carriers with respect to their wholly intrastate services. Interpreting the language of the Texas Aeronautics Act for the Commission, the Attorney General of Texas noted that the precise purpose of the amendatory legislation was to "exempt air carriers who carried passengers or property for commercial compensation between Texas and a place outside of Texas." The Attorney General therefore opined that:

\[\text{[N]o provision of the Texas Aeronautics Act applies to entities carrying passengers or property as a common carrier for hire between any point in Texas and any point outside of the state. The statute . . . twice states that interstate carriers are beyond the reach of the Texas Aeronautics Act. . . .}\]

\[\text{[T]he statute is unambiguous. Any entity that at any time carries passengers or property as a common carrier for hire between a place in Texas and a place outside of Texas is not an "air carrier" as defined by the Act. It is not subject to any provision of the Act. . . .}\]

\[\text{[T]he Act does not reach entities offering interstate air service. They are outside of the jurisdiction of the [Texas Aeronautics] Commission even if they offer some service solely between points within Texas. The Commission has no jurisdiction over interstate carriers and has no authority to impose any burden on or extend benefits to them under the Texas Aeronautics Act.}\]

Federal preemption of state regulation of interstate carriers’ intrastate air transportation pursuant to Section 1305(a)(1) does not offend the tenth amendment. In Hughes Air Corp. v. PUC of California, the Ninth Circuit rejected the notion that air transportation regulation is such an integral and important aspect of state life that federal preemption of state regulation of intrastate air transportation would interfere with the state’s sovereignty guaranteed by the tenth amendment. Finding that "there is little difference between state regulation of air transportation and state regulation of railroad transportation", the Ninth Circuit concluded that Congress could (and did) preempt state regulation of the intrastate rates of air carriers encompassed by Section 1305(a)(1) (i.e. both carriers holding authority or exempted pursuant to Subchapter IV of the Federal Aviation Act). The court held that there was no conflict between such preemption and the tenth amendment of the Constitution because Congress had a rational basis for its legislation and the regulation of air transportation is not an integral governmental function.

Drawing on the parallel between air and rail regulation (or rather, deregulation) in recent years can be very instructive to our analysis here. In

25. Id.
28. 644 F.2d 1334 (9th Cir. 1981).
29. Id. at 1339-1341.
the area of rail regulation, federal preemption of state regulation of interstate rail carriers' intrastate activities has been scrutinized by the United States Supreme Court. In Interstate Commerce Commission v. Texas\(^\text{30}\), the Court determined the extent of the ICC's authority to exempt transportation that is provided by a rail carrier as a part of a continuous intermodal movement under 49 U.S.C. § 10505(f).\(^\text{31}\) The Court found that the ICC had authority to exempt from state regulation the motor freight portion of Plan II TOFC/COFC shipments, even though the intermodal shipment moved entirely within the State of Texas, when the rail carrier was an interstate rail carrier.\(^\text{32}\)

In ICC v. Texas, the State of Texas acknowledged that it had no power to regulate the intrastate truck portion of interstate intermodal rail/truck shipments. Texas asserted jurisdiction only in the case of wholly intrastate intermodal shipments conducted by interstate rail carriers in Plan II TOFC/COFC service. In support of its position, Texas argued that 49 U.S.C. § 10521(b)(1) preserved its jurisdiction to regulate the intrastate transportation provided by a motor carrier.\(^\text{33}\) The Court disagreed. It stated:

> Since all of the railroads . . . are engaged in interstate commerce, the [ICC] has authority over the intrastate transportation, as well as the interstate transportation, provided by such carriers. . . .

> [T]he State's interpretation of Section 10521(b)(1) would make that section authorize state regulation of TOFC/COFC services in areas where it has already been rejected. The term "intrastate transportation provided by a motor carrier" [in Section 10521(b)(1)] must refer either to the intrastate motor portion of any TOFC/COFC movement or to the entire intrastate movement when a portion of it is performed by truck service. If the term refers only to the motor portion, the State's reading of the statute would preserve the State's power to regulate the intrastate motor portion of an interstate Plan II TOFC/COFC shipment. But Texas acknowledges that it has no such power. Alternatively, if the term refers to every intrastate shipment that includes a motor segment, the railroad must be regarded as a "motor carrier" even during the rail portion of the intermodal movement, and the [Railroad Commission] would retain the power to regulate the entire intrastate movement. Again, Texas does not claim that authority. We think it clear that the only way to square the words of the statute with those aspects of the ICC's jurisdiction that the State does accept is to hold that the ICC's authority over intrastate transportation provided by an interstate rail carrier encompasses the entire movement, even when it includes a truck segment under Plan II.\(^\text{34}\)

Attempts to distinguish ICC v. Texas on the basis that there the over-

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\(^{31}\) Id. at 452-453.
\(^{32}\) Id. at 455-457 (emphasis added).
\(^{33}\) Id. at 455 n.8.
\(^{34}\) Id. at 456, 458-459.
the-road transportation was provided in rail-owned equipment and the motor carriers involved were affiliates of the railroads are unpersuasive. The pivotal factor in *ICC v. Texas* was the Court's finding that the intermodal service provided pursuant to a Plan II rail tariff is a rail carrier's service and the truck component thereof is not to be viewed as the service of an independent motor carrier. Similarly, as will be discussed further in this paper, Congress has indicated instances where the truck component of an air/truck movement is not to be treated as the service of an independent motor carrier. In such instances, truck service is integral to the service of the involved air carrier and should be viewed as a component of air service. Thus, the Supreme Court's reasoning is set forth in *ICC v. Texas* is equally applicable in this context. Distinguishing between the wholly intrastate truck portion of an air/truck movement which crosses the state's boundary (i.e., an interstate movement) and the wholly intrastate truck portion of a wholly intrastate air/truck movement is illogical in the context of air transportation as it was in the context of rail regulation. Section 10521(b)(1) of the Interstate Commerce Act\(^3\) does not preserve the states' jurisdiction to regulate such service in either case.

**DOES STATE ECONOMIC REGULATION OF MOTOR CARRIERS "RELATE TO" AIR CARRIER SERVICES?**

Pursuant to Section 1305(a)(1), a state's regulation is preempted only if it "relates to" the rates, routes, or services of an air carrier. In order for the state regulation to "relate to" these matters, there must be a connection or reference thereto. Whether a state regulation has the necessary nexus to an air carrier's activities is not always readily apparent. Certainly, the relationship between a state law aimed at economic regulation of most carriers would upon initial examination seem to have no connection with air carriers' rates, routes, or services. However, where the state seeks to apply such a law to motor carriers providing transportation which is integral to air service, the connection becomes more discernable. The connection is made even more clear when the airlines are threatened with civil penalty enforcement actions as a consequence of their use of motor carriers not complying with a state's licensing or rate requirements.

In *Trans World Airlines, Inc. v. Mattox*, the Fifth Circuit concluded that although the state laws under examination were not aimed specifically at airlines, and did not clearly attempt to prescribe the airlines' rates, it was inescapable that such laws (in that case, deceptive advertising laws) did "relate to" rates when applied to airline fare advertising since the enforcement of a state law regulating fare advertising against airlines obvi-

ously had a connection with or reference to the airlines' rates within the meaning of Section 1305(a)(1). To define the "relating to" phrase of Section 1305(a)(1), the Fifth Circuit relied on the Supreme Court's decision in Shaw v. Delta Airlines, Inc., in which the Court noted that a law related to an employee benefit plan, in the normal sense of the phrase, if it had "a connection with or reference to" such a plan.

In Shaw v. Delta the Supreme Court held that it had to give effect to the plain "relating to" language of the statute preempting state laws unless there was good reason to believe that Congress intended the language to have some restrictive meaning. To determine Congress' intent, the Court used what is, in essence, a three-prong test. First, it examined the language used by Congress. Second, it examined the sections of the same statute which created specific exemptions from the preemption language. Third, it examined the legislative history of the preemption section.

Applying the Shaw test to Section 1305, it is clear that its structure and its legislative history require giving effect to the plain language of Section 1305(a)(1). The only exceptions to the provisions of Section 1305(a)(1) specifically refer to certain wholly intrastate operations. The provisions of Section 1305(a)(2), (b) and (c) demonstrate that Congress was aware of the states' interest in certain activities, such as the operation of airports and transportation between points in Alaska. If Congress had not intended to incorporate wholly intrastate activities in the language in subsection (a)(1), there would have been no need to provide specifically that such activities were saved from the preemption clause. The legislative history of Section 1305(a)(1), previously discussed, clearly indicates Congress' intent to preclude all state regulations so as to "prevent conflicts and inconsistent regulations." In addition, the House Conference Committee's Report notes that one of the purposes of the Deregulation Act was "to encourage, develop and attain an air transportation system which relies on competitive market forces to determine the quality, variety and price of air services."

Like the state enactments scrutinized in TWA, it is inescapable that

36. TWA, 897 F.2d 773, 783 (5th Cir. 1990).
38. TWA, 897 F.2d at 783, quoting Shaw v. Delta Airlines, 463 U.S. at 96-97.
40. See id. at 96-100.
41. See supra notes 21-22 and accompanying text.
42. See supra text accompanying notes 12-22.
state statutes prescribing economic regulation of motor carriers do have a "connection with or reference to" airline rates and services when the state regulation is enforced against motor carriers used by airlines in the performance of intermodal movements or against the airlines themselves. Entry regulation restricts the availability of motor carriers to provide the truck component of such movements. In the case of rate regulation that prescribes the rates charged by the motor carriers to the airlines, there will generally be a direct correlation between the charges which the airline pays for the motor carrier service and the airlines' rates to the public for the involved services. The connection between civil penalty enforcement actions against the airlines for their use of non-complying motor carriers and the airlines' provision of services which are dependent on use of motor carriers is self-evident.

The Fifth Circuit is not alone in utilizing the Shaw v. Delta test to determine whether state regulations are preempted pursuant to Section 1305(a)(1). The First, Seventh and Ninth Circuits have also embraced the test. For example, in New England Legal Foundation v. Massachusetts Port Authority, the First Circuit found a state landing fee structure "related to" the rates, routes, and services of air carriers because in setting standards for the size of aircraft and frequency of air carrier service that would enable carriers to qualify for lower landing fees, the program "ha[d] a connection with or reference to" such activities. Moreover, like the Fifth Circuit in TWA, the First, Seventh, and Ninth Circuits found express rather than implied preemption pursuant to Section 1305(a)(1). Accordingly, these cases held that the involved state regulations were preempted, even though there was no regulation of the involved activity on the federal level. By expressly preempting state and local law, the New England court found, "Congress obviously did not intend to leave a vacuum to be filled by the Balkanizing forces of state and local regulation." Similarly, in Illinois Corporate Travel v. American Airlines, a case involving an airline's proscription of price discounting by travel agents, the Seventh Circuit held that the "relating to language in Section 1305(a)(1) substantially increases the extent of preemption." In light of such express preemption, the court found that the savings clause contained within the Federal Aviation Act did not preserve state common law claims,

46. New England, 883 F.2d at 175.
47. 897 F.2d 773, 783 (5th Cir. 1990).
49. 889 F.2d 751, 754 (7th Cir. 1989).
notwithstanding the absence of contrary federal law on the particular matter to which the state law would apply. In Hingson, the Ninth Circuit said that the “relating to” language of Section 1305(a)(1) constitutes express preemption which preempts not only state laws or regulations that conflict with federal law, but ALL state laws which relate to such matters.

While it might appear that the district court in Federal Express Corp. v. California Public Utilities Commission rejected the Shaw v. Delta test in the process of determining whether the purely truck transportation services of Federal Express, an air carrier, were subject to state regulation or were protected pursuant to Section 1305(a)(1), that is not the case. Federal Express stated that Shaw’s reading of the ERISA preemption should not be taken as a canon of statutory interpretation. However, the court did not reject the Shaw test. It recognized that where the legislative history of preemption language indicates that Congress specifically intended a broad reading of preemption, it must be given effect. In that case, the plaintiff, Federal Express, asserted that Section 1305(a)(1) preempted state regulation of the ground transportation services rendered by it, even when no prior or subsequent movement by air was involved. Federal Express pointed to the fact that it was an air carrier within the scope of Section 1305(a)(1), and therefore all state regulations relating to its operations were preempted by that section. The court disagreed. It found that Federal Express had not presented any legislative history concerning Section 1305(a)(1) comparable to that underlying the ERISA preemption which would require preemption of all state regulations relating to activities with which an air carrier might have some connection, irrespective of whether the activities affected were, in fact, air carrier services. Thus, the court in Federal Express, instead of rejecting the Shaw test, merely recognized a limitation inherent in Section 1305(a)(1): to be preempted, the state regulation must relate to air carrier services, rates, or routes.

**IS THE TRUCK PORTION OF AN AIR/TRUCK MOVEMENT AN AIR CARRIER’S SERVICE WITHIN THE MEANING OF SECTION 1305?**

Federal Express demonstrates that although a regulation may affect an air carrier, it is not preempted unless it affects the “rates, routes, or

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51. Illinois Corporate Travel, 889 F.2d at 754 (emphasis added).
52. Hingson v. Pacific Southwest Airlines, 743 F.2d 1408, 1415 (9th Cir. 1984) (emphasis added).
54. *id.* at 1303.
55. *id.* at 1302.
56. *id.*
57. *id.* at 1303.
services" of an air carrier. In determining whether the wholly intrastate and wholly by truck services of an air carrier were services within the scope of Section 1305(a)(1), the court in Federal Express employed the test enunciated by the Ninth Circuit in Air Transport Association v. Public Utility Commission of State of California.58

The Air Transport court took a rather restrictive view of the scope of Section 1305's phrase "...services of an air carrier." That case involved the monitoring of telephone (both interstate and intrastate) conversations by airlines. The monitored conversations were between the airlines' reservations agents and members of the general public. The airlines claimed that such monitoring was necessary to assure that their agents were giving information accurately, efficiently, and courteously.59 The airlines characterized the contested PUC regulations (which required a third person wishing to listen in on a conversation to give notice by giving warning) as one relating to the services of an air carrier. On this basis, the airlines claimed the regulation was preempted pursuant to Section 1305. The court disagreed.60 The court found that the regulation was not preempted because it did not relate to either the rates, routes or services of an air carrier within the meaning of Section 1305. The telephone operations utilized by the airlines, the court said, were not "services of an air carrier" because they were "not peculiar to airlines;" but rather, were "similar to those operations used by other national service industries where reservations are required. ..."61

Applying the Air Transport test, the court in Federal Express determined that state regulation of wholly intrastate motor carrier transportation of property by an air carrier, where the motor carrier operations were unaccompanied by a prior or subsequent movement by air, was not preempted under Section 1305 because such motor transportation services of an air carrier were not "singularly airline services."62 However, it specifically distinguished joint air/motor vehicle movements from the involved motor vehicle operations throughout its opinion. The court distinguished ICC v. Texas on the basis that it was limited to an "intermodal" transportation situation, which the CPUC was not seeking to regulate in the case of Federal Express.63 Furthermore, referring to Section 10526(a)(8)(B) of the Interstate Commerce Act, the court stated:

One key to Congressional thinking on this matter is the Interstate Commerce Act, which deprives the [ICC] of jurisdiction over certain motor carriers when

59. Id. at 202.
60. Id. at 207.
61. Id. (emphasis added).
63. Id. at 1304 n.3.
air transport is also involved. For example, where transportation of property by motor carrier is part of a continuous movement involving air transportation, the ICC does not have jurisdiction. However, the exemption does not extend to motor carrier service of an air carrier. It is limited to those goods actually transported by joint air and ground carriage. . . . 64

The court concluded that although under normal circumstances ground and air transportation have been viewed by Congress as belonging to two different regulatory regimes, Congress specified in Section 10526(a)(8) instances when motor carrier transportation is to be seen as an adjunct to air transportation and therefore exempt. 65

The distinction recognized in Federal Express between the wholly motor carrier operations of an air carrier and joint air/truck operations is sound. In contrast to the operations scrutinized in Federal Express, intermodal air/motor vehicle operations are "peculiar to airlines." The very nature of airline operations precludes airlines from serving each and every point directly by aircraft. Historically, the airlines have had to rely on other modes of transportation, particularly motor vehicles, to reach shippers and receivers in outlying communities which are not served directly by air. Since the infancy of the air transportation industry, airlines engaging in the transportation of package express have also been dependent on motor carriers to transport such packages within the municipalities served by the airlines. This use of motor carriers by airlines apparently gave rise to the "incidental to air" exemption in the Interstate Commerce Act of 193866 to which the Federal Express court made reference. 67 The ICC interpreted this exemption to include motor transportation rendered on behalf of an air carrier, distinguishing such motor carriage from the motor service of an independent motor carrier. 68

The structure of the Federal Aviation Act also supports the distinction recognized in Federal Express. The Act defines air transportation with reference to interstate air transportation, inter alia. 69 Interstate air transportation is defined as transportation by aircraft or in intermodal opera-

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64. Id. at 1305 (emphasis added).
65. Id.
66. See discussion in Motor Transportation of Property Incidental to Transportation by Aircraft, 95 M.C.C. 71, 84 (1964) (explaining that such use of motor carriage by airlines was the genesis for the "incidental to air" exemption).
67. The Federal Express court referred to § 10526(a)(8) where the "incidental to air" exemption is now found. This exemption was previously contained in 49 U.S.C. § 303(b)(7a). When Congress amended the Interstate Commerce Act in 1980 and enacted 49 U.S.C. § 10526(a)(8), it expanded the exemption as it applies to the transportation of property. The purpose and scope of the exemption, as amended, are discussed in the following section.
69. 49 U.S.C. app. § 1301(10) defines "air transportation" as "interstate, overseas, or foreign air transportation or the transportation of mail by aircraft." (emphasis added).
Interpreting that definition in the context of joint air/truck operations, the Court of Appeals for the District of Columbia found that the term "air transportation" was not restricted to that portion of the service provided by aircraft; it included the trucking service also. The definition of an air carrier includes, inter alia, one who undertakes to engage in air transportation. Nothing could be more essentially a "service" of an air carrier than the performance of "air transportation." Thus, the term "services of an air carrier" must relate to transportation wholly by aircraft or to intermodal transportation where at least some part of the movement is by aircraft.

Significantly, certain motor carrier services were recognized by CAB as "servicers in connection with transportation by air." Such services have been included in airline tariffs pursuant to 49 U.S.C. app. § 1373 requiring specification of airlines' rates, fares and charges for air transportation.

WHAT ARE THE CHARACTERISTICS OF MOTOR CARRIER TRANSPORTATION WHICH IS AN ADJUNCT TO AIR TRANSPORTATION?

In determining the parameters of preemption under the Federal Aviation Act, it is instructive to examine in more depth Congress' subsequent amendment of the Interstate Commerce Act. As the court in Federal Express noted, Congress specified in Section 10526(a)(8) of the Interstate Commerce Act those instances in which ground transportation would be treated as an adjunct to air service. Subsection (A) declares ground transportation of passengers that is "incidental to air" shall be so treated. For property (including baggage), Congress specified in Subsection (B) that this category would include ground transportation that is "part of a
continuous movement which includes a prior or subsequent movement by air." Subsection (C) declares substitute ground transportation in emergency situations also qualifies as an adjunct to air service.

Prior to the enactment of Section 10526(a)(8), Congress' provision for the treatment of adjunct ground transportation was contained in Section 303(b)(7a) and 303(b)(7b). Pursuant to the scheme then in place, both property and passenger movements had to be "incidental to air." However, the exemption insofar as the intermodal transportation of property (as opposed to passengers) was expanded considerably through Congress' enactment of Section 15026(a)(8)(B) in 1980. Unquestionably, by such amendment, Congress meant to remove the restrictions applicable to the "incidental to air" exemption as it had been previously applied by the ICC to the transportation of property. In pertinent part, the legislative history of Section 10526(a)(8)(B) states:

This section also expands the statute's current exemption of motor carrier transportation which is incidental to air transportation. The current exemption has been interpreted by the Commission and the courts to be limited to transportation of air freight which constitutes bona fide collection, delivery, or transfer service. It does not include line-haul transportation by motor carriers. In addition, the exemption has been limited under Commission regulations to geographical areas surrounding airports and cities adjacent to those airports. The bill eliminates the distinction between exempt pick-up, delivery, or transfer operations and regulated line-haul transportation. Further, the bill does away with the geographical limitations imposed by the Commission.

The ICC's interpretation of the previous exemption required the existence of a "through bill of lading" referring to the ground transportation in order to prove the involved ground transportation was in fact incidental to air, in other words, truly a bona fide collection, delivery, or transfer service, and not line-haul transportation. But, since Congress specifically noted that the exemption would no longer be restricted geographically or to bona fide collection, delivering, or transfer service but would also encompass what would otherwise be regulated line-haul transportation, evidently there is no longer a "through bill" requirement in connection with this exemption. It is also clear from the Committee's report that there is no longer a requirement that the motor vehicle service be restricted to points within the air carrier's "terminal area."

76. 49 U.S.C. § 303(b)(7a).
78. See Motor Transportation of Property Incidental to Transportation by Aircraft, 112 M.C.C. 1, 12 (1970); Motor Transportation of Property Incidental to Transportation by Aircraft, 95 M.C.C. 71, 84 (1964); Kenny Extension-Air Freight, 61 M.C.C. 587, 594-596 (1953).
80. Id.
Significantly, the statute does not use the term "incidental to air transportation" with regard to the property exemption. Instead, it specifically spells out the two requirements which are applicable: (1) that there be a prior or subsequent movement by an air carrier and (2) that the motor vehicle operation be part of a continuous movement.81 This was apparently done in order to avoid the future application of unintended restrictions to the exemption.82

Congress did carry forward one of the four elements required under the previous interpretation of the "incidental to air" exemption for property: the "continuous movement" requirement. This term is not defined in Section 10526(a)(8) or any other section of the Interstate Commerce Act. However, in other contexts where the existence of a "continuous movement" has been at issue, the courts and the ICC have focused on the shipper's "fixed and persistent intent" at time of shipment to make the determination.83 Certain ICC and court decisions interpreting the old "incidental to air" exemption for property are also helpful in understanding what Congress must have intended to include in the exemption by reference to the term. For example, in *Kenny Extension-Air Freight*,84 the ICC held that requiring that the intermodal shipment constitute a *continuous movement* moving pursuant to a through air bill of lading would ensure that the line-haul services of an independent carrier as part of a *through air-motor service* would not qualify under the exemption. The ICC reasoned that line-haul movement by an independent carrier would not move on air billing.85 Likewise, in *National Bus Traffic Association v. United States*,86 the court distinguished "[c]onnecting-carrier line-haul motor operations [which] are complimentary to air transportation services with which they connect and are conducted regularly as a part of through interline service" from those which would normally be encompassed within the "incidental to air" exemption.87 From such cases we learn that continuous movements include those that move by independent connecting

82. Notably, there was no requirement under the previous "incidental to air exemption" that the motor vehicle portion of an intermodal movement be provided in the air carrier's own equipment or even by the air carrier itself. No such requirement exists today under Section 10526(a)(8)(B) nor in the Federal Aviation Act. In fact, the definition of the term "air carrier" indicates that an entity may engage in air transportation directly, indirectly, by lease, or any other arrangement 49 U.S.C. app. § 1301(3) (1988).
83. See e.g., Central Freight Lines v. Interstate Commerce Commission, 899 F.2d 413 (5th Cir. 1990); Texas v. United States, 866 F.2d 1546, 1549 (5th Cir. 1989); Package Express Services, Ltd.—Petition for Declaratory Order, 133 M.C.C. 124 (1983); Yellow Cab Company of Pittsburgh v. Pennsylvania Public Utility Commission, 501 A.2d 323 (Pa. 1985).
84. 61 M.C.C. 587 (1953).
85. Id. at 595-596 (emphasis added).
87. Id. at 872-873 (emphasis added).
carriers in line-haul service and that are intended by their shippers to move from point of origin to ultimate destination point. It is this very type of regularly conducted, connecting-carrier, line-haul operation which Congress apparently meant to include within the scope of Section 10526(a)(8)(B). Only by expanding the exemption in that fashion would Congress achieve its declared purpose of achieving the "maximum flexibility" in the movement of air cargo.88

Congress also specifically incorporated in the Section 10526(a)(8)(B) exemption the "prior-or-subsequent movement" by air test which had been previously rejected by the ICC when interpreting the "incidental to air" exemption. The ICC had rejected such a test on the basis that it would impermissibly extend the scope of the exemption.89 The ICC again rejected the prior-or-subsequent test in a later case dealing with the geographical limits of the "incidental to air" exemption for property:

[W]e are not convinced that we should depart from the 25-mile "rule of thumb" terminal area for most airports, and we believe that any enlargement of this standard must be supported by compelling reasons. To conclude otherwise would lead to the unbridled expansion of "exempt" motor operations on a showing that such service is "in connection with" transportation by air, i.e. that the traffic handled has a prior or subsequent air movement. . . .90

Undoubtedly, Congress was aware of these ICC decisions. The legislative history of Section 10526(a)(8)(B) reflects that Congress meant to do exactly what the ICC had previously been unable or unwilling to do under the Interstate Commerce Act prior to its amendment in 1980.91 That is, Congress meant to include in this exemption all motor carrier movements performed in connection with transportation by air.

By expanding the property exemption in this fashion, Congress eliminated the potential for continued conflicts and uncertainties which would arise from having different regulatory schemes applicable to the same service merely as a consequence of joint air/ground modes having been used as opposed to transportation wholly by aircraft. Again, the legislative history of Section 10526(a)(8)(B) clearly explains Congress' intent in this regard:

The Committee's purpose in expanding the existing exemption is to bring it in line with what Congress has done on air cargo movements. Since the transportation of air cargo now is exempt from federal economic regulation, the

89. See Motor Transportation Incidental to Air, 95 M.C.C. at 86.
90. Motor Transportation of Property Incidental to Transportation by Aircraft, 112 M.C.C. 1, 16 (1970) (emphasis added).
91. See supra text accompanying note 75.
Committee believes that it makes sense to exempt the entire movement, including the motor carrier transportation portion. Further, extending the exemption will allow maximum flexibility in dealing with air cargo which generally requires specialized and expedited handling.92

Section 10526(a)(8)(B) can thus be seen as a natural extension of Congress' goal of eliminating conflicts between varying regulatory schemes in the area of air service regulation. While in the Federal Aviation Act it proscribed state regulation in the area, in the Interstate Commerce Act it eliminated the potential for conflicting regulation emanating from the ICC. Of course, its task in this latter regard was considerably easier since it had only to deal with those areas of potential overlap over which the ICC retained jurisdiction: motor carrier and freight forwarder activities.93 By describing in the Interstate Commerce Act the characteristics of ground transportation which are to be viewed as an adjunct to air service, Congress provided a better understanding of the extent to which it views truck transportation as integral to air service. But, preemption pursuant to Section 1305 is not dependent on such movements being encompassed within the Section 10526(a)(8)(B) exemption. Section 10526(a)(8)(B) is merely indicative of those truck services which are to be viewed as an adjunct to air services. Therefore, even if it is assumed that neither Section 10526(a)(8)(A) nor (8)(B) applies to intermodal movements performed wholly within the same state94, preemption of state regulation of such movements pursuant to Section 1305(a)(1) of the Federal Aviation Act is not precluded.

IS STATE REGULATION OF MOTOR VEHICLE MOVEMENTS OF UNINTENTIONALLY UNACCOMPANIED BAGGAGE PREEMPTED?

It is undisputed that intentionally unaccompanied baggage in intermodal air/truck service is encompassed by the Interstate Commerce Act's "incidental to air" exemption applicable to property.95 But, an interesting question is presented when one considers unintentionally unac-
accompanied—that is, lost, misrouted, or delayed—baggage, because the
movement of such baggage has historically been governed by the rules
and regulations pertaining to the transportation of passengers and not the
transportation of property.\textsuperscript{96} \textit{Fourmen Delivery Service, Inc.—Petition for
Declaratory Order} held that baggage accompanying a passenger would
normally come to rest at the destination airport and thus would not move
on a through bill of lading. At that point, the ICC reasoned, the air move­
ment was completed. Any subsequent movement required because the
baggage had been misrouted or delayed would not be "intended" until
the passenger arrived at the destination airport. Therefore, the subse­
quent movement would constitute a separate and distinct movement
wholly apart from the air movement. If that subsequent movement was
between two points within the same state, the ICC concluded, that move­
ment would be in intrastate commerce, even though the prior air move­
ment had originated in a different state.\textsuperscript{97} Under the \textit{Fourmen} reasoning,
therefore, the subsequent motor carrier movement of such baggage
would not be part of a continuous movement. It would then follow that
motor carrier service would not be integral to the services of an air carrier
and state regulation thereof would be permitted.

But the ICC overruled its \textit{Fourmen} decision in this regard in \textit{Package
Express, Ltd.—Petition for Declaratory Order}.\textsuperscript{98} There the ICC held that
the movement of lost or delayed baggage, prior or subsequent to a move­
ment by air, constituted a part of a continuous movement. The ICC ex­
pressly rejected the \textit{Fourmen} reasoning, concluding instead that the
delayed, misplaced, or misrouted baggage does not come to rest until it
is delivered to the passenger it originally accompanied. The ICC stated:

\begin{quote}
[T]he fixed and persistent intent of the passenger is that the baggage will
move through to his ultimate destination. The delay, misplacement, or mis­
routing of the baggage by the airline should not be viewed as altering the
intention or as causing the baggage to "come to rest." An air passenger
expects that the airline [will] be responsible for his baggage, and if the bag­
gage is not tendered to the traveler at his destination [airport], he expects
that the air carrier will make all arrangements and payment for the surface
transportation of the baggage to his ultimate destination. . . . the airline takes
on the status of a shipper in arranging for the continued movement of the
baggage to the passenger's ultimate destination.\textsuperscript{99}
\end{quote}

Having concluded that the motor vehicle movement of lost, delayed or
misplaced baggage was part of a continuous movement which was in­tended
as necessary by the passenger at origin, the ICC held such move­
ment was exempt under Section 10526(a)(8)(B). It noted that the section

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{96} Id.
\item \textsuperscript{97} Id. at 868-869.
\item \textsuperscript{98} 133 M.C.C. 124 (1983).
\item \textsuperscript{99} Id. at 126-127.
\end{itemize}
\end{footnotesize}
does not distinguish between types of baggage or the conditions under which the baggage is being transported. The determinant factor, it held, is whether the involvement property is a part of a continuous movement. There is no basis upon which to distinguish motor carrier service provided as an adjunct to air service when it involves lost, delayed, or misrouted baggage as opposed to other forms of property.

Although *Package Express* and the one case that we have found relying on it, *Yellow Cab Co. of Pittsburgh v. Pennsylvania PUC*, involved intermodal movements which crossed a state boundary, the ICC's reasoning in *Package Express* is equally applicable in the context of a wholly intrastate movement. In any event, as discussed earlier, whether the intermodal air/truck movements are interstate or intrastate is not the controlling factor in the case of preemption under Section 1305(a)(1). The issues are whether such intermodal movements are "services of an air carrier," whether the involved state regulation "relates to" such services, and whether the air carrier is licensed (or exempted) under Subchapter IV of the Federal Aviation Act. The phrase "services of an air carrier" is broad enough to include truck transportation when the truck service is part of a continuous movement which involves a prior or subsequent movement by air, as specified in Section 10526(a)(8)(B). The ICC has concluded that movements of lost, delayed or misrouted baggage are continuations of the originally embarked movement. Therefore, it is clear that state regulation of intrastate intermodal movements of lost, delayed or misrouted baggage is preempted by Section 1305(a)(1).

**CONCLUSION**

There seems little doubt that state motor carrier entry regulations are preempted under 49 U.S.C. app. § 1305(a)(1) where the state seeks to apply them to motor carriers performing the truck portion of an intermodal air/truck movement of property (including lost, delayed, or misplaced baggage), if the truck portion is a part of a continuous movement which includes a prior or subsequent movement by an air carrier licensed or exempt under Subsection IV of the Federal Aviation Act. Such truck service is integral to air service and is included in Section 1305(a)(1)'s reference to the "service of an air carrier." This is amply illustrated by Congress' actions in respect to Section 10526(a)(8)(B) where Congress recognized that truck service used in the transportation of property is an adjunct to air service if it is a part of continuous movement having a prior or subsequent movement by an air carrier. Since it is an adjunct to air

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100. Id.
service, that type of truck service has been exempted from ICC jurisdiction pursuant to Section 10526(a)(8)(B).

A continuous movement for air freight is one where the intent of the shipper at origin of the intermodal movement is that the freight move in continuous movement between point of origin and point of final destination. A continuous movement for lost, delayed, or misrouted baggage is one in which the motor vehicle operation is conducted between the origin (or destination) airport and the passenger’s ultimate destination (or returned to the passenger’s home), and it is not limited to service within terminal zones. Once it is demonstrated that the motor vehicle operation is part of a continuous movement which includes prior or subsequent transportation by an interstate air carrier, state regulation thereof appears preempted even though:

1) the entire intermodal movement is performed wholly within the same state;
2) the motor vehicle operations are not performed by the air carrier itself, but by an unaffiliated motor carrier;
3) the motor carrier operations are conducted using equipment which is not owned or leased by the air carrier; and
4) there is no “through bill” for the intermodal movement.

There do not appear to be any geographical limitations within which the motor vehicle portion of the intermodal movement must be performed in order to be part of an air carrier’s service. As long as the other requirements are met, the length of the truck movements is of no consequence.
I. INTRODUCTION

In the beginning, mass transit was an American standard. From stage coaches to trolley cars to railroads, Americans travelled in groups. But this era ended with the advent of the automobile. The car has come to symbolize American individualism and the ability to come and go at whim.

The days of lone adventurism are coming to a close. Americans still love their cars, but other, perhaps more important factors, give rise to a new attitude toward mass transit. The need to protect the environment from automobile carbon monoxide emissions, to decrease American dependence on foreign oil, and to decrease traffic congestion in urban areas, are such considerations.

More and more, communities are turning to mass transit systems to alleviate these problems. Yet, current transportation systems are inadequate. Few American metropolitan cities have fixed-rail mass transit systems, and those that do have them are not using them efficiently and effectively.

This paper will explore the transportation situation affecting our cities by examining the sources of the problem. It begins with a discussion of current transportation policy and controlling federal laws. The second section sets forth alternative transit systems and ways for local govern-
ments to increase ridership. Funding sources for municipalities considering mass transit systems is the focus of the next section. Finally, a cost-benefit analysis provides a comparison between continued use of funds for highway projects and use of funds for mass transit systems.

II. FEDERAL AND STATE TRANSIT POLICY

A. FEDERAL TRANSPORTATION POLICY

On March 8, 1990, the Bush Administration released its first federal transportation policy. Policy measures included increased flexibility of use of federal funds, a reduction of barriers to private transportation investment, and a concentration of federal funds on transportation systems of national significance.¹

A theme in the transportation policy, and one that is echoed in the Urban Mass Transportation Act,² is encouragement of joint efforts between local, state and federal governments as well as encouragement of private participation in transportation projects.³

Transportation Secretary Samuel Skinner said that the policy emphasizes transportation safety, research and development and greater reliance on "user fees" like highway tolls and mass transit fares. The budget includes $18 billion for capital investments in highway, transit and aviation infrastructure.⁴

The ideals behind federal policy statements are usually followed by the states. However, policy statements do not mandate change. Change comes only through passage of legislation. So, nearly one year after the Bush administration announced its national transportation policy, the Surface Transportation Assistance Act was unveiled.⁵

Provisions of the Act include an increase in the overall level of funding for highway and mass transit and is consistent with the 1990 policy in that the federal government's share of the costs is decreased.⁶ The $105 billion program is designed to expand and improve the nation's deteriorating bridges and highways. It also "encourages" the construction of

². The Act reads that among its purposes is "the cooperation of mass transportation companies both public and private." 49 U.S.C. § 1601 (1964).
⁴. Id.
urban mass transit systems.7

However, the Act is unlikely to pass Congressional scrutiny in its current form. Already there is growing opposition to the thrust of the program which emphasizes highway and bridge construction, that is, cars at the expense of mass transit.8

Officials from public transit agencies threatened to band together if the proposed Act becomes law.9 These officials in particular are annoyed with the administration's plan to cut all mass transit operating subsidies. Without operating subsidies, transit agencies would be forced to hike fares by as much as 25%,10 possibly resulting in decreased ridership.

Numerous arguments exist against the proposal: it does not relieve traffic congestion, pollution, or oil consumption.11 The plan does nothing to further the administration's environmental policy. In fact, the Bush plan would change the allocation of federal funding to the point that states which consume the most gasoline would receive increased federal funding.12 That is, each state's share of federal highway funds would be based largely on its fuel consumption, as reflected by fuel tax figures.13 This factor could jeopardize air quality improvements in large urban areas such as Los Angeles.14

As in the 1990 transportation policy, the Surface Transportation Assistance Act shifts funding from the federal government to the states. The rationale for this decision was provided by Secretary of Transportation Samuel Skinner, who said: "States have a tendency to treat federal transportation funds as 'free money.' "15 Representative Robert Roe, chairman of the House Public Works and Transportation Committee retorted: "I don't know how the states, with all their financial problems, are going to come up with the money that's needed."16

The future of mass transit will be in limbo if the states do not come up with the necessary funding. And, if mass transit is not funded—just "encouraged"—then the pollution, congestion and foreign oil dependence obstacles will become ever-escalating problems.

8. Id.
10. Id.
12. Id.
14. Id.
15. President Unveils Surface Transportation Plan That Would Raise States' Cost Share, supra note 6.
Before discussing the major reasons for needing effective mass transit systems, it is necessary to discuss the evolution of transportation policies, and specific legislation passed effecting urban mass transportation.

B. PERTINENT TRANSPORTATION LEGISLATION: THE URBAN MASS TRANSIT ACT AND THE DEPARTMENT OF TRANSPORTATION ACT

In 1964 the Urban Mass Transit Act was passed. The Act established a comprehensive program of federal assistance to states for urban mass transportation. The purpose of the Act was to:

(1) assist in the development of improved mass transportation facilities, equipment, techniques and methods with the cooperation of [private and public mass transportation companies]; (2) encourage the planning and establishment of area-wide urban mass transportation systems needed for economic and desirable urban development; and (3) provide assistance to state and local governments and their instrumentalties in financing such systems, to be operated by public or private mass transportation companies as determined by local needs.

In 1966 the Act was amended to direct the secretary of transportation to establish a comprehensive research program that would improve the convenience, speed, safety and cleanliness of urban mass transportation.

The Urban Mass Transportation Assistance Act of 1970 was a result of a conviction in Congress that a new mass transportation program must be financed and that it should include a substantially longer period of assured federal funding. The Act also created the Urban Mass Transportation Administration (UMTA) which provides consolidated management of all federal mass transit programs. The 1970 Act provides for a greater role for private enterprise.

In 1974 the Act was again amended to establish a six year program that includes assistance for both capital and operating expenses.

In 1973, Congress passed the Federal-Aid Highway Act. The 1973 Act permits flexibility in the use of highway funds for mass transportation facilities and equipment. The Act sets aside funds for use in either construction of primary highways in urbanized areas or mass transit

20. LAW AND ECONOMIC REGULATION, supra note 18, at 312.
projects.23

According to the Act, local officials may choose to substitute a transit project for an urban highway project as long as the state certifies the project’s priority within the overall urban transportation plan. Under the Act, upon approval by the secretary of transportation, a transit project is substituted for the highway project and receives the same federal share (75% of the total project cost) as it would have if it were used for highway construction.24

Since these acts were passed, transportation needs have changed. Cities have grown in both population and square miles. Shifts in commuting patterns and the increased number of commuters have resulted from the demographic changes. As a result, cities are faced with worsening pollution and traffic congestion. The following section outlines the current situation.

III. THE CURRENT TRANSPORTATION PROBLEM

A. AIR POLLUTION IN THE NATION’S METROPOLITAN CITIES

Mass transit is one solution to the nation’s air pollution situation. In cities such as Los Angeles, where the air is heavily polluted, mass transit systems are being built to alleviate the carbon monoxide buildup. In Denver, where carbon monoxide levels are consistently high, city and state officials are searching for ways to fund a fixed-rail mass transit system.25

Beginning in the 1970s, Congress mandated that states treat their pollution problems. Much of the nation’s air pollution is created by automobiles (mobile sources) which emit carbon monoxide. The Clean Air Act (CAA), for example, deals specifically with automobile-related pollution.26

Section 202 of the CAA gave the Environmental Protection Agency (EPA) authority to set emission standards for new motor vehicles. Other sections of the CAA ensure that new cars, once purchased, continue to meet emission standards.27 Section 110(a) authorizes states to include “transportation control plans” (TCPs) and regulation of “indirect sources” of air pollution (e.g., parking garages) in their state implementation plans (SIPs).28

Today, states are not compelled to adopt TCPs, but many metropoli-

24. LAW AND ECONOMIC REGULATION, supra note 18, at 318.
tan cities have adopted programs designed to decrease air pollution caused by mobile sources. Some cities ask that citizens voluntarily leave their cars at home one day a week. Other cities have high-occupancy vehicle (HOV) lanes for use only by cars with two or more passengers. Still other cities have desirable mass transit systems that citizens choose to ride in lieu of driving.29

In addition to monitoring mobile sources, the EPA, pursuant to the CAA, sets National Ambient Air Quality Standards (NAAQS) for six criteria pollutants—including carbon monoxide and particulates.30 In "non-attainment" areas, continued violations of EPA standards can result in the loss of federal highway funds.31

Continued funding of new highway projects actually worsens the pollution problem because it makes long distance travel more convenient. As a result, automobile traffic, and consequently air pollution, increases. For instance, future population growth, driving habits, fuel costs and the level of urban sprawl will cause vehicle miles travelled (VMTs) to increase 90% by the year 2010.32

Health officials around the country say that long-term air quality improvements will only come with increased use and construction of mass transit systems and a heavy dose of public education.33 Denver, for instance, does not have a fixed-rail mass transit system and has among the worst carbon monoxide and particulate pollution in the country and routinely violates federal standards for carbon monoxide.34

Many of the country's mayors believe that a light-rail system combined with laws requiring employers at new commercial developments to reduce their workers' travel are the best transportation strategies for reducing pollution.35

United States Senators are pressuring administration officials to press for mass transit in order to alleviate air pollution problems. Senator Frank Lautenberg (D.-N.J.) blasted Transportation Secretary Samuel Skinner for endorsing deep cuts in federal mass transit funding at a time when Congress was struggling to pass clean air legislation: "You know and I know, Mr. Secretary, that every time someone uses mass transit, it means one less car on our congested highways and less automobile ex-

30. NATURAL RESOURCE LAW, supra note 27, at 120.
33. Sprawl May Foul Efforts to Clean Area Air, supra note 31.
34. Western Cities Move Aggressively to Clear Up Smoggy Skies, supra note 25.
haust polluting our air." 36

The Bush administration chose not to abide by environmental considerations when it announced its 1991 Transportation Act. Notably, much of the funding for the bill would come from the federal Highway Trust Fund, which is supported by motor fuel taxes. 37 The result of this kind of funding, according to a spokesperson for the Environmental Defense Fund, would be that "[s]tates that reduce gasoline consumption through ride pools, HOV lanes, transit and other creative measures, would actually be penalized by receiving a reduced share of federal highway funds." 38

Yet, states must comply with the CAA. In order to comply, the states' largest cities must develop alternatives to the one-person, one-car phenomenon. Building new super-highways is not the answer. This results in more people living further from where they work, thus increasing the VMTs and air pollution. Mass transit, therefore, is a viable alternative to compliance with the CAA.

B. CURRENT HIGHWAYS AND FREEWAYS ARE NOT EQUIPPED TO HANDLE INCREASED TRAFFIC

Gone are the days when one could walk to work. Today, people "commute." The daily hustle from home to work and back often takes the better part of an hour, and most commuters choose to drive their 30-plus miles alone. When many cars converge, gridlock and traffic congestion occurs. While sitting in the car idly waiting for the light to change, the car is idling—and emitting exhaust through its tailpipe.

Transportation experts point out that getting commuters on public transportation is the only way to solve congestion and other problems. 39

Commuters around the country, frustrated by growing traffic problems, are encouraging the passage of advisory measures asking officials to consider mass transit. 40 Transportation planners listen because they know that not enough space exists to add more urban highways. 41

C. EFFECTIVE MASS TRANSIT IS IMPERATIVE TO ECONOMIC GROWTH

The Urban Mass Transportation Act was passed, in part, due to a Congressional finding that:

38. Id.
41. Congressional Obligation Ceilings Reduce Transportation Prospects, Eng'g News Record, Jan. 21, 1988, at 96.
the welfare and vitality of urban areas, the satisfactory movement of people and goods within such areas . . . are being jeopardized by the deterioration or inadequate provision of urban transportation facilities . . . the intensification of traffic congestion, and the lack of coordinated transportation . . . on a comprehensive and continuing basis.42

Congress’ findings in the 1964 Act hold true today. Among the provisions of the Bush Administration’s 1990 transportation policy is a shift in focus from building basic infrastructure to adapting and modernizing transportation systems to support economic growth.43

Traffic congestion caused by more drivers travelling further to converge upon the same land mass has far-reaching effects. America’s ability to compete in the world marketplace depends upon our ability to move people and products quickly, safely and cheaply.44 It stands to reason that American reliance on foreign oil will decrease if more people use mass transit.

The best way to meet the challenges of improving air quality, lessening congestion, and enabling local economies to compete across the nation and worldwide, is to create in every major metropolitan area a coordinated, centrally operated mass transit commission that works with all transit systems currently available. We must make use of railroad rights of way, make better use of roads and highways and continue to invest in technological improvements that will take us into the Twenty First Century and beyond.

Such a metropolitan area transit commission must take into consideration local realities such as geography, population, climate, funding sources, political atmosphere and the needs of the population. The result must be a comprehensive transit system that utilizes different types of technology.

IV. ALTERNATIVE TRANSPORT SYSTEMS

Mass transit is currently defined as “transportation by bus, rail or other conveyance, either publicly or privately owned, which provides to the public general or special service (but not including school buses or charter or sightseeing service) on a regular basis.”45 Whether this definition will be expanded to include the numerous types of transit being considered remains to be seen. This section discusses the wide range of mass transit alternatives currently available, and what will be available in

42. 49 U.S.C. § 1601(a)(2).
43. HIGHWAY USERS FEDERATION FOR SAFETY AND MOBILITY, Newsletter, March 8, 1990.
the future. Ironically, the first type of mass transit option to be discussed is cars!

A. **Smart Cars and Smart Highways**

The automobile remains a part of the American psyche and until mass transit is more convenient than cars, we will continue to drive. Cars are more fuel efficient than ever and remain an affordable means of transportation. For these reasons, automobiles must be incorporated into any effective mass transit system.

Americans have consistently demonstrated a preference for private automobiles. The convenience, flexibility and affordability of cars and trucks have fostered richly diverse suburban transportation destinations.46

Cars are more useful than buses or fixed-rail systems as mass transportation in sprawling western cities because rail systems are geared to carry riders from the suburbs to the city and the most significant change in commuting patterns in this decade has been the increase in the number of people travelling from suburb to suburb.47 Moreover, people prefer cars because mass transit is not as convenient as cars; it does not depart from one's home and end up at the door to one's destination. It is sometimes also difficult to find a seat on mass transit and on some systems, there is a fear for personal security.48

The "smart car" systems of the future will keep the driver informed of his or her current location, suggest the best route to the destination and alternate routes in case of traffic tie-ups and may eventually include systems for automatic vehicle spacing and collision-avoidance.49

The automobile of the future will respond to sensors along the freeway, automatically set the ideal speed for conditions and keep the driver at a safe distance from other cars. In the meantime, changeable electronic message signs will keep drivers alert to the traffic situation ahead.50

Most "smart car" technology already exists in the form of short-range communications, variable electronic message signs, automatic toll systems, in-vehicle computers and twenty-four hour optical guidance systems.51

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49. *Smart Cars, supra* note 44.
50. *Id.* You could also proceed through Vehicle Identification toll lanes which will automatically deduct appropriate fees from, for instance, your Visa Card.
51. *Id.*
Europe and Japan already have smart car programs in operation. In this country, the California Department of Transportation and the Federal Highway Administration are sponsoring a demonstration project in Southern California along the Santa Monica Freeway.\(^{52}\)

Advantages to the smart car system include: (1) use of existing highways; (2) decreased use of federal funds; (3) less traffic congestion; and (4) less carbon monoxide exhaust.\(^{53}\)

One disadvantage is the high cost of a fully computerized, state-of-the-art vehicle. Even if there is a way to subsidize individuals so that more people can operate these cars, prospects for the project occurring in the near future are slim. Indeed, most transportation experts predict that another twenty years will elapse before systems of this type are commonplace.\(^{54}\)

\section*{B. Bus Systems}

All metropolitan areas utilize bus systems. Buses are most effective when used in areas with a widely dispersed population. Buses use less operating energy than either cars or the new generation of rail transit.\(^{55}\) The problem is how to increase bus patronage.

Despite its availability, bus riding has never caught on. In order to catch a bus, one must walk to a stop and wait outside. When the bus arrives there is no guarantee of a seat. The bus will make numerous stops before reaching its destination and then it is necessary to walk to your final destination. Most people, given the choice between a car and a bus, will likely choose a car.

Marketing busing by transit authorities might help. Many people complain that they do not know which bus to catch or where the bus stops. Until fixed-rail systems are widely available, busing remains the most useful form of mass transit.

\section*{C. Light-Rail}

Across the nation, cities are building or are considering light-rail as an alternative transit system. Baltimore will soon begin construction on a twenty two mile light-rail line.\(^{56}\) The Metropolitan Area Express (MAX) light-rail system in Portland, Oregon, is widely credited with the down-

\begin{thebibliography}{9}
\bibitem{52} Id.
\bibitem{53} Id.
\bibitem{54} Interview with Joe Sullivan, transportation researcher at the Center for the New West, a Denver-based think-tank dedicated to western-states' issues (May 21, 1990).
\bibitem{55} Lave, \textit{supra} note 48, at 10.
\bibitem{56} \textit{Cities Tracking Light Rail as Urban Transit Solution}, City and State, March 13, 1989, at 1.
\end{thebibliography}
town's rebirth. The San Diego Trolley is the most financially successful transit system in the country, with lines to the Mexican border and through bedroom communities to the east. Even Los Angeles, the bastion of automobile autonomy, is building a light-rail line from downtown to Long Beach.

UMTA officials say cities now believe having a rail system is a mark of civic pride, like a professional sports team or a domed stadium. It doesn't pollute, it's clean, it's quiet.

This may be why so many cities consider light-rail systems. Other cities with light-rail systems operating or in the works are Buffalo, New York, Sacramento and San Jose. In addition, Philadelphia, Pittsburgh and San Francisco have converted their turn-of-the-century trolley lines into light-rails.

Light-rail has become trendy and everyone wants one. Unfortunately, the down-side to light-rail is two-fold: it is expensive and few people ride it.

For example, Portland began a light-rail system in 1983. The total cost of the project once completed was $266 million; the projected cost was $172 million. And, while projected ridership was 42,500, only 19,700 people actually ride the rail on a daily basis. Pittsburgh’s light-rail system covers ten miles and cost $622 million dollars; 30,600 people ride the system daily. The projected ridership was 90,500—three times the actual ridership. The situation in Miami is even bleaker. Miami’s light-rail system cost over a billion dollars and only 35,000 people ride it daily, although projected ridership was 239,900!

Projected ridership figures were obviously overly optimistic and city officials may have been persuaded to build the system based on these unreasonably high projections. Estimated projected costs were low for the same reasons. Yet, despite high costs and low turnout, cities continue to consider light-rail.

Given the above statistics, why do cities continue to consider light-
rail as a form of mass transit? One reason is public demand. People in metropolitan areas, tired of the pollution and tired of the congestion, demand that city leaders consider alternative forms of mass transit. But, once cities comply with these demands, no one rides the system. The reason: the public expects their neighbors to use mass transit, but not themselves.66

Another reason for considering light-rail has to do with civic pride. Every metropolitan area wants to attract new business and one way to sell a city is to show how progressive it is—what a model city it is for the future. In cities like Portland, the light-rail system may have served this purpose. In Portland, downtown business is rebounding, a number of historic old buildings have been restored for office and retail use and The Rouse Company, based in Maryland, is building a major mixed-use development adjacent to the MAX line.67

There is also genuine concern for the environment. Los Angeles, with its high carbon monoxide level, has partially completed a light-rail and subway system that, combined, will span 150 miles.68 The Los Angeles system is also efficient in that commuters coming out of the subway station’s two exits can connect with twenty Southern California Rapid Transit buses.69 Officials are hopeful about the number of people using the system, which is up to 24,000 on weekdays.70

Cities also view light-rail as a means of lessening traffic congestion on the freeways and in the city. However, if more people do not start using the systems available to them, none of these goals will be achieved.

D. HEAVY-RAIL

In 1970 Congress declared that “modern, efficient, intercity railroad passenger service is a necessary part of a balanced transportation system.” Accordingly, Congress passed the 1970 Rail Passenger Service Act.71 Congress found that the public convenience and necessity required the improvement of such service and that federal financial assistance, as well as private investment capital, was needed to establish a national rail passenger system.

Although Amtrak has never been profitable, ridership is up, and it seems to be turning the corner. The railroad has a goal of becoming self-
sufficient by the year 2000.72

Indeed, on June 5, 1990, polls indicated that Californians will approve bond issues totalling roughly $3 billion in the first year to expand trolley mass transit and Amtrak service throughout the state. If the bond issues pass, California will spend more for railroad expansion than the total amount the federal government spent on the national Amtrak system in the past four years.73

The difference between a light-rail system and a heavy-rail system is that a heavy-rail line typically draws power from an electrified third rail, meaning the line must be totally separated from automobile and pedestrian traffic. In contrast, light-rail cars are smaller and generally powered by overhead wires, which enable them to run at street level with automobile traffic travelling alongside.74

Light-rail and heavy-rail are not in competition the way light-rail competes with buses. Heavy-rail is used most often to move traffic between metropolitan areas, say, from Baltimore to Washington, or from San Diego to Los Angeles. If California's initiative is any example, then heavy-rail will continue to be a viable mass transit source, easing traffic on the nation's interstate highways.

E. OTHER ALTERNATIVES

Many other alternatives to mass transit have been proposed. Ideas range from magnetically levitated trains to monorails running down freeway medians to monorails that run in river and flood control channels.75

Combining alternatives is the best system. Transit planners see the future of mass transit as analogous to the present communications network: combining all known and available sources of transportation into a coordinated system which uses every link to its fullest potential.76

Mass transit systems will not continue to get funding unless present systems increase ridership. The following section provides methods for transit authorities to accomplish this goal.

F. INCREASING RIDERSHIP

One obstacle to effective mass transit is persuading people to use the system. This is particularly true in the West where cities are spread

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73. California Has Been Driven to Mass Transit, supra note 58.
74. Cities Tracking Light Rail, supra note 56.
76. Interview with Joe Sullivan, supra note 54.
out and mass transit is a relatively recent phenomena. Getting people out of their cars may be more taxing than getting funds for the system itself.

Unfortunately, the belief that one is more "free" when one has a car at her disposal is perpetuated by public figures. Colorado Governor Roy Romer recently stated that he is "open to all alternatives to reduce air pollution from cars that don't result in a loss of freedom or have prohibitive costs. One of the great privileges of being human is to be free."77

Rebuttably, a mass transit system that runs on schedule and is convenient does not make a person less free. In fact, time is utilized more efficiently because mass transit frees a passenger to read the newspaper or do work, rather than concentrate on driving.

Given a choice between transit alternatives, passengers seem to prefer rail to buses, so these systems attract more commuters to public transportation.79

For instance, San Diego’s light-rail system has exceeded its ridership forecast. Officials projected daily ridership of 9,000, but instead found ridership averaging 11,000 daily.80 This may be due to the fact that San Diego’s weather is warm year round so weather does not deter people from using the system. Also, cities which build their systems around the area’s points of interest have higher ridership rates than others.81

In fact, “rail revival” has been effective throughout California because steeply rising land prices have forced the typical resident to live farther from work in order to afford a single family home. The automobile, once the symbol of freedom, has become a trap on crowded freeways.82 Increasingly, these people turn to mass transit.

Providing incentive for people to use mass transit is one way of getting people out of their cars. Transportation planners increasingly use HOV lanes open only to carpools and buses. Use of these lanes by single commuters can result in large fines.83

Other planners favor mandatory programs to make employers give their workers incentives to break the one-person, one-car habit.84

Senators from eastern states suggest using tax incentives. Currently, 77. For instance, in Chicago, RTA board members may use the system for free. However, only one board member actively uses the RTA system. Other members use private automobiles while the RTA chairman maintains a chauffeur-driven limousine at public expense. Lowenstein, The Need for Limitations on Federal Mass Transit Operating Subsidies: The Chicago Example, 12 TRANSP. L.J. 265 (1982).
78. Commuters Love Cars but Hate Brown Cloud, supra note 35.
79. Cities Tracking Light Rail, supra note 56.
80. Id.
81. Id.
82. California Has Been Driven to Mass Transit, supra note 58.
83. Commuters Love Cars But Hate Brown Cloud, supra note 35.
84. Id.
workers do not pay taxes on parking paid by their employer, but they do pay taxes on money their employer gives them to use on mass transit. Changing the law so that mass transit users get the tax benefit provides further incentive.

Transportation officials must also try to coordinate different types of transit modes to make commuting as effortless as possible. Considering mass transit as a convenience rather than a hassle will make people more likely to utilize the system.

Lastly, planners must think about transit systems in the long term. It is unwise to put a light-rail system in one area if the growth area is somewhere else. Continuing to expend funds for busing is infeasible if light-rail attracts more passengers and if rights of way for rail are available.

Once state and local officials decide that a mass transit system, such as light-rail, is necessary, and that the community will use the system, the scramble for funding begins.

VI. FUNDING

A. FEDERAL FUNDING

The principal source of federal financial assistance comes from the Urban Mass Transportation Administration (UMTA). Programs under the UMTA include (1) technical study grants; (2) discretionary capital improvement grants; (3) formula assistance grants; and (4) managerial training grants.

The UMTA provides capital grants or loans to states for (1) construction, acquisition or improvement of mass transit facilities and equipment; (2) coordination of mass transit services with highways and other transportation; and (3) establishment and organization of public transit corridor development corporations. Capital grant programs are based on a matching arrangement, with the federal government paying 75% to 80%, and state and local governments, 20% to 25%.

The formula grant program permits the use of funds for operating as well as for capital assistance.

The Federal-Aid Highway Act of 1973 made highway trust funds available for mass transportation facilities and equipment. If a local proposal to substitute a transit project for an urban highway project is approved by the secretary of transportation, the transit project will receive

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85. LAW AND ECONOMIC REGULATION, supra note 18, at 313.
86. LAW AND ECONOMIC REGULATION, supra note 18, at 314.
88. Cities Tracking Light Rail as Urban Transit Solution, supra note 56.
75% of the total project cost.\textsuperscript{91}

Federal cutbacks, however, have lead to the discretionary allocation of federal funds. Under present transportation policy, only transit systems of national importance (as yet, undefined) will receive substantial federal funding.\textsuperscript{92} Of the $440 million a year the government is spending on new transit, much of that money is given to projects in Los Angeles, Baltimore and Atlanta.\textsuperscript{93}

The current administration’s budget reduces funding for the UMTA by $600 million, cutting UMTA’s budget from $3.1 billion to $2.5 billion in 1991.\textsuperscript{94} Such drastic cuts force local governments to either reduce service or go to the farebox or the state for funding.\textsuperscript{95}

Professor Henry Lowenstein points out that federal funding for local mass transit is not necessarily a good thing because it leads to too much federal involvement in matters of local importance.\textsuperscript{96} Lowenstein argues that in the Chicago area, federal funds have contributed to inefficient operations.\textsuperscript{97}

Too often, according to Lowenstein, federal transit monies are not used to fundamentally improve transit services to the public. Rather, government subsidies at all levels are spent to cover unreasonable labor costs, excessive administrative overhead, the maintenance of artificially low fares and costly, inefficient route systems.\textsuperscript{98}

Others, however, take a diametrically opposing view to Lowenstein.\textsuperscript{99} Commentators Hemily and Meyer argue that federal funds for capital and operating costs are a necessity because local governments cannot make up the difference.\textsuperscript{100}

\section*{B. STATE AND LOCAL FUNDING}

Federal funding is hard to come by and may lead to unwanted federal control. Therefore, some cities refuse to accept federal money. For instance, the successful light-rail system in San Diego was built largely with money raised locally.\textsuperscript{101}

\begin{thebibliography}{99}
\bibitem{91} \textit{Law and Economic Regulation}, \textit{supra} note 18, at 318.
\bibitem{92} \textit{Metro Rail Funds Near OK Despite Federal Cutbacks}, L.A. Times, Nov. 18, 1987, at 1, col. 4.
\bibitem{93} \textit{Will We Ever Ride The Rails}, \textit{supra} note 40.
\bibitem{94} \textit{Dateline: Washington}, \textit{supra} note 3.
\bibitem{95} \textit{id.}
\bibitem{96} \textit{Lowenstein}, \textit{supra} note 77, at 266.
\bibitem{97} \textit{id.}, at 272.
\bibitem{98} \textit{id.}, at 280.
\bibitem{100} \textit{id.}, at 288-289.
\bibitem{101} \textit{Lowenstein}, \textit{supra} note 77, at 284.
\end{thebibliography}
Traditionally, the UMTA provided 75% of the cost of transit systems. UMTA now expects cities to pay at least half the costs of new transit systems.\textsuperscript{102}

Secretary Skinner contends that Washington cannot solve local problems and further argues that increased state and local funding will result in better, more efficient transportation programs. Critics argue that higher user fees are essentially hidden taxes.\textsuperscript{103}

The National Association of Regional Councils also advocate increased state and local funding resulting in "increased flexibility and control over decisions."\textsuperscript{104}

Although the trend is to advocate local funding of mass transit, the problems that arise due to federal cuts are many. For instance, when federal funding is cut, fares are often raised and such an increase falls disproportionately on the poor.\textsuperscript{105}

One way that cities are able to keep operating costs of new light-rail systems down is by using existing rail lines that were abandoned by the railroads and then turned over or sold at a relatively low cost to the local governments.\textsuperscript{106}

San Diego is an example of an effective system that can be built and operated with a minimum of federal funding. However, other proposed projects, such as the one in Seattle, may not ever be built because it is not a system of national importance and because the state may not be able to raise the required funds. Therefore, another source of funding must be found. The administration and others argue that increased use of private funds is such a source.

C. COST PRIVATIZATION

The Bush administration's mass transit policy encourages use of innovative financing options such as benefit assessments, joint public-private initiatives and other means for capturing the value of transportation projects.\textsuperscript{107}

One example of private money funding transportation projects is found in Iowa. Here, money for grants came from $29 million in refunds the state received from oil companies for overcharges to their Iowa customers in the 1970s.\textsuperscript{108}

\begin{enumerate}
\item \textsuperscript{102} Will We Ever Ride the Rails?, supra note 40.
\item \textsuperscript{103} Dateline: Washington, supra note 3.
\item \textsuperscript{104} National Ass'n of Regional Councils, Meeting Our Transportation Needs in the 21st Century, Newsletter (1990).
\item \textsuperscript{105} Hemily & Meyer, supra note 99, at 295-296.
\item \textsuperscript{106} Cities Tracking Light Rail as Urban Transit Solution, supra note 56.
\item \textsuperscript{107} National Transportation Policy, released March 8, 1990.
\item \textsuperscript{108} Mass Transit Grants Awarded to 16 Systems, UPI, Aug. 26, 1986.
\end{enumerate}
In Chicago, dissatisfaction with the Regional Transit Association's (RTA) management of the transit system stimulated the search for alternative methods of transportation by commuters. Private charter bus services to Chicago from western suburbs are springing up and some private employers are supplying employee shuttle buses between key commuter railroad stations and downtown Chicago. These private, non-subsidized carriers operate only premium rush hour service, yet charge a fare 20% to 50% below that of RTA. Ironically, at this lower fare level, these carriers provide high quality service while breaking even or in some instances, showing a profit.109

On the other hand, some argue that privatization of mass transit may actually be harmful.110 The Economic Policy Institute recently released a study which focuses on mass transit. The study—The Emperor's New Clothes: Transit Privatization and Public Policy—finds that UMTA's policies "force" communities to contract out operations to the private sector. The private operators then often become major political players whose interests do not always coincide with the community's interests.111 Another effect of privatization is that the "stranglehold of unions" has been broken.112 This results in private companies paying salaries to mass transit employees that are unreasonably low.

D. FAREBOX FUNDING

Funding from the fare box continues to be a major source of funding, primarily covering operating costs. In Chicago, the RTA operates with a budget of $834.4 million. Of that amount, approximately 39% is derived from farebox revenues.113 Portland's MAX system met about 59% of its operating costs through fares in 1988.114

E. OTHER FUNDING SOURCES

The final funding source comes from the taxpayers. Voter initiatives around the country are being structured to provide funding for construction of mass transit systems through, for instance, gas taxes. In Denver, the light-rail line proposed in the 1990 legislative session was to be funded by a gas tax levied upon Denver-area taxpayers pursuant to the taxing authority granted the Regional Transportation District. The bill

109. Lowenstein, supra note 77, at 280.
111. Id. Such a situation may ultimately parallel the dilemmas besetting the airline industry following deregulation.
112. Id. This point is echoed in Lowenstein's article which stresses that high union salaries keep mass transit fares high.
113. Lowenstein, supra note 77, at 269.
114. Cities Tracking Light Rail, supra note 56.
failed largely because of concerns by rural legislators that their communities would not receive funding in the future.\textsuperscript{115} Gas taxes, however, remain a viable source of funding in other localities, and perhaps in Colorado eventually.

VI. COST-BENEFIT ANALYSIS

A. GENERALLY

Some transportation experts argue that the cost of an effective fixed-rail mass transit system is prohibitive and that not enough people use current systems. Whatever the costs of building and maintaining a mass transit system, the long-term benefits will often outweigh the costs. At a time when the nation’s infrastructure is badly in need of repair, many states and municipalities must make a decision whether to devote limited financial resources to highway projects or mass transit.\textsuperscript{116}

B. MASS TRANSIT COSTS

The costs of building either a light- or heavy-rail system are initially high, but there are ways to mitigate the construction costs. For instance, heavy rails and rights-of-way are often already in place, so that the only cost incurred is that of the trains and operating costs.

Ironically, while the UMTA disparages cities from considering light-rail systems, light-rail can move more passengers at a lower operating cost per passenger than can buses. This is because light-rail lines are cheaper to operate than buses and a light-rail system can meet a larger portion of its operating costs through the farebox than can a bus system.\textsuperscript{117}

C. MASS TRANSIT COSTS COMPARED TO HIGHWAY COSTS

Typically, if a state wants to build an interstate highway, the cost per mile runs anywhere from $50 million to $100 million a mile, not including the acquisition of the right of way. A new subway system costs about $200 million per mile to build. With a light-rail line running at street level or on a private right of way, if one is available, the cost comes down to $20 million to $25 million a mile.\textsuperscript{118}

At a time when many metropolitan areas are considering the option

\textsuperscript{115.} Committee Cuts Gas Tax from MTA Bill, The Denver Post, April 22, 1990, at 1B.
\textsuperscript{116.} White House Press Secretary Marlin Fitzwater recently remarked regarding a possibility of "shortchanging" mass transit in favor of highway improvements: "This is an age old kind of concern and a trade-off that they have had to make since Day One." Bush Proposes a Five-Year, $105 Billion Highway Plan, supra note 7.
\textsuperscript{117.} Cities Tracking Light Rail as Urban Transit Solution, supra note 56.
\textsuperscript{118.} Id.
of mass transit systems despite the high cost, Congress has cut infrastructure expenses due to the federal budget deficit. The budget for fiscal 1988 represented a 5% cut from 1987 and stemmed from a "budget summit" between the President and congressional leaders.\footnote{119}

As previously discussed, funding from the federal government may lead to unwanted federal involvement. The federal government sometimes uses funding as a method of coercing states into compliance with administration objectives. An example of such coercion occurred during the Reagan administration. The administration wanted states to lower their drinking age; when states would not comply, the government threatened to cut off federal highway funds.\footnote{120}

The Urban Mass Transportation Assistance Act of 1971 gives metropolitan areas the option of using the funds for highway projects or using some of the funds for mass transit. In New York City, officials have the option of dividing funds between a six lane at-grade roadway and mass transit. City planning officials use the money to fund mass transit, pointing out that getting commuters onto public transportation is the only way to solve the city's gridlock and other traffic problems.\footnote{121}

The federal government, however, is not the only source for funding a highway project. In particular, the state of Colorado has turned to public and private financing to build E-470, a toll road looping around the east side of Denver. Other states will advance plans to build sections of toll roads under the Federal Highway Administration's pilot program announced in 1987. The program allows states to use their federal funds for up to 35% of the toll road projects' cost.\footnote{122}

Although construction costs of light- and heavy-rail systems may seem initially prohibitive, there are a number of advantages which outweigh the costs in the long run. One of the primary benefits from mass transit is its effect on the environment.

**D. Environmental Benefits of a Mass Transit System**

One of the most important benefits of mass transit systems is the decrease in air pollution. If state and federal funds are spent on highway projects, people will continue to drive to work, usually with one passenger per car.\footnote{123} For example, the majority of commuters in Denver—84%, according to a recent poll by the Metropolitan Transportation Develop-
The problem is that motor vehicles are perhaps the most significant source of air pollution, especially in the nation’s cities. Four of the six major criteria pollutants—carbon monoxide, hydrocarbons, nitrogen oxides and photochemical oxidants (ozone)—are chiefly caused by the passenger auto.\footnote{125}

One of the main reasons city officials are being drawn to light-rail systems rather than continuing to fund highway projects is the environmental advantages\footnote{126} and compliance with the CAA may prove costlier than a new rail system. For cities like Denver and Phoenix, which have among the worst carbon monoxide and particulate pollution in the country and continually violate federal standards for carbon monoxide, continued violations could cost the state $33 million in federal highway funds,\footnote{127} not to mention the negative health effects on citizens forced to breathe carbon monoxide fumes. Putting a price tag on health benefits is impossible.

Although it is difficult to attach an accurate dollar figure to the air pollution harm, in the late 1970s the Council on Environmental Quality estimated that air pollution was costing the country $21.4 billion per year.\footnote{128} From 1972 to 1979, a total of $65.2 billion was spent on air pollution abatement.\footnote{129}

Construction of urban mass transit systems such as light- and heavy-rail can therefore provide an important catalyst for improving air quality within metropolitan areas. Cities which do not presently have mass transit systems are being fined for violating the CAA. A mass transit system will decrease pollution levels within a city, freeing up funds for more important uses.

\section*{E. Mass Transit Leads to Better Use of Diminishing Downtown Property}

In addition to the environmental advantages, many cities find that switching to mass transit results in more efficient use of land because of the decreased need for parking lots and parking garages. As cities grow, downtown real estate becomes too valuable to be devoted solely to park-

\begin{itemize}
\item \footnote{124} Id.
\item \footnote{125} NATURAL RESOURCES LAW, supra note 27, at 145.
\item \footnote{126} Cities Tracking Light Rail as Urban Transit Solution, supra note 56.
\item \footnote{128} NATURAL RESOURCES LAW, supra note 27, at 118, \textit{quoting} the Tenth Annual Report of the Council on Environmental Quality 44-50 (1979).
\item \footnote{129} NATURAL RESOURCES LAW, supra note 27, at 118, \textit{quoting} N.Y. Times, April 12, 1982, at 16.
\end{itemize}
Consequently, the downtown area benefits aesthetically and ultimately may lure more customers and businesses back to the downtown area.  

F. MASS TRANSIT ALLEVIATES GRIDLOCK

Mass transit systems provide other unique benefits that highways cannot provide. Gridlock is created by the large number of automobiles on the highways converging upon a central area. Mass transit alleviates such gridlock. Outside of the automobile industry, there is a consensus that urban highways cannot cope with many more vehicles. There is not space to add any more lanes in most downtown areas. For this reason, transportation planners are showing more interest in rails to move people into and through cities.  

G. MASS TRANSIT SYSTEMS CONTRIBUTE TO ECONOMIC GROWTH

"Infrastructure is essential to economic growth. Without transportation, communications and energy, prosperity is unattainable."  

In 1974, Atlanta began building its heavy-rail system. The reason for building the system was due largely to the concern that the region was being kept from reaching its fullest potential due to traffic conditions. Regional planners were concerned that serious traffic conditions, congestion and mass transportation deficiencies, would increasingly impede the cultural and social development of the area. Today, Atlanta is a thriving metropolis and the heart of the new South.  

On a national scale, groups such as the National Association of Regional Councils are concerned about the viability of the United States in the world marketplace. On the one hand, they praise the interstate highway system which has provided mobility between regions. On the other hand, the Council cites a failure to develop a system that provides a comparable level of mobility within regions. If the United States is to continue to compete in the international marketplace, it must rely on the economic viability of each and every region of the country. American competition cannot be enhanced if it is struck in traffic.

130. Cities Tracking Light-Rail as Urban Transit Solution, supra note 56.
131. In downtown Denver an historic building is being torn down to accommodate a parking lot. Wrecking Ball Speeds Toward Historic Bank, The Denver Post, May 14, 1990, at 1.
132. Congressional Obligation Ceilings Reduce Transportation Prospects, supra note 41.
133. LAW AND ECONOMIC REGULATION, supra note 18.
H. MASS TRANSIT REPRESENTS AN AESTHETIC IMPROVEMENT


For years Colorado residents have been telling public opinion pollsters that their concerns over air pollution are related to three things: public health, aesthetics and the fact that some business are reluctant to move to the Denver area because of the brown cloud. 136

Overall, mass transit represents an improvement over status quo, and local governments may be able to shift some funding from highway projects to mass transit systems. Each metropolitan area must decide which system is most useful to their particular area based on considerations such as those outlined in this section. Decisions made on the local level will determine the future of transportation across the country.

I. USE OF MASS TRANSIT CAN LEAD TO A DECREASE IN AMERICAN DEPENDENCE ON FOREIGN OIL

Recent events in the Persian Gulf have demonstrated that America's dependence on foreign oil can lead to disastrous results. However, not since the 1970's has there been a concerted effort to conserve oil and gas, thus lessening our overall need for foreign oil. 137 In particular, the Bush administration, during the height of Iraqi-American aggressions, released an energy policy that indignantly continued to stress consumption, rather than conservation, of energy. 138 The nation currently imports 42% of its oil, and according to the President, "will continue to import energy for years to come." 139

The Bush policy favors development of nuclear energy and domestic oil reserves, but fails to emphasize energy efficiency. 140 The administration's energy policy, like its 1991 proposed Surface Transportation Assistance Act, is unlikely to be passed by Congress in its current form unless it is amended to include higher fuel efficiency standards for automobiles. 141 A comprehensive energy strategy must conform to the administration's environmental and transportation policies and must in-

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clude the potential for energy efficiency. This is because the nation’s transportation sector currently accounts for more than 60% of the oil consumed in the United States.\textsuperscript{142} Maintaining our current dependence on foreign oil will not provide the incentive for Americans to utilize mass transit and thereby accrue environmental and economic benefits. Currently, two-thirds of the petroleum used in the United States goes to fuel cars and light trucks.\textsuperscript{143} If Americans are encouraged to drive less, dependence on imported oil will necessarily decrease.

\textbf{VII. CONCLUSION}

American metropolitan cities face a transportation crisis. Pollution and traffic congestion have lead voters to call for mass transit systems. However, once cities comply with these demands, citizens fail to use the system. What is needed is a concerted effort by federal, state and local governments to develop incentives designed to increase mass transit use.

Areas that do not already have fixed-rail or other types of mass transit must consider changing their current transportation scheme. If fixed-rail is cost prohibitive, local governments must use present busing systems more effectively and provide incentives for people to ride the bus.

Mass transit in the future should combine all methods of transportation into one central transportation system, coordinating systems to work harmoniously, thereby, inspiring use by commuters.

For the sake of the environment, alleviating traffic congestion, aiding local economies and decreasing our dependence on imported oil, the one-person, one-car phenomenon must cease. America must start looking toward the future and more effective mass transportation is the beginning.

\textsuperscript{142} Id.
The Role of the Federal Employers’ Liability Act in Railroad Safety

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DR. MICHAEL OLFATHER**

I. INTRODUCTION

Safety emerged as a premier transportation issue in the late 1980s. The increasing number of near mid-air collisions led to proposals for re-regulating the airline industry as well as increased spending for air traffic control and airports. The Truck and Bus Safety Act was passed in 1988. The Railroad Safety Act was reauthorized and amended in 1987. As highway congestion increases and the number of large trucks proliferate, the safety issue is sure to be in the forefront of the debate concerning the 1991 re-authorization of the federal highway program.

In the past few years, the railroad industry has asked Congress to change the reparations system governing injuries to railroad workers. Their proposal involves replacing the Federal Employers’ Liability Act (FELA) with a no-fault system such as state workers’ compensation. The objectives of this paper are: (1) to analyze safety trends in the rail indu-

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try in recent years, and (2) to compare the impact of FELA and workers' compensation on railroad investment in safety.

II. RAILROAD SAFETY TRENDS

Before examining safety trends in detail, a brief look at the aggregate safety picture is instructive. By any standard, railroading is a dangerous job. In the 1976-1988 period, there were 80,143 train accidents, 130,884 train incidents, and 477,273 non-train incidents.\(^1\) Thus, total mishaps were 688,300. If these numbers are calculated on an average daily basis, 17 accidents, 28 train incidents, and 101 non-train incidents occur every single day.

The toll on railroad workers is extraordinary. Between 1978 and 1988, 998 railroad on-duty employees were killed and 551,657 injured.\(^2\) This results in an average of 91 on-duty employees killed and 50,151 injured per year.

Railroad accidents also present a significant safety problem for the public. Between 1980 and 1988 there were 4,384 train accidents involving hazardous materials. Of these, 629 cars released hazardous materials, which in turn caused 141,000 people to be evacuated.\(^3\)

Table 1 contains the number of fatalities for all types of persons involved in railroad accidents/incidents during the 1982-1988 period. The number of fatalities remained roughly the same throughout the period. The highest number of fatalities was 1,247 in 1984 and the lowest number was 1,036 in 1985. The mean number of total fatalities for the entire time period was 1,133. Thus, there is no trend either up or down in railroad fatalities. In fact the total number of fatalities in 1988 (1,199) was nearly the same as in 1982 (1,119).

The total number of on-duty railroad worker fatalities declined from 78 in 1982 to 43 in 1988. Railroad employment, however, declined 38% during this period, placing fewer workers at risk.\(^4\) A more accurate gauge is the fatality rate, computed as fatalities per million man hours x

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1. U.S. DEPARTMENT OF TRANSPORTATION, FEDERAL RAILROAD ADMINISTRATION, OFFICE OF SAFETY, Accident/Incident Bulletin, various years. Train accidents, train incidents, and non-train incidents are defined by the Federal Railroad Administration as follows:
   - **Train Accident**: A collision, derailment, or other event involving the operation of railroad on-track equipment resulting in damages that exceed the reporting threshold.
   - **Train Incident**: Any event involving the movement of railroad on-track equipment that results in a death, a reportable injury, or a reportable illness, but in which railroad property damage does not exceed the reporting threshold.
   - **Non-train Incident**: Any event arising from railroad operations but not from the movement of on-track equipment, which does not exceed the reporting threshold, and results in a death, a reportable injury, or a reportable occupational illness.
2. Id.
3. Id.
Table 2 displays fatality rates of railroad on-duty employees for the 1982-1988 interval. The rate remains relatively constant throughout the period, reaching a high of 9.73 in 1982 and a low of 6.60 in 1985 with a mean of 8.21. There is also no consistent trend, either positive or negative in the fatality rates of railroad on-duty employees. The rate fell between 1982 and 1985, increased in 1986 and 1987, and then declined in 1988.

Table 3 contains injuries for all types of persons involved in railroad accidents/incidents. The trend in fatal injuries during the 1982-1988 time frame has been downward. The trend, however, is not consistent or predictable. For example, total injuries declined in 1983, increased in 1984, fell in 1985, 1986, and 1987; then rose in 1988.

Injury rates (defined as injuries per million man hours) of on-duty railroad employees displayed no predictable trend over the 1982-1988 interval (see Table 4). The rate fell about 7% in 1983, increased 8% in 1984, and again dropped about 5% in 1985. In 1986, the injury rate plunged nearly 19%; but this was followed by a 7% increase in the rate in 1987-1988.

Table 5 contains passenger casualty rates (defined as passengers injured and killed per billion passenger miles). There is no consistent nor predictable pattern in the passenger casualty rate that persists over the entire 1982-1988 interval. In the 1982-1984 period, the rate increased 130%. Between 1985 and 1988, it fell nearly 75%.

As noted above, there is no consistent trend in the fatality and injury rates of on-duty rail employees. There is, however, reason to believe that the Federal Railroad Administration (FRA) accident statistics have understated rail employee injuries. James Snyder of the United Transportation Union (UTU) has testified that:

The Railway Labor Executives Association has little confidence in the validity of the statistical data base. The FRA is ignoring the increasingly widespread failures by the railroads to report accidents and incidents as required by law. We have knowledge of many cases where the railroads simply keep injured employees on the payroll and do not report the accident. Other situations involve blatant non-reporting even though the accident or incident is obvious.\(^5\)

Mr. Snyder's lack of confidence in FRA accident statistics was confirmed by a General Accounting Office (GAO) study released on May 1, 1989.\(^6\) The GAO study involved an audit of 1987 railroad accident and

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6. UNITED STATES GENERAL ACCOUNTING OFFICE, RAILROAD SAFETY, FRA NEEDS TO CORRECT DEFICIENCIES IN REPORTING INJURIES AND ACCIDENTS (April, 1989).
injury records of four railroads that accounted for one third of the accidents reported in 1987. Some of the findings of the study are as follows:

- Lost work days associated with employee injuries, which is an FRA measure of injury severity, were underestimated by about 269%.
- FRA data reflected only 57% of the actual number of severe injuries, defined by FRA as 10 or more lost work days, at three of the railroads surveyed.
- Of the 521 unreported injuries, about 12% should have been reported to FRA.
- Of the 532 unreported accidents, about 10% should have been reported to FRA.

The GAO study also referred to FRA's periodic audits of railroads which confirm the GAO findings of railroad under reporting of accidents and injuries. For example, in 1987, FRA conducted an audit of Conrail safety records. They discovered that Conrail only reported 68% of the worker injuries that should have been reported to FRA.\(^7\) A 1987 FRA audit of Burlington Northern also discovered significant under reporting of injuries and accidents.\(^8\)

The GAO investigators concluded that the findings "raise questions about the overall effectiveness of FRA's safety program and the extent to which railroads have become safer."\(^9\)

III. COMPARISON OF RAILROAD SAFETY TO OTHER INDUSTRIES

The hazardous nature of the rail industry is indicated by Table 6. The table compares occupational injury incidence rates by industry for the 1975-1987 period. On average, the railroad injury rate was 44.6% higher than the rate for all private sector industries.

The National Safety Council compiles occupational injury and illness incidence rates by industry. Table 7 contains 1987 injury and illness incidence rates per 100 full-time employees for injury cases involving lost work days. The National Safety Council data is based on reports of National Safety Council members participating in the Occupational Safety/Health Award Program. Table 7 indicates that the railroad transportation injury rate is 161.7% greater than the rate for the total economy and 134.3% more than the Transportation and Public Utilities industry.

IV. SEVERE INJURIES IN THE RAILROAD INDUSTRY

Table 8 contains the types of injuries suffered by railroad on-duty employees in 1988. While over 50% of the injuries are sprains and strains, there is also a high percentage of severe, potentially, career-ending inju-

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7. Id. at p. 30.
8. Id. at p. 31.
9. Id. at p. 3.
ries. For example there were 64 amputations and 1,289 fractures (combin-
ing to equal 8.3% of total injuries). There were 44 concussions and 1,138 lacera-
tions (7.2% of total injuries). Of the 1,138 lacerations, 324 were potential disfig-
urements involving cuts to the head or face. There were 228 burns and 618 poten-
tially blinding injuries involving objects in the eye.

The severity of injuries in railroading can be compared to other indus-
tries by using the Supplementary Data System (SDS) compiled by the U.S. De-
partment of Labor. Established under the Occupational Safety and Health Act (OSHA), SDS pro-
vides valuable information about the characteristics of injuries for various occupa-
tions and industries. The data are compiled from state workers' compensation re-
cords and are organized into three groups. Group 2 is used in this analysis. It in-
cludes data from 18 states and each case involves disability.

While Group 2 of the SDS contains injury data for only 18 states, the geo-
graphic and industrial diversity of these states makes the data repre-
sentative of the national experience. The SDS data were adjusted to ob-
tain national totals by industry for the most severe injuries—amputations and frac-
tures. The national total amputations (fractures) in a given indus-
try was divided by national employment in that industry. This results in an amputation (fracture) rate, which is the number of amputations (frac-
tures) per million employed workers. The 1983 rates by industry are in Table 9.

The amputation rate in railroading is 58% greater than the economy as a whole. Only mining and manufacturing have significantly higher rates than railroading. The fracture rate in the rail industry is 114% greater than the rate for all U.S. industries as a group. Although the amputation rate in manufacturing is higher than railroads, the reverse is true of the fracture rate. In 1983 the railroad fracture rate was 52% greater than manufacturing. Only mining had a significantly higher fracture rate than railroading.

The last column of Table 9 contains the sum of the amputation and frac-
ture rates. The combined rate in the rail industry is 111% greater than the economy as a whole, 43% greater than manufacturing. Only mining has a significantly higher combined rate of severe injuries. This analysis clearly indicates that rail workers suffer a higher rate of severe injuries relative to other industries.

The comparisons used throughout this and the preceding section employ railroad accident and injury statistics reported by FRA in the Accident/Incident Bulletin. If the May, 1989 GAO report cited above is correct

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10. The 18 states in Group 2 of SDS account for 41.6% of U.S. employment. Thus national totals can be obtained for each industry by dividing the number injured by .416.
that rail industry totals are materially understated, railroad accident rates could compare even less favorably with other industries.

V. AMTRAK’S SAFETY RECORD

In 1989 a bill was introduced in Congress to switch the reparations system for Amtrak injuries from FELA to state workers’ compensation. In 1986 the GAO issued a report comparing Amtrak FELA costs to those that would occur under state workers’ compensation. Thus, it is relevant to examine the safety record of Amtrak in recent years. Table 10 contains several measures of Amtrak safety during the 1982-1988 interval. The first two columns contain fatalities and injuries to all types of persons in Amtrak accidents, train incidents, and non-train incidents. Fatalities averaged about 40 per year in the 1982-1984 interval, then declined to an average of 17 in 1985-1986. Fatalities, however, jumped to 101 in 1987 and 99 in 1988. Even after excluding the 16 deaths that occurred in the Chase, Maryland disaster, Amtrak fatalities in 1987 and 1988 were up sharply. Injuries increased 21% between 1982 and 1987, but fell 16% in 1988. The third column displays the casualty rate measured as the frequency of fatalities and injuries per million train miles (involving all types of persons). The rate increased 14% between 1982 and 1987, before dropping 21% in 1988. The next column contains the casualty rate for on-duty rail employees only. It is measured as the frequency of fatalities, injuries, and illness per 200,000 man hours. It increased about 12% between 1982 and 1986, but declined 25% in the 1986-1988 period. The last column displays lost day injury cases which declined by one third between 1982 and 1984, jumped nearly 62% in the 1984-1987 period, and then fell about 12% in 1988. It is interesting to compare the safety of passenger trains to that of other for-hire passenger transportation modes. Table 11 contains passenger death rates (defined as deaths per 100 million passenger miles) for buses, passenger trains and scheduled airlines. In the 1980-1987 period, the average death rates for buses and scheduled airlines were both .04, about two-thirds the rate for passenger trains.

VI. A MODEL OF SAFETY INCENTIVE

From the railroads’ point of view, injury prevention involves both costs and benefits. The costs are the outlays for injury prevention. The benefits are reduced outlays for injury claims, equipment damage, labor downtime, and labor recruitment and training costs. A profit maximizing firm will continue to invest in safety as long as the extra benefits exceed the incremental costs.

These considerations can be formalized in a model as follows:

- MCS (Marginal Cost of Safety)—the increase in the firm's costs stemming from an increase in injury prevention expenditure.
- MBS (Marginal Benefits of Safety)—the reduction in the firm's costs stemming from an increase in injury prevention expenditure.

In Figure 1 the left vertical axis represents expenditures on injury prevention. The right vertical axis, labeled $S^*$, represents perfect safety (no injuries). The horizontal axis represents the degree of safety. At the left origin, all of the firm's workers are being injured; at $S^*$, none are injured. The MCS curve slopes upward, suggesting that it becomes much more expensive to reduce injuries as safety improves.

The MBS curve slopes downward. When many workers are being injured, the marginal benefits of safety are high. When safety is nearly perfect, the marginal benefit of further investment in safety is low.

The profit maximizing level of safety for the railroad is $S_0$. To the left of $S_0$, the MBS exceed the MCS. Therefore, the railroad can increase its profits by investing in more injury prevention. To the right of $S_0$, the MCS are greater than the MBS. These levels of injury prevention would reduce railroad profits.

Suppose the MBS curve reflects the railroad industry under FELA. Now suppose Congress repeals FELA and replaces it with state workers' compensation. Workers' compensation is a no-fault system which partially compensates injured workers for lost wages. It does not compensate the worker or his family for pain and suffering. Furthermore, most states replace only two-thirds of the worker's lost wages, subject to some ceiling amount, which heavily penalizes highly paid workers such as rail employees. If two-thirds of the worker's weekly wage is more than the ceiling amount, the worker does not receive two-thirds wage replacement. A Michigan study concluded that only 20% of the workers' compensation cases received the 66% gross wage replacement specified by statute. In California, average workers' compensation benefits replace only 49% of the earnings lost by permanently disabled workers. Another study revealed that workers' compensation benefits were less than half the workers' pre-injury weekly wage.

Workers' compensation benefits often are paid according to a rigid schedule (loss of an arm or a leg results in a fixed payment) regardless of

the worker’s economic losses. Thus, an employee near retirement age and a new employee facing decades of future wage loss receive the same damage award for a scheduled injury. Maximum payments for scheduled injuries in most states are very low. In 1987, 82% of the states paid a maximum award for loss of an arm that would be less than two years’ salary and benefits for a railroad operating craft employee.\(^{15}\)

Benefits provided by workers’ compensation would keep families of injured railroad workers close to the poverty level. As of January 1, 1987, the U.S. average maximum weekly compensation payment for total disability was $303.\(^{16}\) Maximum payments for permanent partial disability are much less.\(^{17}\) The 1986 poverty line income was an average of $215 per week (family of four).

Therefore, it is clear that injury awards would decline dramatically if FELA is replaced by worker’s compensation. Costs avoided through investment in safety (MBS) would decline substantially. The MBS curve would, therefore, shift downward for all levels of safety investment. The result is a reduction in the profit maximizing level of safety from \(S_0\) to \(S_0'\). Thus the safety incentives of FELA clearly exceed those of state workers’ compensation.

An important question pertains to the magnitude of the difference in safety incentives between the two types of reparations systems. In terms of Figure 1, how much would the MBS curve decline and what would be the reduction in safety investment? Some evidence of this can be gained by a review of actual FELA cases and the differences in awards that would result from the two types of reparations systems.

VII. Cases

A. Hoecker vs. Santa Fe Railroad\(^{18}\)

In this case the victim was injured when he was ordered to cross over a railroad car to get to his train. The train moved, knocked him off the car, and caused soft tissue injuries in the neck area.\(^{19}\)

Under workers’ compensation the injury would have been judged a temporary total disability with the total award in the area of $3,000, depending on the state. However, in the subsequent FELA case the victim was awarded $38,000 in an out-of-court settlement.

\(^{15}\) Calculations are based on 1987 total compensation per rail employee of $49,558 and assuming no raises in future years. Most state workers’ compensation payments ignore supplemental benefits. Fringe benefits in the railroad industry were 22.8% of total rail wages in 1987.
\(^{17}\) Id.
\(^{19}\) Id.
This case involved a worker who suffered a crushed foot while in the railyard. The injury required four surgeries and the victim continued to work for the railroad throughout the surgeries. The foot condition progressively worsened to the point where he was rendered permanently disabled from railroad work.\textsuperscript{21}

In this FELA case the jury issued a judgment of $460,000. Under workers' compensation, the victim would have received a maximum of $18,000.

After the accident, the railroad equipped all employees with steel-toed work boots which would mitigate or eliminate the type of injury suffered by the victim.

C. \textit{Barrett vs. Conrail}\textsuperscript{22}

In this case the victim was killed when the sides of a ditch where he was required to work collapsed around him. Afterward, it was discovered that the ditch had not been shored up in a way that would have prevented the accident. A substantial settlement was reached that provided for the victim's widow and minor children, which among other things, included their education. The settlement was much higher than would have been possible under workers' compensation.\textsuperscript{23}

The importance of FELA is emphasized by the insignificant $490 fine assessed by OSHA in the incident. Had this fine been the only financial incentive for safety, it would have had no significance.

D. \textit{Barker vs. Conrail}\textsuperscript{24}

In this case the victim was a train dispatcher for Conrail in the Philadelphia area. He had a heart attack on the job and subsequently retired. In the ensuing FELA suit it was demonstrated that the railroad company had created such a stressful work environment and had so overburdened the victim with assignments, that as a result he suffered the heart attack.\textsuperscript{25}

As a consequence of the settlement made in this case, working conditions for train dispatchers improved significantly. Territories covered by train dispatchers were decreased and a number of complaints made by train dispatchers concerning stressful working conditions were finally addressed by the railroad company. Had the victim been covered under workers' compensation it is unlikely that he would have received any benefits. Furthermore, the railroad would have had little incentive to alter its work procedures.

\textsuperscript{20. Id.}
\textsuperscript{21. Id.}
\textsuperscript{22. Id. at 27.}
\textsuperscript{23. Id.}
\textsuperscript{24. Id. at 28.}
\textsuperscript{25. Id.}
E. PERKINS VS. MISSOURI PACIFIC

In this case the victim was killed in a derailment. He was survived by a wife and three children, who received $1,250,000 in the wrongful death settlement. Under workers' compensation, the surviving family would have received a maximum of $16,762 per year for a limited number of years, depending on the respective state's workers' compensation regulation.

F. QUIRING VS. ATCHISON, TOPEKA AND SANTA FE

In this case the victim was killed in a derailment. He was survived by a wife and two children who received $1,200,000 in a wrongful death verdict. Under workers' compensation they would have received a maximum of $13,333 per year for a limited number of years (again depending on the state).

Other statistical evidence is available which indicates a large disparity in the awards received by injured workers under the two reparation systems. In a sample of FELA cases terminated between 1982 and 1985, the average compensation for loss of a leg was $751,000. In 1989, the average scheduled compensation for loss of a leg in the workers' compensation system was approximately $64,000.

VIII. CONCLUSION

Both rail employees and railroad companies have incentives to avoid workplace injuries. Employees want to avoid the pain and suffering of an injury and railroad firms want to reduce the costs of accidents and injuries. Thus the relevant question is not whether workers and railroads want to avoid casualties, but which compensation system provides the greatest economic incentives to do so. FELA safety incentives for railroads exceed those of the workers' compensation system. Since FELA fully compensates rail workers for lost income and workers' compensation would not, the cost of an injury to the railroad is higher under FELA. Thus, under FELA railroads would have a greater economic incentive to insure safe working conditions rather than under a system based simply on workers' compensation.

26. Id. at 29.
27. Id.
28. Id.
29. Id.
30. Computed from a representative example of 2,645 FELA cases that were closed by 25 law firms in 15 states in the 1982-1985 period.
TABLE 1
FATALITIES IN RAILROAD ACCIDENTS/INCIDENTS
1982-1988

<table>
<thead>
<tr>
<th>Year</th>
<th>Fatalities</th>
</tr>
</thead>
<tbody>
<tr>
<td>1982</td>
<td>1,119</td>
</tr>
<tr>
<td>1983</td>
<td>1,073</td>
</tr>
<tr>
<td>1984</td>
<td>1,247</td>
</tr>
<tr>
<td>1985</td>
<td>1,036</td>
</tr>
<tr>
<td>1986</td>
<td>1,091</td>
</tr>
<tr>
<td>1987</td>
<td>1,165</td>
</tr>
<tr>
<td>1988</td>
<td>1,199</td>
</tr>
</tbody>
</table>

**TABLE 2**
**FATALITY RATES OF RAILROAD ON DUTY EMPLOYEES***
1982-1988

<table>
<thead>
<tr>
<th>Year</th>
<th>Fatality Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1982</td>
<td>9.73</td>
</tr>
<tr>
<td>1983</td>
<td>8.36</td>
</tr>
<tr>
<td>1984</td>
<td>7.94</td>
</tr>
<tr>
<td>1985</td>
<td>6.60</td>
</tr>
<tr>
<td>1986</td>
<td>8.85</td>
</tr>
<tr>
<td>1987</td>
<td>8.89</td>
</tr>
<tr>
<td>1988</td>
<td>7.07</td>
</tr>
</tbody>
</table>

*Fatalities per million man hours x 100.


**TABLE 3**
**INJURIES IN RAILROAD ACCIDENTS/INCIDENTS**
1982-1988

<table>
<thead>
<tr>
<th>Year</th>
<th>Injuries</th>
</tr>
</thead>
<tbody>
<tr>
<td>1982</td>
<td>40,275</td>
</tr>
<tr>
<td>1983</td>
<td>34,819</td>
</tr>
<tr>
<td>1984</td>
<td>38,570</td>
</tr>
<tr>
<td>1985</td>
<td>34,304</td>
</tr>
<tr>
<td>1986</td>
<td>26,923</td>
</tr>
<tr>
<td>1987</td>
<td>26,033</td>
</tr>
<tr>
<td>1988</td>
<td>27,054</td>
</tr>
</tbody>
</table>

TABLE 4
INJURY RATES OF RAILROAD ON DUTY EMPLOYEES*
1982-1988

<table>
<thead>
<tr>
<th>Year</th>
<th>Injury Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1982</td>
<td>44.96</td>
</tr>
<tr>
<td>1983</td>
<td>41.67</td>
</tr>
<tr>
<td>1984</td>
<td>44.92</td>
</tr>
<tr>
<td>1985</td>
<td>42.79</td>
</tr>
<tr>
<td>1986</td>
<td>34.74</td>
</tr>
<tr>
<td>1987</td>
<td>35.51</td>
</tr>
<tr>
<td>1988</td>
<td>37.12</td>
</tr>
</tbody>
</table>

*Injuries per million man-hours.


TABLE 5
CASUALTY RATES OF RAILROAD PASSENGERS*
1982-1988

<table>
<thead>
<tr>
<th>Year</th>
<th>Casualty Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1982</td>
<td>99.2</td>
</tr>
<tr>
<td>1983</td>
<td>119.7</td>
</tr>
<tr>
<td>1984</td>
<td>228.6</td>
</tr>
<tr>
<td>1985</td>
<td>137.9</td>
</tr>
<tr>
<td>1986</td>
<td>137.7</td>
</tr>
<tr>
<td>1987</td>
<td>91.6</td>
</tr>
<tr>
<td>1988</td>
<td>59.6</td>
</tr>
</tbody>
</table>

*Casualty rate is passenger injuries and deaths per billion revenue passenger miles.


Passenger Miles, ASSOCIATION OF AMERICAN RAILROADS, Railroad Facts, various issues.
### Table 6

**Occupational Injury and Illness Incidence Rates by Industry**

*1975-1987*

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Private sector</td>
<td>54.6</td>
<td>57.8</td>
<td>60.0</td>
<td>62.1</td>
<td>66.2</td>
<td>63.7</td>
<td>60.4</td>
<td>57.5</td>
<td>57.2</td>
<td>61.8</td>
<td>64.9</td>
<td>65.8</td>
<td>69.9</td>
</tr>
<tr>
<td>Railroads</td>
<td>77.8</td>
<td>78.0</td>
<td>88.3</td>
<td>98.5</td>
<td>104.7</td>
<td>106.1</td>
<td>94.9</td>
<td>87.1</td>
<td>76.1</td>
<td>92.6</td>
<td>92.0</td>
<td>75.1</td>
<td>88.3</td>
</tr>
<tr>
<td>Agriculture</td>
<td>68.4</td>
<td>81.1</td>
<td>78.8</td>
<td>78.3</td>
<td>81.7</td>
<td>81.3</td>
<td>81.4</td>
<td>84.2</td>
<td>89.5</td>
<td>89.4</td>
<td>91.3</td>
<td>93.6</td>
<td>94.1</td>
</tr>
<tr>
<td>Mining</td>
<td>109.6</td>
<td>113.9</td>
<td>128.3</td>
<td>142.3</td>
<td>149.8</td>
<td>162.8</td>
<td>145.7</td>
<td>136.7</td>
<td>124.1</td>
<td>159.3</td>
<td>145.3</td>
<td>125.9</td>
<td>144.0</td>
</tr>
<tr>
<td>Construction</td>
<td>98.6</td>
<td>102.6</td>
<td>109.7</td>
<td>108.1</td>
<td>119.2</td>
<td>116.1</td>
<td>112.1</td>
<td>114.6</td>
<td>117.3</td>
<td>126.7</td>
<td>128.9</td>
<td>134.5</td>
<td>135.8</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>72.9</td>
<td>76.7</td>
<td>79.3</td>
<td>82.3</td>
<td>87.3</td>
<td>84.0</td>
<td>79.4</td>
<td>72.4</td>
<td>70.4</td>
<td>74.2</td>
<td>80.2</td>
<td>85.2</td>
<td>95.5</td>
</tr>
<tr>
<td>Wholesale Trade</td>
<td>48.8</td>
<td>50.9</td>
<td>51.9</td>
<td>56.8</td>
<td>58.2</td>
<td>57.1</td>
<td>53.5</td>
<td>51.6</td>
<td>50.1</td>
<td>54.8</td>
<td>59.8</td>
<td>62.5</td>
<td>64.0</td>
</tr>
<tr>
<td>Retail Trade</td>
<td>34.6</td>
<td>38.9</td>
<td>40.0</td>
<td>39.1</td>
<td>44.1</td>
<td>44.1</td>
<td>40.8</td>
<td>42.1</td>
<td>46.3</td>
<td>47.9</td>
<td>47.0</td>
<td>50.5</td>
<td>52.9</td>
</tr>
<tr>
<td>Finance, Insurance, Real Estate</td>
<td>10.5</td>
<td>11.0</td>
<td>10.2</td>
<td>12.1</td>
<td>12.9</td>
<td>11.6</td>
<td>11.3</td>
<td>12.8</td>
<td>12.4</td>
<td>13.2</td>
<td>15.4</td>
<td>17.1</td>
<td>14.3</td>
</tr>
<tr>
<td>Services</td>
<td>31.2</td>
<td>31.9</td>
<td>34.2</td>
<td>35.4</td>
<td>37.1</td>
<td>34.5</td>
<td>34.7</td>
<td>35.1</td>
<td>36.2</td>
<td>40.3</td>
<td>45.4</td>
<td>43.0</td>
<td>45.8</td>
</tr>
</tbody>
</table>

*Total lost workdays per 100 fulltime workers. Total lost workdays includes number of days away from work and number of days of restricted work activity.

TABLE 7
OCCUPATIONAL INJURY AND ILLNESS INCIDENCE RATES BY INDUSTRY*
1987

<table>
<thead>
<tr>
<th>Industry</th>
<th>Lost Work Days per 100 Full Time Employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>All Industries</td>
<td>60</td>
</tr>
<tr>
<td>Railroad Transportation</td>
<td>157</td>
</tr>
<tr>
<td>Agriculture, Forestry, and Fishing</td>
<td>121</td>
</tr>
<tr>
<td>Mining</td>
<td>49</td>
</tr>
<tr>
<td>Construction</td>
<td>71</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>58</td>
</tr>
<tr>
<td>Durable Goods Manufacturing</td>
<td>67</td>
</tr>
<tr>
<td>Non-Durable Goods Manufacturing</td>
<td>50</td>
</tr>
<tr>
<td>Transportation and Public Utilities</td>
<td>67</td>
</tr>
<tr>
<td>Wholesale Trade-Durable Goods</td>
<td>80</td>
</tr>
<tr>
<td>Wholesale Trade-Non-Durable Goods</td>
<td>26</td>
</tr>
<tr>
<td>Retail Trade</td>
<td>39</td>
</tr>
<tr>
<td>Services</td>
<td>35</td>
</tr>
</tbody>
</table>

*Total lost work days per 100 full time employees. Lost work days include both days away from work and days of restricted work activity.

TABLE 8  
NATURE OF INJURIES TO ON DUTY RAILROAD EMPLOYEES — 1988*

<table>
<thead>
<tr>
<th>Nature of Injury</th>
<th>Number</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amputations</td>
<td>64</td>
<td>0.4</td>
</tr>
<tr>
<td>Fractures</td>
<td>1,289</td>
<td>7.9</td>
</tr>
<tr>
<td>Concussions</td>
<td>44</td>
<td>0.3</td>
</tr>
<tr>
<td>Cuts, Lacerations</td>
<td>1,138**</td>
<td>6.9</td>
</tr>
<tr>
<td>Burns</td>
<td>228</td>
<td>1.4</td>
</tr>
<tr>
<td>Objects in the eye</td>
<td>618</td>
<td>3.8</td>
</tr>
<tr>
<td>Dislocations</td>
<td>108</td>
<td>0.7</td>
</tr>
<tr>
<td>Contusions, Bruises</td>
<td>2,862</td>
<td>17.5</td>
</tr>
<tr>
<td>Sprains, Strains</td>
<td>8,792</td>
<td>53.6</td>
</tr>
<tr>
<td>Non-fatal Illness</td>
<td>236</td>
<td>1.4</td>
</tr>
<tr>
<td>Others</td>
<td>1,009</td>
<td>6.2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>16,388</td>
<td>100.0</td>
</tr>
</tbody>
</table>

*Injuries involving lost work days or days of restricted work activity.

**Of this total, 324 are cuts, lacerations to the head or face.

TABLE 9
SEVERE INJURY RATES BY INDUSTRY — 1983

<table>
<thead>
<tr>
<th>Industry</th>
<th>(1) Amputation Rate*</th>
<th>(2) Fracture Rate**</th>
<th>(3) (1)+(2)***</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total—All Industries</td>
<td>159</td>
<td>2,503</td>
<td>2,662</td>
</tr>
<tr>
<td>Railroads</td>
<td>252</td>
<td>5,356</td>
<td>5,608</td>
</tr>
<tr>
<td>Agriculture</td>
<td>166</td>
<td>2,522</td>
<td>2,688</td>
</tr>
<tr>
<td>Mining</td>
<td>479</td>
<td>6,215</td>
<td>6,694</td>
</tr>
<tr>
<td>Construction</td>
<td>258</td>
<td>5,591</td>
<td>5,849</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>421</td>
<td>3,513</td>
<td>3,934</td>
</tr>
<tr>
<td>Transportation &amp; Public Utilities</td>
<td>67</td>
<td>2,717</td>
<td>2,784</td>
</tr>
<tr>
<td>Wholesale Trade</td>
<td>234</td>
<td>3,587</td>
<td>3,821</td>
</tr>
<tr>
<td>Retail Trade</td>
<td>103</td>
<td>1,861</td>
<td>1,964</td>
</tr>
<tr>
<td>Finance, Insurance, &amp; Real Estate</td>
<td>27</td>
<td>866</td>
<td>893</td>
</tr>
<tr>
<td>Services</td>
<td>31</td>
<td>1,032</td>
<td>1,063</td>
</tr>
<tr>
<td>Public Administration</td>
<td>11</td>
<td>621</td>
<td>632</td>
</tr>
</tbody>
</table>

*Amputations per million employed.
**Fractures per million employees.
***Amputations and fractures per million employed.


# Table 10
## Amtrak Casualties
1982-1988

<table>
<thead>
<tr>
<th>Year</th>
<th>Killed</th>
<th>Injured</th>
<th>Casualty Rate&lt;sup&gt;2&lt;/sup&gt;</th>
<th>Casualty Rate&lt;sup&gt;3&lt;/sup&gt;</th>
<th>Lost Day Injury Cases</th>
</tr>
</thead>
<tbody>
<tr>
<td>1982</td>
<td>39</td>
<td>1,709</td>
<td>58.46</td>
<td>8.05</td>
<td>1,086</td>
</tr>
<tr>
<td>1983</td>
<td>36</td>
<td>1,749</td>
<td>61.98</td>
<td>8.23</td>
<td>832</td>
</tr>
<tr>
<td>1984</td>
<td>44</td>
<td>2,005</td>
<td>70.41</td>
<td>8.06</td>
<td>727</td>
</tr>
<tr>
<td>1985</td>
<td>19</td>
<td>1,963</td>
<td>68.27</td>
<td>8.79</td>
<td>1,048</td>
</tr>
<tr>
<td>1986</td>
<td>15</td>
<td>1,904</td>
<td>66.08</td>
<td>8.99</td>
<td>1,163</td>
</tr>
<tr>
<td>1987</td>
<td>101</td>
<td>2,072</td>
<td>66.66</td>
<td>7.60</td>
<td>1,176</td>
</tr>
<tr>
<td>1988</td>
<td>99</td>
<td>1,737</td>
<td>52.50</td>
<td>6.72</td>
<td>1,040</td>
</tr>
</tbody>
</table>

*Casualties are fatal and non-fatal casualties in Amtrak accidents, train incidents, and non-train incidents.

**Rate is frequency of fatalities and injuries per million train miles (involving on- and off-duty rail employees, passengers, trespassers, and non-trespassers).

***Rate is the frequency of fatalities, injuries, and illness per 200,000 man-hours (on-duty employees only).

### TABLE 11

**PASSENGER DEATH RATES BY MODE***

**1980-1987**

<table>
<thead>
<tr>
<th>Year</th>
<th>Buses</th>
<th>Passenger Trains</th>
<th>Scheduled Airlines</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980</td>
<td>.05</td>
<td>.04</td>
<td>.01</td>
</tr>
<tr>
<td>1981</td>
<td>.05</td>
<td>.04</td>
<td>.01</td>
</tr>
<tr>
<td>1982</td>
<td>.04</td>
<td>.09</td>
<td>.10</td>
</tr>
<tr>
<td>1983</td>
<td>.05</td>
<td>.04</td>
<td>.01</td>
</tr>
<tr>
<td>1984</td>
<td>.03</td>
<td>.11</td>
<td>.02</td>
</tr>
<tr>
<td>1985</td>
<td>.04</td>
<td>.03</td>
<td>.07</td>
</tr>
<tr>
<td>1986</td>
<td>.03</td>
<td>.03</td>
<td>.001</td>
</tr>
<tr>
<td>1987</td>
<td>.03</td>
<td>.13</td>
<td>.07</td>
</tr>
</tbody>
</table>

**Average** | **.04** | **.064** | **.036** |

*Death rate is deaths per 100 million passenger miles.

**SOURCE:** NATIONAL SAFETY COUNCIL, Accident Facts, 87 (1988):
FELA and Rail Safety: 
A Response to Babcock and Oldfather 
The Role of the Federal Employers’ Liability Act in Railroad Safety

DANIEL SAPHIRE*

INTRODUCTION

During the last session of Congress, the railroad industry urged Congress to repeal the Federal Employers’ Liability Act (FELA), the law that provides compensation to railroad employees who are injured on the "job," and put railroads under the jurisdiction of the no-fault, state workers’ compensation systems. In Babcock & Oldfather, The Role of the Federal Employers’ Liability Act in Railroad Safety (Babcock & Oldfather), the authors argue that FELA provides a greater incentive for railroads to provide a safe working environment than would the state workers’ compensation systems, the systems that cover virtually all other workers. To

* Mr. Saphire is an attorney with the Association of American Railroads, and is a graduate of the George Washington University National Law Center.


bolster their contention that FELA is appropriate for the railroad industry, they purport to demonstrate that the industry's safety record is poor.

In fact, the two major premises of Babcock & Oldfather are incorrect. The railroad industry's safety record is far better than Babcock & Oldfather suggests and is indeed a good and consistently improving one. Moreover, FELA does not provide a superior safety incentive to no-fault systems: if anything, it is inferior. This article will address the contentions made in Babcock & Oldfather about rail safety and FELA.

BACKGROUND

Some background on FELA is useful in analyzing the substance of Babcock & Oldfather. FELA was enacted in 1906 and, after the original statute was found unconstitutional, was reenacted in 1908. At the time of FELA's enactment, railroading was the nation's dominant industry. It played a key role in industrial expansion and employed nearly 1.7 million people. Railroading was also an extremely dangerous industry. In the year ending June 30, 1907, 4,534 railroad employees were killed and 87,644 were injured.

At that point in our nation's history, the law greatly favored employers. The common law of torts, which relied on concepts of negligence, provided the remedy for on-the-job injuries and was heavily stacked against employees. In order to receive compensation, not only did an employee have to prove the employer was negligent, but contributory negligence on the part of the employee or a co-worker completely barred recovery. Further, recovery if the worker was also denied if worker knew the inherent dangers of his job and assumed the risk of those dangers by accepting the employment. By the turn of the century, there was great pressure to move away from these rigid concepts and provide more equitable protection.

When Congress undertook to enact a compensation law for railroad employees, the experience of American jurisprudence was limited to the fault-based concept of negligence. Not surprisingly, Congress utilized that concept in enacting FELA. However, in what was, for the time, for-

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7. Id. at 99.
ward-thinking legislation, Congress replaced the doctrine of contributory negligence with one of comparative negligence. Thus, under FELA, an employee’s contributory negligence does not bar recovery, but rather, merely reduces the employee’s compensation in proportion to the employee’s negligence.10 Furthermore, if violation of a safety statute causes the injury, there is no reduction of the award regardless of the employee’s contributory negligence.11 As a result of amendments enacted in 1910, an employee may bring a FELA lawsuit, in either state or federal court, in any state where the railroad does business.12 In 1939, further amendments eliminated the assumption of the risk doctrine in all cases.13

Subsequent to FELA’s enactment, the individual states began adopting no-fault compensation systems as a means of providing compensation to workers injured on the job.14 The fundamental difference between workers’ compensation and traditional tort law is that under the former the right to compensation is based on the connection of the injury to employment, as opposed to the notion of fault.15 Today, every state in the nation has a comprehensive and well-established workers’ compensation law that covers virtually all employees other than railroad workers.16

With the passage of time, the Supreme Court has eroded the standards of negligence and causation, leaving FELA plaintiffs with a lesser burden in proving their case than in a traditional negligence action.17

11. Id.
14. Compensation systems designed to provide insurance-type benefits to injured workers had been adopted in Germany in 1884 and in England in 1897, but did not take a foothold in the United States until after FELA’s enactment. 1 LARSON, THE LAW OF WORKMEN’S COMPENSATION § 5.10 (1952) [hereinafter LARSON]. Limited workers’ compensation laws were enacted, and subsequently found unconstitutional, in Maryland in 1902, Franklin v. United Rys. & Elec. Co. of Baltimore, 2 Baltimore City Rep. 309 (1904), and in Montana in 1903. Cunningham v. Northwestern Improvement Co., 44 Mont. 180, 119 P. 554 (1911). The first compulsory coverage act of a general nature was enacted in New York in 1910 and applied to certain “hazardous employments.” This law was also found unconstitutional. Ives v. South Buffalo Ry., 201 N.Y. 271, 94 N.E. 431 (1911). New York enacted a new law in 1913 that was ultimately upheld by the Supreme Court, New York Central R.R. v. White, 243 U.S. 188, 197 (1917), as were similar laws in Iowa, Hawkins v. Bleakley, 243 U.S. 210 (1917) and Washington, Mountain Timber Co. v. Washington, 243 U.S. 219 (1917). By 1920 all but eight states had adopted a workers’ compensation law. In 1949, Mississippi became the last continental state to adopt such a law. After its admission to the union, Hawaii became the last state to adopt a workers’ compensation law. LARSON, supra at § 5.30.
15. LARSON, supra note 14, at § 2.10.
Rogers v. Missouri Pacific R. Co., the Court conceded that the negligence standard it applied in FELA cases was "significantly different from the ordinary common law negligence action."18 Although FELA has moved toward a no-fault law in terms of liability, tort concepts of damages remain unmodified.

While judicial interpretation of FELA has made it easier for employees to prevail, because some fault must still be proved, some injured workers, including some with severe injuries, get no compensation. Further, sometimes similarly situated workers receive vastly different amounts of compensation.19 This contrasts with the workers' compensation systems that are designed to compensate every employee who is injured on the job, without regard to fault and, within a given jurisdiction, to provide workers suffering similar losses with similar compensation.

Given that the legislatures of all fifty states, as well as Congress,20 have determined that no-fault systems are the appropriate means of providing compensation to injured workers within their jurisdiction, the ques-

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18. Rogers v. Missouri Pacific R. Co., 352 U.S. at 509. There is some evidence that the Court's move to liberalize FELA through judicial interpretation was motivated by its dissatisfaction with the use of a tort law to provide recompense for work related injuries. See also, Bailey v. Central Vermont Ry., 319 U.S. 350, 354 (1943), where the Court referred to FELA as "crude, archaic, and expensive as compared with the more modern systems of workmen's compensation." Stone v. New York C. & St. L. R.R., 344 U.S. 407 (1953), (Frankfurter, J., dissenting) reh'g denied, 345 U.S. 914 (1953) (referring to the use of a tort system to address workplace injuries as "a wholly inappropriate procedure." Stone, 344 U.S. at 410).

19. Two cases recently brought against the Southern Pacific Railroad by employees alleging hearing loss illustrate this point. In the first case, Koehler v. Southern Pacific Transportation Company, No. 88-2972-D (105th Jud. Dist. Tex. May 1990), a 55 year old employee received a net award of about $20,000 after the jury's award was reduced for contributory negligence and to repay unemployment payments received from the Railroad Retirement Board. Three months later, in Bernhard v. Southern Pacific Transportation Company, No. 87-5135-D (105th Jud. Dist. Tex. Aug. 1990), a case tried in the same Texas court, before the same judge and by the same lawyers, a 63 year employee asserting the same type of claim was awarded $340,000. Furthermore, the employee in the Koehler case missed two years of work, while the employee in Bernhard lost no time from the job and continues to work for the railroad. Letter from James L. Walker, counsel for Southern Pacific to Daniel Saphire, counsel for Association of American Railroads (November 15, 1990) (discussing verdicts in Koehler and Bernhard cases).

tion persists as to why one industry continues to be covered by a fault-based system like FELA. Indeed, there are numerous reasons why FELA is an inappropriate means of accomplishing the goals of a workplace compensation system, discussion of which is beyond the scope of this article. Certainly, retention of FELA cannot be supported on a safety rationale.

**RAILROAD SAFETY TRENDS**

Babcock & Oldfather focuses on the relation between FELA and rail safety and attempts to establish a link. As a prelude to this argument, the authors attempt to demonstrate that the railroad industry in unusually hazardous, and, presumably, therefore in need of the added safety incentive allegedly provided by FELA.

Though railroad employment is not without hazards, as is work in all heavy industries, the contention that it is unusually dangerous is not supported by the facts. In a discussion of railroad safety trends, Babcock & Oldfather offers a plethora of data on rail accidents, injuries and fatalities. While suggesting that this review of safety trends is "instructive," little insight about rail safety is provided. For the period 1982-1988, Babcock & Oldfather merely concludes that with respect to on-duty employee fatality rates "there is no consistent trend" and that on-duty employee injury rates "displayed no predictable trend."

Moreover, some of the data presented in Babcock & Oldfather are incorrect. For example, for the period 1978-1988, it overstates, by 214, the number of railroad employees killed on the job, and overstates by 118,917 the number of on-the-job injuries.

Finally, Babcock & Oldfather includes data relating to injuries to rail

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22. Id. The real story with respect to railroad safety trends is the significant improvement experienced since 1980, the year the industry was partially deregulated by the Staggers Rail Act, Pub. L. No. 96-488, 94 Stat. 1895 (1980). Deregulation greatly improved the financial situation of the railroad industry and facilitated increased investment in safety related maintenance. Although employee casualty rates undergo year to year fluctuations, the data shows that there have been marked improvements since enactment of Staggers. For the five year period prior to enactment of Staggers, 1976-1980, the average annual employee injury rate, per million man hours, was 58.63, and the fatality rate was 0.1016. For the five years from 1985 through 1989, the injury rate averaged 37.78, and the fatality rate 0.0798. Federal Railroad Administration Accident/Incident Bulletin Calendar Year 1989, 5 (Table 1 and 17, Table 9 (1990)); Calendar Year 1983, 3 (Table 1 and 15, Table 9 (1984)); Calendar Year 1981, 3 (Table 11 and 15-16, figures 10-14 (1982)).

23. Babcock & Oldfather, supra note 21, states that "[b]etween 1978 and 1988, 988 railroad on duty employees were killed and 551,657 injured." The actual numbers were 784 and 432,740, respectively. Federal Railroad Administration, Accident/Incident Bulletin Calendar Year 1988, 17 (Table 9 (1989)), and Calendar Year 1983, 15 (Table 9 (1984)).
passengers and other non-employees. However, only employees of a railroad may seek compensation under FELA. Therefore, in the context of evaluation of a system designed to compensate railroad employees, non-employee injuries are not relevant to the issue at hand.\(^{24}\)

After several pages of discussion of Federal Railroad Administration data, Babcock & Oldfather suggests that this data may be unreliable.\(^{25}\) They base this assertion on a General Accounting Office report released in 1989.\(^{26}\) Analysis of the GAO report does not support the conclusion that railroad accidents and injuries are substantially underreported or inaccurate. The GAO's conclusions result primarily from its lack of understanding of the FRA reporting requirements and methodological errors in sample selection and extrapolation.

For example, the GAO conclusion that railroads underreported the total number of lost workday stems from its failure to consider all the relevant documents. Railroads are required to report lost time injuries at the end of the month in which the injury occurred. If the employee has not returned to work at the time the monthly report is filed, the railroad must estimate the number of days the employee will remain off the job. If the employee remains off the job longer than estimated, those additional days are reported to the FRA in a year-end summary. GAO did not review or acknowledge the year-end reports and, as a result, based its conclusion about lost workday reporting only on the railroads' preliminary reports. This failure largely accounts for GAO's finding in the area of lost workdays.\(^{27}\)

**RAILROAD SAFETY COMPARED TO OTHER INDUSTRIES**

Babcock & Oldfather goes on to compare the safety record of the railroad industry with that of other industries. In an effort to portray the railroad industry as unusually dangerous, the authors consistently compare it with light industry and white collar jobs. This proves only the obvious: that working in a heavy industry is more hazardous than sitting behind a desk. In order to make a meaningful comparison of the dangers of a heavy industry like rail, logic and fairness call for comparisons with

\(^{24}\) See infra note 37 and accompanying text.

\(^{25}\) Babcock & Oldfather, supra note 21.


\(^{27}\) In addition, the GAO findings on unreported injuries is exaggerated by the fact that GAO used an improper method of calculation. It is suggested that there was a 12 percent underreporting of injuries. This percentage was derived by dividing the number of unreported injuries found reportable (61) by the number of unreported injuries reviewed (520). The more appropriate percentage would have been the number of unreported injuries found reportable by the total number of reportable injuries (932) in the sample. Thus the underreporting of injuries on the segments of the railroads audited was more in the order of 6 percent.
other heavy industries. When such a comparison is made, the rail industry is not unusually unsafe, a conclusion that is supported by the data presented in Babcock & Oldfather.

Referring to Table Six (an attachment Babcock & Oldfather), which contains data on lost workdays in nine major sectors of the economy, the article states that for the 1975-1987 period "[o]n the average, the railroad injury rate was 44.6% higher than the rate for all private sector industries." In fact, Table Six also shows that over that entire period, the railroad injury rate was consistently and significantly lower than that of the mining and construction industries. For the most recent five year period, the rail industry rate also was lower than that of the agricultural sector, and was comparable to that of the manufacturing sector. The sectors that fare better than the railroad industry are the non-heavy industries: wholesale trade, retail trade, finance, insurance and real estate, and services.

Based on data contained in Table Seven, Babcock & Oldfather asserts that "the railroad transportation injury rate is 161.7% greater than the rate for the total economy." This presentation is very misleading. According to Table Seven, the railroad industry experienced 157 total lost work days per 100 full time employees, compared to 60 for all industries, 49 for mining, 71 for construction and 58 for manufacturing. The source of this data is a table on pp. 44-45 of the National Safety Council, Accident Facts (1988 edition). This clearly states that "[t]hese rates should not be interpreted as representative of the industries listed." In fact, this particular table in Accident Facts is derived only from reports on National Safety Council members participating in the Occupational Safety/Health Award program. However, if one consults the table in Accident Facts which is based on data compiled by the United States Department of Labor's Bureau of Labor Statistics (BLS), a more comprehensive survey, it is clear that in comparison to other industries, the railroad industry's lost workday rate is far better than suggested in Babcock & Oldfather. In contrast to the limited and unrepresentative data contained in Table Seven of Babcock & Oldfather, the BLS data shows that the railroad lost work day rate is lower than the rate for mining; construction; manufacturing; agriculture, forestry and fishing; and transportation and public utilities.

29. For the period from 1983 through 1987, the average rate of total lost work days per 100 full time workers in the railroad industry was 84.82; in the agricultural sector it was 91.58; and in manufacturing it was 81.10. Babcock & Oldfather, supra note 21, at Table 6.
32. Id.
33. Id. at 42-43. The total lost workday rate for rail transportation in 1987 was 88.3, compared to 144.0 for mining, 135.8 for construction, 95.5 for manufacturing, 94.1 for agriculture,
Tables A and B of this article compare 1987 and 1988 injury and lost workday rates for the same industrial groups as does Table Seven of Babcock & Oldfather using BLS data. This data shows that the railroad industry falls near the middle in terms of occupational hazards. Clearly, they dispel any notion that railroad work is unusually hazardous.

Babcock & Oldfather argue that the rate of severe injuries in the railroad industry is excessively high. Based on data from the year 1983, it states that the amputation rate "is 58% greater than in the economy as a whole."34 It also states the rail industry has a fracture rate of 114% greater than the economy as a whole.35 Table Nine (the source of these statements) reveals that the three other heavy industries listed—mining, manufacturing and construction—all had higher amputation rates than railroading. And, with respect to fractures, the rates for the mining and construction industries were higher.

THE SAFETY IMPACT ON NON-EMPLOYEES

Babcock & Oldfather goes on to address the safety record of Amtrak, the nation's only intercity passenger railroad. This section does little to further the debate about FELA, as the data on fatalities and injuries include non-employees as well as employees. In fact, the vast majority of the fatalities are to non-employees. (For example, of 99 deaths reported in Table Ten to have resulted from Amtrak operations in 1988, none were to on-duty employees; of 101 deaths in 1987, three were to on-duty employees.)36

In the context of FELA, analysis of casualties to non-employees is simply not relevant. FELA covers only employees. Non-employees injured in an Amtrak accident (or an accident involving any railroad) may not sue under FELA. Instead, they would have a remedy under state tort law, through which they would be compensated if the railroad was at fault. If FELA was replaced with the state workers' compensation systems, the rights and remedies available to non-employees would be unaffected. So, to the extent that the obligation to respond in damages provides an economic incentive for railroads to operate safely, that obligation with respect to non-employees would remain completely intact after a switch to workers' compensation.37
Babcock & Oldfather also raises the specter of rail accidents involving hazardous materials. In point of fact, the railroad industry's record with respect to the transportation of hazardous materials is good. From 1981 through 1989, there were no deaths attributable to the transportation of hazardous materials by rail, and an average of only 68 injuries annually.

Once again, however, this issue is not relevant to a debate on the merits of FELA. If a railroad mishap involving hazardous materials caused injury to members of the general public, FELA would impose no financial penalty on the railroad. However, the railroad would be subject to serious financial accountability as a result of other laws, in addition to bearing the high costs of clean-up and loss of lading and equipment damage. It is simply erroneous to imply that but for FELA, railroads would have little incentive to consider the consequences of their transportation of hazardous materials.

In sum, the data presented in Babcock & Oldfather completely fail to make the case that the railroad industry is unusually dangerous. The only conclusions that can be drawn from the data presented in Babcock & Oldfather are that there is some degree of danger in railroad work; that it tends to be more hazardous than light industry jobs; and that it is less hazardous than many other occupations in heavy industry. None of this is startling.

SAFETY INCENTIVES

The second prong of Babcock & Oldfather's argument is that FELA provides more of an incentive to prevent injuries than does workers' compensation because the former is the more costly system. The railroads readily admit that FELA is a more costly system than is workers' compensation. However, the conclusion that this results in greater safety incen-

39. U.S. Department of Transportation, Research and Special Programs Administration, Annual Report on Hazardous Materials Transportation: Calendar Year 1989 Exhibit 1. In contrast to the rail industry's record, during the 1981-1989 period there were 113 deaths attributed to transportation of hazardous materials by highway, and an average of 196 injuries annually. Id.
40. FELA Hearings, supra note 2, at 48. To be sure, FELA is more costly than workers' compensation. However, it is also the case that a substantial amount of the total monies ex-
tives is simplistic in that it assumes that there are no other aspects of the two systems, or external factors, that affect industrial safety. In fact, there are many aspects of FELA, aside from costs, that cause it to be a disincentive to safety.41

To support the theory that FELA creates stronger safety incentives than workers' compensation, Babcock & Oldfather offers six FELA cases. The article claims that in each case the injured worker received far more under FELA than would have been available under workers' compensation. With respect to some of the cases, the article asserts that as a result of the large FELA award, the railroad subsequently made safety related changes to its operation.42

This evidence is anecdotal, at best. Further, it is often vague, and provides no bases with which to judge the validity of the representation made about the consequences of the cases. For example, with respect to Barrett v. Conrail, it is stated that "a substantial settlement was reached" that "was much higher than would have been possible under workers' compensation."43 There is no mention of how much was actually awarded, or how the amount that would have been payable under workers' compensation was ascertained, let alone what it would have been or even which state's law would have applied. With respect to Barker v. Conrail, it is asserted that "[a]s a consequence of the settlement made in this case, working conditions for train dispatchers improved significantly."44 No evidence is offered to show that any putative change in working conditions was in any way related to the (unquantified) settlement of this case, or any other.

The sole source cited to support the conclusions proffered about the six FELA cases is a document published by the Illinois Public Action Council entitled Railroading the Public Safety (Railroading). On review, it becomes apparent that the case summaries provided in Babcock & Oldfather are lifted directly, and practically verbatim, from that document, calling into question whether the authors have any familiarity with these cases. Further, Railroading provides no citations to any of the cases, making it difficult to check the accuracy of any of its assertions. Moreover, at a hearing before the United States Senate it was revealed that Railroading was funded by lawyers who bring FELA lawsuits against the railroads.45 This revelation was hardly surprising in that the FELA bar

41. See infra pp. 711-712.
42. Babcock & Oldfather, supra note 21.
43. Id.
44. Id.
45. See Hearings to Receive Testimony on the Federal Employers' Liability Act in Relation to
reaps substantial rewards from the system, and would be the biggest losers were a switch made to workers’ compensation.46

Babcock & Oldfather fails to offer any compelling evidence that FELA provides an incentive for a safer working environment. Empirical data on the relative effects of fault-based and no-fault compensation systems on safety is sparse.47 However, the experience of the industry suggests that FELA may very well present obstacles to optimizing workplace safety.

Because the employee’s right to be compensated for injuries is conditioned on showing the railroad was at fault, and because, conversely, the railroad can eliminate or reduce its liability by showing that the employee’s negligence contributed to the injury, both parties have an economic incentive to place the blame for accidents on the other. This provides motivation to obscure the true causes of workplace accidents, and thus hinder their objective investigation. As a result, effective modifications of workplace procedures and equipment may be delayed or prevented.

This result was underscored by Amtrak Chairman, W. Graham Claytor, Jr. at a 1988 hearing before the Senate Surface Transportation Subcommittee. Chairman Claytor testified about Amtrak’s efforts to improve workplace safety through the use of safety and accident prevention committees made up of employee and management representatives. These committees are responsible for monitoring compliance with safety regulations and investigating accidents. Chairman Claytor pointed out that FELA places limits on the effectiveness of these committees in accomplishing their goals:

A management member of such a committee, looking out for the department’s or company’s budget, may be inclined to place blame for the accident on employee error, while a labor member of the committee, realizing


46. According to data compiled by the Association of American Railroads (AAR), FELA lawyers collected approximately $150 million in fees out of FELA judgments and settlements in 1988. Association of American Railroads, Report of Claim & Litigation Experience for 1988 3-6 (1989) (on file with the author, Association of American Railroads, 50 F Street, NW, Washington, D.C. 20001). Lawyers were involved in cases accounting for 32 percent of the dollar payout of $811 million in 1988. Assuming that the lawyer took no more than 25 percent of the award as a contingency fee, a conservative estimate, total fees of $148 million were realized by the FELA bar. In commenting on the possibility of replacing FELA with workers’ compensation, one FELA lawyer candidly admitted that “[t]he bottom line is that it [would] take away big verdicts and big attorneys fees.” Himmelstein, Railroads Find Fault in Liability Act, LEGAL TIMES, July 11, 1988, at 6, col. 4.

47. At least one study indicates that injury rates decline when fault-based systems are replaced with strict liability systems. Chelius, Liability for Industrial Accidents: A Comparison of Negligence and Strict Liability Systems, 5 J. LEGAL STUDIES 293-309 (1976).
that attributing fault to the employee may result in no compensation whatsoever for the injured employee, may be just as inclined to fault the corporation. As a result, the critically important task of learning from past accidents to prevent future ones is inherently undermined and necessarily deficient. I believe that any system that encourages this result is bad public policy.\textsuperscript{48}

This aspect of FELA is not lost on rail employees. A book purporting to advise railroad employees of their rights under FELA, recommends that when filling out an accident report, rather than attempting to answer the question “what could have been done to prevent the accident,” the employee merely respond that “the full extent of the carrier’s negligence is unknown at this time.”\textsuperscript{49} In response to the question, “describe how the accident happened” it is suggested that the employee “says as little as possible.”\textsuperscript{50} Under a no-fault system, there would be no reason to follow such advice, as the circumstances of the accident would not affect the employee’s right to compensation.

\textbf{CONCLUSION}

The question of whether FELA should be repealed will be debated in Congress in the coming months. The railroad industry believes that there is no justification to retain an outdated law like FELA, that exist essentially as a result of an historic anomaly. There is already growing support for this position.\textsuperscript{51} Perhaps as a result of the paucity of arguments in support of FELA, some have asserted that it provides a significant incentive for rail safety and should be retained for that reason. This is an argument with emotional appeal but, upon analysis, no factual basis. Public policy makers should see the safety issue for what it is, a red herring, and move quickly to bring the railroad industry into the twentieth century in the area of employer liability.

\textsuperscript{48} Amtrak Hearings, supra note 45, at 39 (statement of W. Graham Claytor, Jr., Chairman, Amtrak).

\textsuperscript{49} J. Blount & E. Dvorak, JUSTICE FOR THE INJURED RAILROAD WORKER 3 (1987).

\textsuperscript{50} Id.

\textsuperscript{51} The Secretary of Transportation has called for legislation to “[r]epeal the Federal Employers’ Liability Act and bring Federal treatment of railroads into conformity with treatment of other modes.” U.S. Department of Transportation, MOVING AMERICA; NEW DIRECTIONS, NEW OPPORTUNITIES: A STATEMENT OF NATIONAL TRANSPORTATION POLICY STRATEGIES FOR ACTION 120 (February 1990). The Federal Courts Study Committee, a committee established by Congress and appointed by the Chief Justice to recommend ways to improve the federal court system, recommended that FELA be repealed and rail workers’ be put under the jurisdiction of the state workers’ compensation systems. REPORT OF THE FEDERAL COURTS STUDY COMMITTEE 62-63 (April 1990).
**TABLE A**

**OCCUPATIONAL INJURY AND ILLNESS RATES, 1987**

<table>
<thead>
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Rates are per 100 full-time workers


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**TABLE B**

**OCCUPATIONAL INJURY AND ILLNESS RATES, 1988**

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Rates are per 100 full-time workers

Volume 19, issue 2 of the Transportation Law Journal includes two articles on the topic of International Transportation Law. The Denver Journal of International Law and Policy in conjunction with the Transportation Law Journal solicited various articles from international legal scholars and practitioners for our joint symposium issue. We have selected these two articles for publication because they represent both the public and private sides of International Transportation Law.

The article written by Werner Ebke and George Wenglorz provides an in depth look at the European Community's liberalization of air transportation. In stark contrast, Dean Alexander has written a timely piece on maritime terrorism and the possible civil remedies which may be sought by individuals against the terrorists and the maritime carriers.

These articles serve to remind us of the importance of global transport and the legal issues involved, now and into the future.

MATTHEW W. SANIDAS
DANIEL S. WITTENBERG
Symposium Editors
Special Topic—International Transportation Law

Liberalizing Scheduled Air Transport Within the European Community: From the First Phase to the Second and Beyond

WERNER F. EBKE*
GEORG W. WENGLORZ**

I. INTRODUCTION

During the founding years of the European Community,¹ the law and

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¹ Although the European Community ("EC" or "Community") is often thought of as a single entity, there are three legally independent Communities: the European Coal and Steel Community ("ECSC"), the European Economic Community ("EEC"), and the European Atomic Energy Community "Euratom". See Treaty Instituting the European Coal and Steel Community, Apr. 18, 1951, 261 U.N.T.S. 140 (1957); Treaty Establishing the European Economic Community, Mar. 25, 1957, 298 U.N.T.S. 11 (1958) [hereinafter EEC Treaty or Treaty]; Treaty Establishing the European Atomic Energy Community, Mar. 25, 1957, 298 U.N.T.S. 167 (1958). The Merger Treaty of 1965 did not merge the three Communities as such: rather, the Treaty instituted a single Commission ("EC Commission" or "Commission") to replace the High Authority of the
policy of air transport was largely ignored. It was not until the end of the 1970's that the First Memorandum of the EC Commission on Air Transport brought about a change to this situation. This memorandum was the catalyst for the dialogue between the EC Commission, the EC Council, the European Parliament, and the Member States concerning the future development of civil aviation within the Community and beyond. The efforts were reinforced by the publication of the Second Memorandum of the EC Commission in 1984.

As a result of two decisions rendered by the European Court of Justice in 1985 and 1986 and the impetus provided by the Single European Act, there has been a considerable increase in legislative activity concerning air transport during the last few years. The Commission has

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2. For a detailed explanation of the reasons, see J. BASEDOW, WETTBEWERB AUF DEN VERKEHRSMARKTEN 157-63 (1989).


proved itself in this respect, to be a major force behind the liberalization movement. The Council of Ministers only recently came to a decision concerning the important question of the Second Phase of the liberalization of scheduled air transport. The pertinent regulations became effective on November 1, 1990, and they represent a major step towards entry into the Single European Market on January 1, 1993. The purpose of this article is to present and critically evaluate the current state of scheduled air transport deregulation within the EC. The analysis will focus primarily upon the legislative measures promulgated by the Council of Ministers concerning the Second Phase of air transport liberalization which were published in August 1990.

In order to evaluate the regulations enacted by the Council, it is necessary to throw some light on the general legal framework of international air transport. The article will then take a closer look at the pertinent provisions of the EEC Treaty. Finally, the historical process of the liberalization of air transport within the EC and the prospects for air transport deregulation will be analyzed.

II. THE LEGAL FRAMEWORK OF WORLD AIR TRANSPORTATION

The present world air transport system is based upon the Convention on International Civil Aviation, commonly referred to as the Chicago Convention. 10

A. THE CHICAGO CONVENTION


shortly before the end of World War II when it became apparent that a new legal framework for world air transport would be necessary.\textsuperscript{11} The Chicago Convention went into effect on April 4, 1947.\textsuperscript{12} One of the basic principles of the Convention is that of national air sovereignty. According to this principle, every nation has complete and exclusive sovereignty over the airspace above its territory.\textsuperscript{13} As a result, every nation has the right to decide upon the distribution of air transport rights to and from its territory on a case by case basis.

Initially, the parties to the Chicago Convention intended to establish a multilateral system of transport rights. Due to the uncompromising positions of the United States which took a very liberal view, and the United Kingdom which followed a protectionist approach, a comprehensive agreement could not be reached.\textsuperscript{14} Agreement was only reached with respect to two of the eight "Freedoms of the Air."\textsuperscript{15} The two freedoms agreed upon are commonly known as the "technical freedoms." The failure to achieve an all-encompassing multilateral agreement concerning air transport rights at the Chicago conference led, in the following years, to the system of bilateral agreements that still forms the legal basis of the current international air transport system.

\textbf{B. Bilateral Agreements}

Over the years, a tight international network of bilateral air transport agreements concerning scheduled air services has developed between

\begin{itemize}
\item \textsuperscript{11} See A. Kark, \textit{Die Liberalisierung der Europäischen Zivilluftfahrt und das Wettbewerbssrecht der Europäischen Gemeinschaft} 73 (1989).
\item \textsuperscript{12} See Chicago Convention, supra note 10, art. 91. For a list of countries that have signed the Chicago Convention, see S. Rosenfield, \textit{The Regulation of International Commercial Aviation}, Booklet 5, 52-54 (1984).
\item \textsuperscript{13} See Chicago Convention, supra note 10, art. 1.
\item \textsuperscript{14} For details, see A. Kark, supra note 11, at 73-75; M. Dautzenberg, \textit{Der britisch/amerikanische Kartell-Rechtsstreit um die IATA-Flugtarife aus dem Blickwinkel des Protection of Trading Interests Act} 70-72 (1987).
\item \textsuperscript{15} The First through the Fifth Freedoms are defined in article 1(1) of the International Air Transport Agreement, an appendix to the Chicago Convention, supra at 10. The Sixth through the Eighth Freedoms are combinations of the Third through the Fifth Freedoms. For a detailed discussion of the First through the Eighth Freedoms, see S. Rosenfield, supra at 12, Booklet 3, at 3-6. The First through Fifth Freedoms of the Air read as follows:
\begin{itemize}
\item \textbf{First Freedom:} The right to fly across the territory of a foreign country without landing.
\item \textbf{Second Freedom:} The right to land for non-commercial purposes (technical operations relating to the aircraft, the crew, refueling, etc.) in the territory of a foreign country.
\item \textbf{Third Freedom:} The right to fly from the country of registration to another country and put down, in the territory of the other country, passengers, freight, or mail taken aboard in the country of registration.
\item \textbf{Fourth Freedom:} The right to fly from a foreign country with passengers, cargo, or mail loaded in that foreign country, to the country of its registration.
\item \textbf{Fifth Freedom:} The right to transport passengers, mail, or cargo between another contracting state and a third country.
\end{itemize}
\end{itemize}
almost all countries of the world. The agreement between the United States and the United Kingdom that was negotiated in Bermuda in early 1946 ("Bermuda I Agreement"), served as a model for the majority of such bilateral agreements. The bilateral air transport agreements of the Federal Republic of Germany were, and still are, based upon the German Model Draft of a Bilateral Air Transport Agreement, which in turn is based upon the Bermuda I Agreement. Almost all of the agreements based upon the Bermuda I Agreement contain the following provisions:

1. The distribution of air transport rights with respect to the First, Second, Third, and Fourth Freedoms. In some bilateral agreements, the Fifth Freedom is also granted;
2. The determination of particular flight routes;
3. The number of air carriers permitted to make use of the transport rights mentioned above (single or multiple designation);
4. Determination of capacity (size of aircraft and frequency of service);
5. The tariff approval process, usually including a double approval clause.

Bilateral air transport agreements based upon such provisions thus regulate market access, the number and scope of air transport rights, capacity, and tariffs. Almost all bilateral agreements considerably restricted competition between airlines well into the 1980's, and some of them continue to do so to this day. Specifically, a number of significant aspects of market structure were excluded from the forces of competition. This is also true with respect to most bilateral air transport agreements between Member States of the EC.

### C. TARIFF AGREEMENTS

The network of bilateral air transport agreements has been supplemented by tariff agreements between airlines. These tariff agreements

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16. There are approximately 2,500 bilateral air transport agreements today. See also L. WEBER, DIE ZIVILLUFTFAHRT IM EUROPÄISCHEN GEMEINSCHAFTSRECHT 47 (1981).
18. See German Model Draft of a Bilateral Air Transport Agreement, reprinted in D. KLOSTER-HARZ, DIE LUFTVERKEHRSABKOMMEN DER BUNDESREPUBLIK DEUTSCHLAND Appendix I (1976) [hereinafter Model Agreement].
19. Id. art. 2(1)(c).
20. Id. art. 8(3).
21. Id. art. 2(2).
22. Id. art. 3(1).
23. Id. art. 8(4).
24. Id. art. 10(1).
25. See A. KARK, supra note 11, at 77-78.
were, and still are, negotiated within the International Air Transport Association ("IATA"). As a general rule, tariffs are set at IATA conferences and then approved by national governments. Such tariff agreements are reinforced by both EC law and the laws of EC Member States.

1. **EC LAW**

Under article 85(3) of the EEC Treaty, tariff agreements may be exempt from European antitrust laws. Article 85(3) of the EEC Treaty has been implemented by two EC Regulations. Under these Regulations, tariff "consultations" between airlines are permitted to the extent that the various conditions of article 4 of Commission Regulation 2671/88 are met. Most importantly, article 4(1)(e) of this Regulation requires that

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27. See generally Bermuda I, supra note 17, Annex II h.

28. See EEC Treaty, supra at 1, art. 85(3) reads as follows:

1. The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings, and concerted practices which may affect trade between Member states and which have as their object or effect the prevention restriction or distortion of competition within the common market, and in particular those which:
   (a) directly or indirectly fix purchase or selling prices or any other trading conditions;
   (b) limit or control production, markets, technical development, or investment;
   (c) share markets or sources of supply;
   (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
   (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which by their nature or according to commercial usage, have no connection with the subject of such contracts.

2. Any agreements or decisions prohibited pursuant to this Article shall be automatically void.

3. The provisions of paragraph 1 may, however; be declared inapplicable in the case of:
   (a) any agreement or category of agreements between undertakings;
   (b) any decision or category of decisions by associations of undertakings;
   (c) any concerted practice or category of concerted practices which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:
      (a) impose on the undertakings concerted restrictions which are not indispensable to the attainment of these objectives;
      (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.


30. See Commission Regulation 2761/88, supra note 8, art. 4 that reads, in its pertinent part, as follows:

   1. The exemption concerning the holding of consultations on tariffs shall apply only if:
      (a) the consultations are solely intended to prepare jointly tariff proposals covering scheduled air fares to be paid by members of the public directly to a participating air carrier or to its authorized agents for carriage as passengers with their accompanying baggage on a scheduled service and the conditions under which those fares apply, in application of Article 4 of Directive 87/601/EEC:
      (b) the consultations only concern tariffs subject to approval by the aeronautical
tariff proposals resulting from such "consultations" not be binding.\(^{31}\)

Until 1978, IATA member airlines were legally bound to participate in IATA tariff coordination conferences and to adopt tariffs that were negotiated at such conferences.\(^{32}\) As a result of the 1978 "show cause order"\(^{33}\) of the Civil Aeronautics Board ("CAB") of the United States, the IATA regulations were changed. Beginning in 1979, member airlines were no longer required to participate in, nor to adopt tariffs agreed upon by the IATA conferences. Because of the non-binding tariff setting process within IATA, the participation of European carriers is consistent with the two Regulations aforementioned.\(^{34}\)

2. **GERMAN LAW**

Until December 31, 1989, tariff agreements among airlines were also exempt from Germany's antitrust laws. According to German law,\(^{35}\) the Antitrust Statute did not apply to contracts of companies dealing with the transportation of persons or goods, if the tariffs for the transport services had to be approved by a state agency.\(^{36}\) Under German law,\(^{37}\) airline tariffs must be approved by the Federal Department of Transportation (Bundesverkehrsministerium).\(^{38}\) Consequently, tariffs agreed upon at IATA conferences were exempt as a matter of law.

Effective January 1, 1990, however, this policy changed. Under the

\(^{31}\) See id. art. 4(1)(e).

\(^{32}\) See M. DAUTENBERG, supra note 14, at 80.

\(^{33}\) For details of the "show cause order," see P. BARLOW, AVIATION ANTITRUST 21-23 (1988).

\(^{34}\) See supra note 29 and accompanying text.


\(^{36}\) See id. art. 99(1).


\(^{38}\) See id. art. 21(1).
new law, contracts of airlines concerning interstate transportation with the EC are no longer subject to Germany's Antitrust Statute. The German legislature has thereby taken account of the fact that EC law takes priority over the laws of the Member States when air transportation involving at least two Member States is concerned. How the new law will affect air transport services rendered solely within Germany remains to be seen.

3. IMPLEMENTATION OF IATA TARIFF CONSULTATIONS

In order for a tariff that has been negotiated by participating airlines at an IATA conference to become effective in a given country, it is necessary that the tariff proposal be approved by the government of that country. In the past, such proposals have almost always been approved. Accordingly, IATA airlines may in fact be viewed as a price cartel.

D. POOLING AGREEMENTS

Bilateral air transport agreements are typically supplemented not only by tariff agreements but also by pooling agreements. Such agreements concern the financial or organizational cooperation of two or more airlines. Pooling agreements may contain a multitude of regulations. Very often they deal with the distribution of earnings from a particular flight route serviced by two or more airlines. In pooling agreements, airlines occasionally agree to restrict the number of flights on a particular route and to regulate the joint use of airport services. Pooling agreements, along with tariff agreements and bilateral agreements, have been the foundations upon which an almost completely regulated market has been built.

E. LIBERALIZATION TENDENCIES IN EUROPE

In the last ten years, there has been a tendency towards more liberal bilateral air transport agreements. In particular, since the 1980's, the British Government has negotiated procompetitive bilateral air transport agreements with Luxembourg, the Netherlands, Belgium, and the Federal

40. See id. art. 99(1), No. 1.
41. See Council Regulation 2342/90, supra note 9, art. 4(1). See also Luftverkehrsgesetz, supra note 37, art. 21(1).
42. A. Kark, supra note 11, at 86.
46. W. Schwenk, supra note 26, at 205.
Republic of Germany. These bilateral agreements were modeled after the Agreement between the United Kingdom and Luxembourg of March 1985. The Air Route Agreement provides for a dismantling of market access and capacity restrictions, as well as introducing the double disapproval procedure for tariffs. According to the double disapproval principle, a tariff proposed by an airline becomes effective unless the governments of both countries voice their disapproval within an agreed period of time. Each of the agreements between the United Kingdom and the aforementioned countries contain similar provisions.

While such bilateral agreements may be likely to further the liberalization process within the EC, they are unlikely to accomplish a complete liberalization of air transport, as not all Member States are prepared to agree to similar, let alone even more liberal measures. If the Single European Market is to become reality, a comprehensive air transport law applicable to all EC Member States in an absolute requirement. The regulations of the Council of Ministers that went into force on November 1, 1990, are an important step towards this goal.

III. THE EEC TREATY AND EUROPEAN AIR TRANSPORT POLICY

The EEC Treaty lays the foundations for a European air transport policy. According to the EEC Treaty, the establishment of a common market is the Community’s primary goal. The introduction of a common transport policy is expressly stated in the Treaty as one of the means of establishing a common market. In view of the important role that transport
services play in the process of integration of the economies of EC Member States, the EEC Treaty contains special provisions dealing with transport.\textsuperscript{54} Of these provisions, only one directly addresses air transport;\textsuperscript{55} the other provisions apply to road transport, railways, and inland waterways. Article 84(2) of the EEC Treaty grants the EC Council of Ministers the power to decide "whether, to what extent and by what procedure appropriate provisions may be laid down for sea and air transport."\textsuperscript{56} It was not until 1983 that the Council acted pursuant to the powers granted by article 84(2). This is due to the fact that individual Member States' views with respect to both the function of civil aviation and its implications for the European transport policy differed significantly, and still do today.\textsuperscript{57}

\textbf{A. The French Seamen's Case}

EC Member States and the EC Commission have long disagreed on whether or not the general provisions of the EEC Treaty, including the antitrust provisions of the Treaty, apply to air transport. The Commission has always taken the position that the Treaty's general provisions are applicable to air transport, even though the Treaty leaves the shaping of specific air transport rules and policies to the Council.\textsuperscript{58} France, on the other hand, was of the opinion that the general provisions of the EEC Treaty did not apply to air transport.\textsuperscript{59} The French government argued that under article 84(2) of the EEC Treaty, air transport, like sea transport, is regulated exclusively by the Council of Ministers.\textsuperscript{60} Prior to 1983, the Council had not, however, taken any action with regard to air transport.

In 1974, the European Court of Justice had an opportunity, in the French Seamen's case, to address the related issue of whether the general provisions of the EEC Treaty apply to sea transport.\textsuperscript{61} The case arose in connection with a French law requiring that "leading" positions abroad French ships be given to French citizens only. The EC Commis-
sion was of the opinion that the French law violated the EEC Treaty. Specifically, the Commission argued that the French law was contrary to the Treaty’s general provisions on the free movement of labor. In its decision the European Court of Justice confirmed the Commission’s view that the general provisions of the EEC Treaty apply to all transport services, including sea transport. The Court held that while they are not subject to the specific provisions of the EEC Treaty concerning transport services, air and sea transport services, like other transport services (i.e., road transport, railways, inland waterways), are subject to the general provisions of the EEC Treaty. Although it did not concern air transport, the Court’s decision provided an important signal for the integration of air transport within the Community.

B. AFTERMATH

Unfortunately, in the years following the Court’s decision in the French Seamen’s case, the Council used its powers under article 84(2) of the EEC Treaty with a great deal of reluctance. Many of the proposals of the EC Commission concerning the establishment of a competitive air transport system amounted to nothing, or were postponed from one Council meeting to the next. The goal of a common air transport policy was not realized due to a lack of political will on the part of a majority of Member States. According to one commentator, air transport policy developed into “a dark chapter in the history of European integration.”

The European Parliament seemed to have agreed with this view. In 1983, the Parliament took the unusual step of taking the Council to court, under article 175 of the EEC Treaty, for its inactivity in the entire area of

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62. See EEC Treaty, supra note 1, arts. 48-51.
63. Id. arts. 74-83.
64. See Commission, [1974] Sig. at 371.
69. See EEC Treaty, supra note 1, art. 175 which reads as follows:

Should the Council or the Commission, in infringement of this Treaty, fail to act, the Member States and the other institutions of the Community may bring an action before the Court of Justice to have the infringement established.

The action shall be admissible only if the institution concerned has first been called upon to act. If, within two months of being so called upon, the institution concerned has not defined its position, the action may be brought within a further period of two months.

Any natural or legal person may, under the condition laid down in the preceding paragraphs, complain to the Court of Justice that an institution of the Community has failed to address to that person any act other than a recommendation or an opinion.
transport policy. The Parliament argued that the Council had failed to introduce a common transport policy, or to provide a binding framework for such a policy, and that the Council had thereby violated the EEC Treaty.\(^70\)

**C. TRANSPORT POLICY DECISION**

In 1985, the European Court of Justice held partly in favor of the European Parliament.\(^71\) The Court opined that the EEC Treaty’s provisions that generally required a common transport policy within the Community, were not sufficiently concrete to be actionable.\(^72\) The Court determined that articles 75(1)(a) and (b) of the EEC Treaty were adequately clear to require the Council of Ministers to take appropriate actions to implement a policy of intra-community transportation and to regulate cabotage rights.\(^73\) According to the Court, the failure of the Council to act in accordance with articles 75(1)(a) and (b) of the EEC Treaty constituted an inactivity amounting to a violation of the Treaty.\(^74\) The Court set no deadline by which time the Council had to meet its obligations under these articles; rather, the Court granted the Council a “reasonable period of time” to take appropriate actions.\(^75\)

At first glance, the Court’s decision may appear to be of relatively little importance inasmuch as it only reiterated the principle of freedom of trade in services provided for in the EEC Treaty. The decision had, however, far-reaching political implications. Only a few months after the Court’s decision, the Council of Ministers presented a Master Plan Con-

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\(^70\) The Parliament claimed that the Council’s failure to act constituted a violation of EEC Treaty, *supra* note 1, art. 3(e), art. 61, art. 74, art. 75, and art. 84, Art. 61 reads, in its pertinent part, as follows:

1. Freedom to provide services in the field of transport shall be governed by the provisions of the Title relating to transport.

Article 74 reads as follows:

The objectives of this Treaty shall, in matters governed by this Title, be pursued by Member States within the framework of a common transport policy.

Article 75 reads, in its pertinent part, as follows:

1. For the purpose of implementing Art. 74, and taking into account the distinctive features of transport, the Council shall, acting unanimously until the end of the second stage and by qualified majority thereafter, lay down, on a proposal from the Commission and after consulting the Economic and Social Committee and the Assembly;

   (a) common rules applicable to international transport to or from the territory of a Member State or passing across the territory of one or more Member States;

   (b) the conditions under which non-resident carriers may operate transport services within a Member State.

\(^71\) European Parliament v. Council, Case 13/83, [1985] Sig. 1513. For a general discussion of this case, see P. DAGTROGLOU, AIR TRANSPORT AND THE EUROPEAN COMMUNITY 50-75 (1989).

\(^72\) *European Parliament*, [1985] Sig. at 1596-1600.

\(^73\) Id. at 1600-1601.

\(^74\) Id. at 1600.

\(^75\) Id.
cerning Transport Policy that, among other areas of transport services, affected air transport. Additionally, the Council set a seven year time limit within which substantial progress in regard to the freedom of trade in services had to be accomplished. The Council also accepted the proposals made in the EC Commission's White Paper on the Completion of the Internal Market. The White Paper contained a detailed plan of actions for the integration of the transportation markets. At roughly the same time, the governments of the EC Member States arrived at an agreement concerning the Single European Act (the "SEA"). The SEA amended the EEC Treaty and provided the foundation for the Single European Market.

On the basis of these measures, the Council and the Commission of the EC have become very active in the field of air transportation. With its decisions in the French Seamen's case and the Transport Policy case, the European Court of Justice made a significant contribution to the establishment of European Community transport policy which should not be underestimated. These decisions helped accelerate the process of European integration towards a common market.

IV. THE DEVELOPMENT OF THE EC AIR TRANSPORT POLICY PRIOR TO DECEMBER 1987

The first major step towards the development of a common, liberalized air transport system within the European Community was taken by the Commission in 1979 with the publication of its First Memorandum.

A. THE FIRST MEMORANDUM

The First Memorandum was based upon a detailed analysis of EC air transport policies existing prior to 1979. On the basis of this analysis, the Memorandum set forth the short, intermediate, and long term objectives relating to a common air transport policy within the EC. It also proposed possible and desirable measures for effecting their implementation.

77. See Schrötter, supra note 68, at 84.
79. See SEA, supra at 7.
80. See, e.g., the measures concerning the First and Second Phase of air transport liberalization, supra notes 8-9 and accompanying text.
82. European Parliament, [1985] Sig. at 1513.
83. See First Memorandum, supra at 3.
84. See First Memorandum, supra note 3, at 20-26.
Most importantly, the Memorandum underscored the need for a change to the then existing market structures.

In the following years, the First Memorandum provoked a broad discussion of the proposed measures among all concerned, including airlines, the EC Commission, the EC Council, and the EC Member States.

B. **INTER-REGIONAL AIR SERVICES DIRECTIVE**

After intensive discussions, the EC Council, at the suggestion of the EC Commission, promulgated the first directive for the liberalization of air transport. The impact of this directive however, was limited. The directive applied only to international flights within the Community by aircraft with no more than 70 seats over a distance of at least 400 kilometers. In addition, the directive only pertained to flights into small airports (i.e., category II and III airports). As a result, the practical importance of the Council's first step towards air transport liberalization remained modest.

It was not until 1989, that the Inter-regional Air Services Directive was further liberalized. As a result of the 1989 amendments to the Directive, airlines were allowed to service routes under 400 kilometers. Furthermore, aircraft size restrictions were removed. Regarding this rather advanced step towards the aim of a deregulated framework for regional air transport services, the Council has adopted the Commission's attitude. This attitude, developed in recent years, is that regional air service between Member States is to be strongly promoted in order to take pressure off the large congested airports within the Community.

C. **THE SECOND MEMORANDUM**

In view of the world-wide crisis in civil aviation at the beginning of the 1980's and the increased competitive pressure upon both the airline and the aircraft industry, the EC Commission published a Second Memorandum on Civil Aviation. This Memorandum reflected the United States' experience with airline deregulation, which had its roots in the Airline De-
regulation Act of 1978. The Second Memorandum set forth the major features of a future common air transport policy for the EC. The Commission was primarily concerned with the regulation and creation of conditions for a competitive market for scheduled air transport. The Memorandum was aimed at a liberalization of the existing bilateral air transport agreements. The deregulation envisaged by the Second Memorandum included only the EC Member States. Air transport between EC Member States and third countries would be deregulated at a later date.

D. THE NOUVELLES FRONTIÈRES CASE

The Second Memorandum of the EC Commission and the decision of the European Court of Justice in the Transport Policy case increased pressure on the EC Council to take effective measures towards the liberalization of EC air transport. The discussions within the Council proved to be difficult and time consuming. It was the European Court of Justice that finally took the lead in the liberalization process. In April 1986, the Court handed down the single most important decision relating to the liberalization of EC air transport. The case, commonly known as the Nouvelles Frontières case, involved the issue of whether a travel agency registered in an EC Member State has the right to sell airline tickets at fares below the tariffs agreed upon by IATA-airlines and approved by the Member States’ government.

In its decision, the Court held that the Community’s antitrust laws, in particular articles 85 and 86 of the EEC Treaty, are as a general rule


94. See Second Memorandum, supra note 4, at 21-28.
95. See id. at 28-40.
96. See id. at 21.
99. For the text of the EEC Treaty, see supra note 1, art. 85. See also supra at 28.
100. See EEC Treaty, supra note 1, art. 86 that reads as follows: Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market in so far as it may affect trade between Member States. Such abuse may, in particular, consist in:
The Court, however, qualified its holding by stating that articles 85 and 86 of the EEC Treaty cannot be enforced directly by the Commission or the Member States until these provisions are implemented by secondary Community law, such as implementing regulations or directives (as required by article 87 of the EEC Treaty). Pointing to articles 88 and 89 of the EEC Treaty, the Court suggested that the Commission and the competent authorities of the Member

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(a) directly or indirectly imposing unfair purchase or selling prices or unfair trading conditions;
(b) limiting production, markets or technical development to the prejudice of consumers;
(c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
(d) making the conclusion of contacts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contacts.

102. See id. 1466-1470. EEC Treaty, supra note 1, art. 87 reads as follows:
1. Within three years of the entry into force of this Treaty the Council shall, acting unanimously on a proposal from the Commission and after consulting the Assembly, adopt any appropriate regulations or directives to give effect to the principles set out in Arts. 85 and 86.
If such provisions have not been adopted within the periods mentioned, they shall be laid down by the Council, acting by a qualified majority on a proposal from the Commission and after consulting the Assembly.
2. The regulations or directives referred to in paragraph 1 shall be designed, in particular:
(a) to ensure compliance with the prohibitions laid down in Art. 85(1) and in Art. 86 by making provision for fines and periodic penalty payments;
(b) to lay down detailed rules for the application of Art. 85(3), taking into account the need to ensure effective supervision on the one hand, and to simplify administration to the greatest possible extend on the other;
(c) to define, if needed be, in the various branches of the economy, the scope of the provisions of Arts. 85 and 86;
(d) to define the respective functions of the Commission and of the Court of Justice in applying the provisions laid down in this paragraph;
(e) to determine the relationship between national laws and the provisions contained in this Section or adopted pursuant to this Article.

103. EEC Treaty, supra note 1, art. 88 reads as follows:
Until the entry into force of the provisions adopted in pursuance of Art. 87, the authorities in Member States shall rule on the admissibility of agreements, decisions and concerted practices and on abuse of a dominant position in the common market in accordance with the law of their country and with the provisions of Art. 85, in particular paragraph 3, and of Art. 86.

104. EEC Treaty, supra note 1, art. 89 reads as follows:
1. Without prejudice to Art. 88, the Commission shall, as soon as it takes up in duties, ensure the application of the principles laid down in Arts. 85 and 86. On application by a Member State or on its own initiative, and in co-operation with the competent authorities in the Member States, who shall give it their assistance, the Commission shall investigate cases of suspected infringement of these principles. If it finds that there has been an infringement, it shall propose appropriate measures to bring it to an end.
2. If the infringement is not brought to an end, the Commission shall record such infringement of the principles in a reasoned decision. The Commission may publish its decision and authorize Member States to take the measures, the conditions and details of which it shall determine, needed to remedy the situation.
States take appropriate measures to enforce the general principles underlying articles 85 and 86 of the EEC Treaty.\textsuperscript{105} Citing its decision in the \textit{Bosch} case,\textsuperscript{106} the Court made it very clear that the enforcement procedure of articles 88 and 89 of the EEC Treaty is not capable of assuring complete compliance with articles 85 and 86 of the EEC Treaty.\textsuperscript{107}

Due to the limited applicability of articles 85 and 86 of the EEC Treaty, the Court's decision provides no answer to the question of whether IATA tariff agreements are in compliance with EC law. The Court's decision is also politely silent on the issue of whether or not Member States are in breach of the EEC Treaty when they approve tariffs agreed to at IATA conferences. Despite its limited holding, the Court's decision has had an immediate impact. In view of the Court's emphasis of the Commission's responsibilities under article 89 of the EEC Treaty, the Commission proceeded against ten major European airlines for violation of article 85 of the EEC Treaty.\textsuperscript{108} With the Commission's threat of a lawsuit against them looming ahead, the airlines eventually agreed, among other things, to bring their tariff, capacity, and pooling agreements into compliance with the EC antitrust laws.\textsuperscript{109}

\textbf{E. \textit{THE SINGLE EUROPEAN ACT}}

The decisive step towards the liberalization of scheduled air transport within the Community was finally brought about by the Single European Act, which went into effect on July 1, 1987.\textsuperscript{110} The Single European Act provides for the establishment of a Single European Market for air transport.\textsuperscript{111} Most importantly, decisions concerning the establishment of a single market for air transport no longer require unanimous voting by Member States; rather, measures can now be taken by a majority of votes.\textsuperscript{112}

June 1987, after intensive discussions, the Council agreed upon a package of measures for the liberalization of scheduled air transport.\textsuperscript{113} The implementation of these measures was delayed by a veto of the

\begin{footnotesize}
\textsuperscript{105} Ministère Public v. Asjes, [1986] Sig. at 1469.
\textsuperscript{107} Ministères Public v. Asjes, [1986] Sig. at 1469.
\textsuperscript{108} These airlines included Air France, Aer Lingus, Alitalia, British Airways, British Caledonian, KLM, Deutsche Lufthansa, Olympic, Sabena, and SAS.
\textsuperscript{110} See SEA, supra at 7.
\textsuperscript{111} See id. art. 13.
\textsuperscript{112} Id. art. 16.
\textsuperscript{113} See Dempsey, supra note 8, at 671-72.
\end{footnotesize}
Spanish government. The Spanish government was unwilling to accept the application of the EC liberalization measures to Gibraltar airport, as Spain still contests British sovereignty over Gibraltar. The concerns of the Spanish government were overcome by the end of 1987. The Council's compromise cleared the way for the First Phase of the process of liberalizing air transport within the EC.

V. THE FIRST PHASE

In December 1987, the Council took a number of measures toward the liberalization of air transport that are commonly referred to as the First Package of Liberalization. This Package consists of the following: a Council Directive on tariffs, a Council Decision concerning capacity sharing and market access, a Council Regulation concerning the application of the EC antitrust laws to the air transport sector, and a Council Regulation concerning exemptions from EC antitrust laws.

The measures mentioned are applicable only to flights between EC Member States. They do not apply to domestic flights within a given Member State, nor do they apply to flights between a Member State and third countries. Rights and obligations of Member States vis-à-vis their airlines are not subject to the First Package. The regulation of domestic air transport remains the responsibility of each Member State. The First Package affects the Member States' sovereign rights with respect to market access for intracommunity flights, capacity sharing, and tariff approval. To illustrate the significance of the First Package, we shall take a closer look at the various provisions.

A. ANTITRUST REGULATIONS

For the first time in the history of the European Community, the Council Regulation (EEC) 3975/87 effected the application of articles 85 and 86 of the EEC Treaty to airline companies in regards to flights between EC airports. The Regulation also grants the EC Commission power to investigate and impose sanctions on both airlines and Member States for violations of articles 85 and 86 of the EEC Treaty.

According to Council Regulation (EEC) 3976/87, the Commission may, by means of a further regulation, exempt from EC antitrust laws cer-

114. Id. at 672.
115. See supra at 8.
116. See, e.g., Council Regulation (EEC) 3975/87, supra note 8, art. 1(2).
117. Id.
118. Id. art. 1.
119. Id. arts. 3-6.
120. See Council Regulation (EEC) 3976/87, supra at 8.
tain categories of agreements and concerted practices of airlines. Such group exemptions are generally permitted under article 85(3) of the EEC Treaty. Group exemptions may be subject to certain conditions and specific requirements. In case of a breach of an obligation that was attached by the Commission to an exemption, the exemption may be revoked. The Commission may also impose a fine on airlines that violate a granted exemption. The following activities between airlines may be exempt: agreements concerning slot allocation, flight schedules, the joint acquisition of computer reservation systems, the maintenance of aircraft, tariff setting, the coordination of capacities and the division of earnings from scheduled flights (i.e., pooling agreements).

Without delay, the Commission made use of its powers pursuant to article 2 of Council Regulation (EEC) 3976/87 by promulgating three regulations. These regulations set forth the prerequisites for group exemptions with respect to the activities mentioned above. Those exemptions granted by the Commission were far-reaching and remained effective until January 1, 1991. For example, airlines were permitted to continue to cooperate with other airlines on the basis of the above mentioned agreements. Thus, the exemptions provided the airlines concerned with a significant amount of protection in an increasingly competitive market.

B. **TARIFFS**

Council Directive 87/601/EEC on tariffs for scheduled flights between Member States maintains the traditional tariff approval procedure. Hence, a tariff becomes effective only if it has been approved by the governments of both Member States. The substantive prerequisites for the approval of a proposed tariff are set forth in article 3 of the Directive. According to this provision, a tariff proposed by an airline shall be approved by the government if they are reasonably related to long-term, fully allocated costs of the applicant carrier. Under article 3 of the Directive, the fact that the proposed air fare is lower than that offered

121. Id. art. 2.
122. EEC Treaty, supra note 1, art. 85(3). See supra note 28 for text of art. 85(3).
123. See Council Regulation (EEC) 3976/87, supra note 8, art. 2(3).
124. Id. art. 7.
125. Id. art. 7(2).
126. Id. art. 2(2).
130. Id. art. 4.
131. Id. art. 4.
132. Id. art. 3.
by another carrier, on the same route, is not a sufficient reason for withholding approval.\textsuperscript{133}

Tariff proposals may be made by an airline alone or after consultations with other airlines.\textsuperscript{134} In the latter case, the consultations must conform to Commission Regulation 3976/87.\textsuperscript{135} Article 7 of Council Directive 87/601/EEC provides a detailed procedure of notification and the consultation and arbitration process, should a Member State withhold approval.\textsuperscript{136}

The Tariff Directive introduces a new tariff approval concept that the Directive refers to as "zones of flexibility."\textsuperscript{137} Proposed tariffs that are within the margins of such zones of flexibility, are to be approved automatically by the governments concerned.\textsuperscript{138} The Directive creates two discount zones. In the first zone (i.e. the discount zone), the discount is 10 to 35 percent of the reference tariff.\textsuperscript{139} In the second (i.e. the deep discount zone), the discount of the reference tariff may be between 35 and 55 percent.\textsuperscript{140} Discount tickets are subject to considerable restrictions.\textsuperscript{141} Still, member states are free to agree to more liberal discount practices than those set forth in the Tariff Directive.\textsuperscript{142}

\textbf{C. \textit{MARKET ACCESS AND CAPACITY SHARING}}

The Council Decision 87/602/EEC liberalizes market access and capacity sharing.\textsuperscript{143} Bilateral agreements have traditionally provided for an equal (50:50) sharing of passenger capacity based upon the number of passengers of one airline on a given route. The Decision aims at a liberalization of firm sharing clauses. According to the Decision, airlines may increase or decrease their capacity by 5 percent, a capacity sharing ratio of 55:45.\textsuperscript{144} The country in which the airline is registered may not interfere for the benefit of its airline. Effective October 1, 1989, the ratio was changed to 60:40.\textsuperscript{145}

For the first time in the history of EC air transport law, the Council Decision grants every Member State the right of multiple designations.

\begin{itemize}
  \item \textsuperscript{133} Id.
  \item \textsuperscript{134} Id. art. 4(1).
  \item \textsuperscript{135} See Council Regulation (EEC) 3976/87, supra note 8.
  \item \textsuperscript{136} See Council Directive 87/601/EEC, supra note 8, art. 7.
  \item \textsuperscript{137} Id. art. 5.
  \item \textsuperscript{138} Id. art. 5(2).
  \item \textsuperscript{139} Id. art. 5(1).
  \item \textsuperscript{140} Id.
  \item \textsuperscript{141} Id. Annex II.
  \item \textsuperscript{142} Id. art. 6.
  \item \textsuperscript{143} See Council Decision 87/602/EEC, supra at 8.
  \item \textsuperscript{144} Id. art. 3(1).
  \item \textsuperscript{145} Id. art. 3(2).
\end{itemize}
Each Member State may appoint more than one airline to service a given bilateral route, to the extent that the route is used by a certain number of passengers.\textsuperscript{146}

The Decision also permits Community carriers to establish flight connections between major airports (i.e., category I airports)\textsuperscript{147} in their home country and regional airports (i.e., category II and III airports)\textsuperscript{148} of another Member State, regardless of distance or aircraft size.\textsuperscript{149} In addition, Community carriers are entitled to introduce scheduled air services to and from two or more points in other Member States, provided that no traffic rights are exercised between the combined points.\textsuperscript{150}

Most importantly, Community carriers may also carry out scheduled flights falling within the Fifth Freedom if certain conditions are met. The flight route thus needs to include at least one regional airport and the first or final airport must be within the home country of the carrier. In addition, the flight service in question may not exceed more than 30 percent of the annual capacity of the airline on any given route.\textsuperscript{151}

\textbf{D. CRITIQUE}

The First Package was a cautious and conservative step toward more competition in scheduled air transport within the Community. Radical changes to the market structure were not accomplished by the new laws. Rather, the reforms were relatively minor since they were coupled with generous exemptions for EC carriers from the EC antitrust laws. Therefore, it should not come as a surprise that the First Package had only modest effects on both airlines and passengers.\textsuperscript{152}

\textsuperscript{146} Id. art. 5(2) which reads as follows:
A Member State shall also accept multiple designation on a country-pair basis by another Member State:
1. in the first year after the notification of this Decision, on routes on which more than 250,000 passengers were carried in the preceding year;
2. in the second year, on routes on which more than 200,000 passengers were carried in the preceding year or on which there are more than 1,200 return flights per annum.
3. in the third year, on routes on which more than 180,000 passengers were carried in the preceding year or on which there are more than 1,000 return flights per annum.

\textsuperscript{147} Category I airports are listed in Annex II to Council Decision 87/602/EEC, supra note 8, at 25.

\textsuperscript{148} Category II and III airports are also listed in Annex II to Council Decision 87/602/EEC, supra note 8, at 25.

\textsuperscript{149} See Council Decision 87/602/EEC, supra note 8, art. 6(1).

\textsuperscript{150} See id. art. 7(1).

\textsuperscript{151} Id. art. 8(1).

market entries and the establishment of many new flight routes, the development of air fares has remained a disappointment given the Commission's high expectations. The measures did not result in noticeable tariff reductions. Consequently, additional more far-reaching measures are necessary if the objective of competitive market structures, in the area of scheduled air transport within the EC, is to be accomplished by January 1993.

VI. THE AHMED SAEED CASE

In April 1989, the European Court of Justice took the opportunity, in Ahmed Saeed Flugreisen v. Zentrale zur Bekämpfung unlauteren Wettbewerbs e.V., to comment on the First Package position concerning the new legal situation in EC air transport. This case involved two travel agencies in Frankfurt, Germany, that had sold tickets at fares that were up to 60 percent less than those approved by the German government. For this purpose, the travel agencies purchased tickets outside of Germany for flights originating in the country of purchase with a destination in a third country outside the EC, but having a stopover in a German airport.

In the lawsuit brought by the Association for the Protection Against Unfair Trade Practices in Germany, the plaintiff alleged that the two travel agencies had violated German law by selling the tickets above described. It was argued that the agencies had violated the German Air Transport Statute, which prohibits the application of air fares not approved by the German government. It was further argued that the agencies had engaged in unfair trade practices, insofar as the fares for the tickets sold undercut the approved tariff applied by their competitors. The lower courts held in favor of the Association. The Bundesgerichtshof, Germany's highest court in civil and commercial matters, granted the writ of certiorari and submitted the case to the European Court of Justice for a preliminary ruling pursuant to article 177 of the EEC Treaty. The Euro-

153. Id. at 7-12.
156. See Air Transport Statute, supra at 37.
157. See EEC Treaty, supra note 1, art. 177(3), which reads as follows:
The Court of Justice shall be competent to make preliminary rulings concerning:
(a) the interpretation of this treaty;
(b) the validity and interpretation of acts of the institutions of the Community;
pean Court of Justice concluded that tariff setting agreements between carriers constituted illegal cartels and therefore violated Article 85(1) of the EEC Treaty.\(^{158}\)

**A. ASSUMPTIONS OF THE COURT**

The holding of the Court is based upon the assumption that Article 85 of the EEC Treaty was directly applicable to the case at hand. This assumption went beyond the holding in the *Nouvelles Frontières* case.\(^ {159}\) In that case, the Court held that because of the lack of implementing Community legislation, Article 85 of the EEC Treaty could not be enforced directly; rather, the Commission and the competent authorities of the Member States could take measures against airlines only pursuant to Articles 88 and 89 of the EEC Treaty. If Article 85 of the EEC Treaty is directly applicable, the Commission no longer needs to utilize the procedures provided for in Article 89 of the EEC Treaty. Rather, the Commission may proceed directly under Article 85 of the EEC Treaty as implemented by Council Regulations 3975/87 and 3976/87.\(^ {160}\)

**B. ARTICLE 85 OF THE EEC TREATY**

In *Ahmed Saeed*, the European Court of Justice explicitly stated that tariff setting agreements constitute illegal cartels and violate Article 85(1) of the EEC Treaty.\(^ {161}\) According to Council Regulation 3976/87, such agreements may not be subject to group exemptions.\(^ {162}\) The Court pointed out that tariff "consultations," as opposed to tariff "agreements," remain exempt.\(^ {163}\) The criteria for differentiating between permissible tariff consultations and illegal tariff agreements are set forth in Article 4 of the Commission Regulation 2671/88.\(^ {164}\) Consequently, tariff agreements...
for intracommunity flights that did not fall within the group exemption were void per se, unless an objection made by the carrier concerned under article 5 of Council Regulation 3975/87 was successful.\textsuperscript{165} With respect to domestic flights and flights between a Member State and a third country, the procedure pursuant to articles 88 and 89 of the EEC Treaty remains applicable.\textsuperscript{166}

\textbf{C. \textit{ARTICLE 86 OF THE EEC TREATY}}

The statements of the European Court of Justice as to article 86 of the EEC Treaty are particularly interesting. The Court suggests that the abuse-of-market-power provisions of article 86 of the EEC Treaty apply to the entire air transport sector. That is to say that article 86 of the EEC Treaty applies to intracommunity flights, to domestic flights and flights from an EC Member State to a third country.\textsuperscript{167} Consequently, tariff agreements concerning flights from an airport of an EC Member State to an airport outside of the Community fall as much within the ambit of article 86 of the EEC Treaty, as do tariff agreements concerning intracommunity and domestic flights. This is particularly true in cases where an airline company is in a position to control the market or to charge excessively high or extremely low tariffs on a given route.\textsuperscript{168}

According to the Court, the fact that article 86 of the EEC Treaty has not been implemented by secondary Community law does not prevent the Commission from enforcing the provision.\textsuperscript{169} Member States' courts may also enforce article 86 of the EEC Treaty, even absent secondary Community law implementing said Treaty provision.\textsuperscript{170} For the Bundesgerichtshof, this was an important observation, as it had to decide the issue of whether a court may enforce article 86 of the EEC Treaty despite the lack of implementing Community legislation.

\textbf{D. \textit{ARTICLES 5 AND 90 OF THE EEC TREATY}}

Based upon its conclusions with respect to articles 85 and 86 of the EEC Treaty, the European Court of Justice stated that a Member State violates Community law (i.e., its obligations under article 5\textsuperscript{171} and article

\begin{itemize}
\item \textsuperscript{165} See Ahmed Saeed, 38 ZLW at 127.
\item \textsuperscript{166} id. at 128. For details of the procedures under arts. 88 and 89 of the EEC Treaty, see supra notes 99-107 and accompanying text.
\item \textsuperscript{167} See Ahmed Saeed, 38 ZLW at 129.
\item \textsuperscript{168} id. at 130-131.
\item \textsuperscript{169} id. at 129.
\item \textsuperscript{170} id. at 130-131.
\item \textsuperscript{171} EEC Treaty, supra note 1, art. 5 reads as follows:

Member States shall take appropriate measures, whether general or particular, to ensure fulfillment of the obligations arising out of this Treaty or resulting from action taken by the institutions of the Community. They shall facilitate the achievement of the Com-
90(1)\textsuperscript{172} of the EEC Treaty) if it approves tariffs that are contrary to article 85 or article 86 of the EEC Treaty.\textsuperscript{173} As a result, the Member States’ governments are required, in the approval process, to assure that the tariff consultations are in conformity with the principles laid down in articles 85 and 86 of the EEC Treaty, as well as Council Directive 87/601/EEC and Commission Regulation 2671/88.\textsuperscript{174} The Court also made it perfectly clear that it expects the Member States not to enter into new bilateral agreements with third countries that, directly or indirectly, provide for illegal tariffs.\textsuperscript{175}

\section*{E. \textsc{Analysis}}

In the \textit{Ahmed Saeed} case, there are two issues concerning the tariff setting process worth noting. By extending the application of article 86 of the EEC Treaty to flights between Member States and third countries, the Court put considerable pressure on the Member States to make sure that tariff setting and tariff approval provisions in bilateral agreements are consistent with EC antitrust laws. As a result, existing agreements that are contrary to article 86 of the EEC Treaty need to be renegotiated. Also, the applicability of article 86 to agreements concerning flights from within the Community to third countries is an extension of existing EC Laws\textsuperscript{176} not only to intracommunity flights but also to both domestic flights within an EC Member State and flights to third countries.

The European Court of Justice rendered its decision in the \textit{Ahmed Saeed} case just as the Commission was about to finish its work on the proposals for the Second Phase of Liberalization. Nevertheless, the Commission managed to include the implications of the \textit{Ahmed Saeed} decision in its proposals for the Second Phase of liberalization.\textsuperscript{177}

\section*{VII. \textsc{The Second Phase}}

In September 1989, the EC Commission published proposals for fur-

\textsuperscript{172} EEC Treaty, \textit{supra} note 1, art. 90 reads, in its pertinent part, as follows:

1. In the case of public undertakings and undertakings to which Member States grant special or exclusive rights. Member States shall neither enact nor maintain in force any measure contrary to the rules contained in this Treaty, in particular to those rules provided for in Art. 7 and Arts. 85 through 94.

\textsuperscript{173} \textit{See Ahmed Saeed}, 38 ZLW at 131.


\textsuperscript{175} \textit{See Ahmed Saeed}, 38 ZLW at 131-132.

\textsuperscript{176} \textit{See} Council Regulations, Directive and Decision, \textit{supra} note 8.

\textsuperscript{177} \textit{See} COM(89) 417 final (Sept. 8, 1989) at 1-5.
ther liberalization of EC scheduled air transport. The proposals are aimed at the relaxation of tariffs, capacity sharing, and market access. On the basis of the Commission’s proposals, the Council of the EC Transport Ministers, at its meeting in June 1990, agreed to a package of measures, commonly referred to as the Second Phase of the liberalization of EC air transport. These measures consist of three Council Regulations, two of which became effective November 1, 1990.

A. Tariffs

The new Tariff Regulation is the centerpiece of the second package. This Regulation provides more flexibility in the tariff setting and approval process. While the requirement that tariffs be approved by the affected governments remains unchanged, both the approval procedure and the range of approvable fares have changed considerably. Most importantly, the 1990 Tariff Regulation introduces, for the first time in the history of EC air transport laws, the double disapproval system. The Regulation did not, however, go so far as to permit the double disapproval system to be applied to all tariffs, as proposed by the EC Commission. Rather, the double disapproval system applies only to tariffs that exceed the reference tariff by at least 5 percent.

The First Phase system of reference tariffs and flexibility zones was revised. The Tariff Regulation allows Community carriers to set the price for a “normal economy class ticket,” independently, within a margin of plus or minus 5 percent of the reference tariff. Under the First Phase, the price for an economy class ticket was fixed at 100 percent of the reference tariff. The margins of the discount zone were changed from between 90 and 65 percent to between 94 and 80 percent. The margins of the deep discount zone were broadened from between 65 and 45 percent.

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178. COM(89) 373 final and COM(89) 417 final (Sept. 8, 1989). For a detailed discussion of the Commission’s proposals see Ebke & Wenglorz, supra note 51, at 475-477.
179. See Council Regulations 2342/90 and 2343/90, supra at 9.
180. See, e.g., Council Regulation 2342/90, supra note 9, art. 14.
181. See id. art. 4(1).
182. Id. art. 4(4).
183. See COM(89) 373 final (Sept. 8, 1989), art. 4(3).
184. See Council Regulation 2342/90, supra note 9, art. 4(4). The reference tariff is described in more detail infra, note 186.
185. Id. art. 4(3).
186. The reference tariff is defined in Council Regulation 2342/90, supra note 9, art. 2(i) which reads as follows:
Reference fare means the normal one way or return, as appropriate, economy air fare charged by a third or fourth freedom air carrier on the route in question; if more than one such fare exists, the arithmetic average of all such fares shall be taken unless otherwise bilaterally agreed; where there is no normal economy fare, the lowest fully flexible fare shall be taken.
The diagram in Table 1 illustrates the differences concerning the zones of flexibility between the First and Second Phase:

**TABLE 1**

<table>
<thead>
<tr>
<th>1st Phase</th>
<th>2nd Phase</th>
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<tbody>
<tr>
<td>(Jan. 1988)</td>
<td>(Nov. 1990)</td>
</tr>
</tbody>
</table>

The prerequisites for attaining a ticket within the discount zone have been eased. Prior to November 1, 1990, the journey had to include at least one Saturday night and a total of six nights, or alternatively, had to take place during off-peak times. Under the new Tariff Regulation, these requirements, particularly detrimental to business travelers, no longer exist. This impressive move towards more flexibility for a passenger wanting to acquire lower priced tickets is counteracted by the fact that the discount zone was reduced from 35 to 14 percent. The reduc-

187. Id. art. 4(3).
189. See Council Regulation 2342/90, supra note 9, Annex II No. 1.
190. Id. art. 4(3).
tion is not offset by the increase in the margins of the deep discount zone from 20 to 49 percent. For the most part, the restrictive requirements for entering the deep discount zone continue to be in effect.\textsuperscript{191}

1. THE TARIFF APPROVAL PROCESS

According to the new Tariff Regulation, tariff approval follows from one of three procedures:

A. AUTOMATIC APPROVAL

If the proposed tariff of an airline lies within one of the aforementioned flexibility zones, the governments of the Member States are required to approve the tariff.\textsuperscript{192} This results in a system of automatic approval, as the approval itself is merely a formality if other conditions, particularly for those set forth in article 3 of the Tariff Regulation are fulfilled.

If a tariff proposed by an airline lies above the zones mentioned in article 4(3) of the Tariff Regulation (i.e., if it is more than 5 percent above the reference tariff),\textsuperscript{193} the system of Double Disapproval applies. Under this system, tariff is deemed to be approved if the Member States concerned do not, within 30 days of the airlines' application for approval, reject the requested tariff.\textsuperscript{194} While it applies to a small number of tickets only, the double disapproval system enables the Member States and the EC Commission, to gain practical experience with the procedure. This is important when one takes into consideration that, beginning January 1, 1993, the double disapproval system will be applied to all tariffs.\textsuperscript{195}

B. DOUBLE APPROVAL

A tariff proposed by an airline that is neither within one of the flexibility zones nor above the reference tariff, must be approved explicitly by both governments.\textsuperscript{196} In such a case, the tariff is deemed to be approved if neither one of the governments involved rejects the tariff within 21 days upon receipt of the application.\textsuperscript{197} Tariffs subject to the double approval system are most likely to be below the deep discount zone. The Member States, it seems, were not prepared to give up their strict control over these tariffs.

\textsuperscript{191} Id. Annex II, No. 2.
\textsuperscript{192} Id. art. 4(3).
\textsuperscript{193} For a definition of the reference tariff, see supra at 186.
\textsuperscript{194} See Council Regulation 2342/90, supra note 9, art. 4(4).
\textsuperscript{195} Id. art. 12.
\textsuperscript{196} Id. art. 4(5).
\textsuperscript{197} Id.
2. INVESTIGATION AND CONSULTATION PROCEDURE

The Tariff Regulation provides control mechanisms for cases in which a Member State challenges a tariff for lack of conformity with the Tariff Regulation.

A. ARTICLE 5 OF THE COUNCIL REGULATION

At the request of a Member State having a reasonable interest in the route in question, the Commission is obliged to inquire into the conformity of any previously approved tariff that does not lie within the flexibility zones.198 The Commission is also required to inquire whether the other Member State has met its obligations under article 3(3) of the Regulation.199 According to article 3(3),200 the Commission must investigate whether or not the Commission must investigate whether or not an airline charges unjustifiably high tariffs that are not in the best interest of consumers. It is also obliged to investigate whether the tariffs are "dumping tariffs" aimed at the expulsion of competitors from a given route.201 Within 14 days of being called upon by a Member State, the Commission must decide whether or not the tariff in question is to remain in effect during the investigation period.202 The final decision on all these matters must be made within two months of the receipt of the Member State’s request.203 Within one month after the decision, the affected Member State may appeal to the EC Council.204

The procedure provided for by article 5 of the Tariff Regulation is an important instrument in the hands of the Member States. The provision enables the Member States to control a fare’s development, especially if the tariff deviates too far in one direction or another. It should be recognized, however, that the possibility of an appeal by the concerned Member State to the EC Council of Ministers adds a political dimension to the tariff setting process which could be undesirable in light of the importance of the enforcement of EC antitrust laws.

B. ARTICLE 6 OF THE COUNCIL REGULATION

Article 6 of the Tariff Regulation deals with cases in which tariffs that are below the flexibility zones and have to be approved by both governments,205 are rejected by one government.206 In those cases, article 6

198. id. art. 5(1).
199. id.
200. For the text of Council Regulation 2342/90, supra note 9, art. 3; text of Council Regulation 2342/90 supra, at 193.
201. See Council Regulation 2342/90 supra note 9, art. 3(3).
202. id. art. 5(2).
203. id. art. 5(3), (4).
204. id. art. 5(5).
205. See supra notes 197-98 and accompanying text.
provides for a detailed consultation and arbitration procedure.\textsuperscript{207} If confirmed by the EC Commission, the arbitrators' decision becomes binding on both governments.\textsuperscript{208}

3. \textit{Price Leadership}

The new Regulation extends the possibilities for EC airlines to become price leaders (i.e., introducing lower tariffs on an existing flight route).\textsuperscript{209} Prior to November 1, 1990, the possibility for increased price competition was limited to routes on which the Third and Fourth freedom rights were exercised (i.e., on intra-community non-stop connections).\textsuperscript{210} According to the new Tariff Regulation, Community carriers may now become price leaders when operating on the Fifth Freedom route; provided, the tariffs proposed by the airlines remain within the flexibility zones.\textsuperscript{211} Despite this limitation, the provisions are likely to considerably strengthen competition on routes on which airlines of the third, fourth, and fifth freedoms operate.

4. \textit{Other Provisions}

The Tariff Regulation allows Member States to enter into or maintain more flexible bilateral agreements than those mentioned in article 4 of the Tariff Regulation.\textsuperscript{212} This is true, for example, of the British-German Agreement\textsuperscript{213} and the British-Luxembourg Air Transport Agreement.\textsuperscript{214} Furthermore, EC Member States are required to bring their bilateral agreements with third states that were granted Fifth Freedom rights for their carriers on routes within the Community, in line with the Tariff Regulation "at the first possible occasion," if the agreements are contrary to the Council Regulation.\textsuperscript{215} Most importantly, the new Regulation requires that the double disapproval system be introduced by January 1, 1993.\textsuperscript{216}

5. \textit{Scope of the Tariff Regulation}

Contrary to the proposals of the EC Commission,\textsuperscript{217} the Council did not extend the Tariff Regulation to flights from within the EC to flights from

\begin{itemize}
\item \textsuperscript{206} See Council Regulation 2343/90, \textit{supra} note 9, art. 6(1).
\item \textsuperscript{207} Id. arts. 6(10)-(9).
\item \textsuperscript{208} Id. art. 6(8).
\item \textsuperscript{209} Id. art. 3(6). For the text of art. 3, see \textit{supra} at 193.
\item \textsuperscript{210} See Council Directive 87/601/EEC, \textit{supra} note 8, art. 4(5).
\item \textsuperscript{211} See Council Regulation 2342/90, \textit{supra} note 9, art. 3(6).
\item \textsuperscript{212} Id. art. 7.
\item \textsuperscript{213} See \textit{supra} notes 47-48 and accompanying text.
\item \textsuperscript{214} See Air Route Agreement, \textit{supra} note 47.
\item \textsuperscript{215} Id. art. 11.
\item \textsuperscript{216} Id. art. 12.
\item \textsuperscript{217} See COM(89) 373 final (Sept. 8, 1989), Annex I, art. 1.
\end{itemize}
an EC airport to a third country. The Regulation applies only to scheduled flights on routes between Member States.218 It should also be noted that the new Tariff Regulation binds Member States directly. Thus, there is no room for the Member States to exercise discretion in the transformation and application of the Regulation. This differs significantly from the old Tariff Directive of 1987219 that, like all Directives, left the form and methods of implementation to the Member States.

B. MARKET ACCESS AND CAPACITY

The Council Regulation Concerning Capacity Sharing and Market Access220 may be divided into two parts:

1. MARKET ACCESS

The Regulation explicitly grants the right of an EC carrier to fly an international route within the Community, as part of the Third and Fourth Freedom rights.221 Consequently, EC carriers that operate under the Third and Fourth Freedom rights have free access to all EC airports.222 At the same time, the Regulation requires Member States (country of destination) to allow, on the basis of reciprocity, airlines that operate internationally and are registered in another Member State (country of registration) to make use of the Third and Fourth Freedom rights on the same route.223

The reciprocity requirement is controversial as it allows a Member State to make the introduction of new routes or frequencies on an existing route conditional upon the receipt of the same number of new routes or frequencies for its airlines. The reciprocity rule can have the effect that a carrier based at a slot-tight airport (i.e., British Airways in London-Heathrow, England) may be unable to obtain new frequencies at, or routes to, less frequently used airports (e.g., Lisbon, Portugal) unless an airline of that country (e.g., TAP Air Portugal) attains route rights for London-Heathrow. While it may be detrimental to large carriers operating out of slot-tight airports, the reciprocity requirement may be beneficial to smaller carriers operating out of less frequented airports as they may use their leverage power to gain access to the slot-tight airport.

218. See Council Regulation 2342/90, supra note 9, art. 1.
220. See Council Regulation 2343/90, supra at 9.
221. Id. arts. 4, 5(1).
222. There are a few exceptions to this general rule, see id. art. 1(4).
223. Id. arts. 5(1), (2).
A. MULTIPLE DESIGNATION

The new Regulation reduces the threshold for multiple designations on a country-pair basis. Since January 1, 1991, a Member State must agree to a multiple designation by another state on a given bilateral route if there were more than 140,000 passengers travelling on the route or more than 800 return flights in the preceding year. Effective January 1, 1992, however, the threshold will be reduced to 100,000 passengers or 600 return flights per year and route. The Regulation opens the way for EC Member States to allow more than one airline to service a particular route. As a result, a route that has previously been limited to a single carrier per country, may in the future be served by more than one carrier.

B. FIFTH FREEDOM RIGHTS

In addition, the Regulation extends the possibility for airlines to exercise Fifth Freedom rights. Under the First Phase Decision, an airline was only allowed to use 30 percent of its annual carrying capacity on a given route for Fifth Freedom service. Under the new Regulation, it is possible to use up to 50 percent of the seating capacity per flight plan period on any given route. The 20 percent increase constitutes modest improvement towards more competition. Unfortunately, the Council did not follow the Commission’s proposal to allow carriers to make use of their rights of the Fifth Freedom in regard to third countries, if such countries agree. Thus, there is considerable room for further liberalization in the future.

C. PUBLIC SERVICE OBLIGATION

Under the new Regulation, an airline may be required to service regional airports within its home country. In order to fall within this category of airports, however, the airport must be of paramount importance to the economic development of the region concerned.

D. INTER-REGIONAL AIR SERVICE

The 1990 Regulation replaces the Inter-regional Air Services Direc-
Inter-regional air transport is now subject to the new Market Access and Capacity Sharing Regulation. To a limited extent, the 1990 Regulation protects airlines that service regional airports and that have opened new routes, against carriers operating with larger aircraft. To protect regional carriers, the reciprocity requirement is not applied for a period of two years; provided, the carrier has been granted the privilege to fly a new route between two regional airports within the Community. The reciprocity rule comes into effect again, however, if a foreign carrier with an aircraft carrying no more than 80 passengers intends to fly the same route.

E. REVERSE DISCRIMINATION AND CABOTAGE

It is important to call attention to two provisions that were part of the Commission's proposals that the Council, however, did not include in the 1990 Tariff Regulation.

The Commission had proposed a clause according to which each Member State was required to allow more than one airline in its own territory to offer scheduled flights, if certain financial and technical criteria were met. The Council, however, was of the opinion that the new Regulation should not interfere with the relationship between a Member State's government and carriers registered in that Member State. Consequently, there is always a possibility that domestic carriers may be discriminated against under the laws of its country of registration. Under the new Regulation, it is still possible that an EC Member State would deny a carrier that is registered under its laws the ability to offer certain air services, only to allow a carrier registered under the laws of another Member to do so. It seems to have been impossible to obtain majority within the Council for the Commission's proposal because the adoption of the Commission's proposal would, in effect, have resulted in the loss of national sovereignty rights which the Member States were not prepared to accept at this point in time. Accordingly, the problem of reverse discrimination of domestic carriers continues to exist and there continues to be no relief under EC laws to remedy this situation.

Furthermore, the Council did not adopt the Commission's cabotage rights proposal. According to this proposal, the Member States were to

233. For details of the Inter-regional Air Service Directive, see supra notes 85-88 and accompanying text.
234. See Council Regulation 2343/90, supra note 9, art. 5(4).
235. Id.
236. Id.
237. See COM(89) 373 final (Sept. 8, 1989), Annex II, art. 3(1), 9.
238. Id. art. 3(1).
239. See Council Regulation 2343/90, supra note 9, art. 3(1).
introduce, beginning in 1990, cabotage rights for Community airlines to a limited extent. The Council stated, however, that it found it "desirable" to take further liberalization measures with respect to market access and capacity sharing, including the introduction of a cabotage rule by June 30, 1992. It remains to be seen whether the Council will meet its own deadline. It should be noted that the deadline stated in the Regulation creates no legal obligation on the part of the Council to act.

2. CAPACITY SHARING

Starting with the 60:40 capacity sharing ratio that came into effect on October 1, 1989, the new Regulation allows Community carriers to extend their seating capacity, beginning on November 1, 1990, by 7.5 percent per flight plan period. At the request of a Member State, the Commission may, however, limit the growth in capacity, if the capacity increase results in substantial damage to a carrier registered in that Member State.

It is worth noting that the new Regulation states as one of its objectives, the full dismantling of barriers regarding capacity sharing between Member States by January 1, 1993. This has, however, already been implemented for all regional flights within the EC, effective November 1, 1990, regardless of the seating capacity of the aircraft used. Unfortunately, the Regulation again does not go as far as the Commission's original proposal. The Commission had suggested that capacity limits also be dismantled for flights between category I airports and regional airports. Such a measure would have benefitted international air services between regional airports and large airports. At the same time it would have relieved the pressure on major European airports that are already heavily congested.

C. ANTITRUST PROVISIONS

The EEC Council Regulation 2344/90 which forms part of the Second Phase, should be mentioned as well. The Regulation consists of one provision only. This provision empowers the Commission to continue to

240. For details see COM(89) 373 final (Sept. 8, 1989), Annex II, art. 9.
241. See Council Regulation 2343/90, supra note 9, preamble.
242. See Council Decision 87/602/EEC, supra note 8, art. 3(2).
243. See Council Regulation 2343/90, supra note 9, art. 11(1). It should be noted that the summer flight plan period lasts from April 1 until October 31, the winter period from November 1 until March 31.
244. See id. art. 12(1).
245. Id. art. 11(2).
246. Id. art. 11(3).
247. See COM(89) 373 final (Sept. 8, 1989), Annex II, art. 12(3).
exempt, until December 31, 1992, certain airline practices and airline agreements from the EC antitrust laws.\(^{249}\) The Council did not, however, follow the Commission's proposal concerning amendments and extensions of Council Regulations 3975/87 and 3976/87.\(^{250}\) The Council's failure to adopt the Commission's proposal is regretful because the Council simply ignored the holding of the European Court of Justice in the *Ahmed Saeed* case\(^{251}\) concerning the application of articles 85 and 86 of the EEC Treaty to flights to third countries and domestic flights.\(^{252}\)

**VIII. OTHER AIR TRAFFIC PROBLEMS**

The degree of competition that may develop in air transport within the EC depends to a large extent upon the available infrastructure, including runways, air traffic control systems, and slots. In this area a number of problems exist. With the expected growth in air traffic,\(^{253}\) these problems are likely to become more severe. It has been said that, in Europe, chaos on the ground and in the air is no longer a myth, but nearly a reality.\(^{254}\) Necessary changes and improvements will be extraordinarily expensive. At a number of European airports, such as Frankfurt, Madrid, and London-Heathrow, slots are no longer available during peak hours. The shortage of slots makes it very difficult, if not impossible, for new airlines to enter the market.\(^{255}\) Also, the European air traffic control system is technically outdated and still largely based upon the traditional system of national air space control.\(^{256}\) Internationally integrated air traffic control systems, such as Eurocontrol, are, unfortunately, still of relatively little significance.\(^{257}\) The lack of a modern international control system within the Community is a technological and political anachronism at a time when

\(^{249}\) Id. art. 1.

\(^{250}\) See COM(89) 417 final (Sept. 8, 1989).

\(^{251}\) See *Ahmed Saeed*, 38 ZLW at 124. See also supra notes 155-76 and accompanying text.

\(^{252}\) See supra notes 161-70 and accompanying text.

\(^{253}\) IATA expects European air traffic to grow at least 6% *per annum* in the coming years. See Süddeutsche Zeitung, Oct. 30, 1989, at 26.

\(^{254}\) According to a Stanford Research Institute study that was prepared for IATA, European air traffic is likely to collapse unless there is a radical improvement in the organization of air traffic, especially in the field of air traffic control and the capacity of larger airports. See Frankfurter Allgemeine Zeitung, May 3, 1990, at R13.

\(^{255}\) The great importance of attractive slots for new market entries could be observed in the case of the German airline newcomer "German Wings." The company went out of business less than a year after its entry, mainly because "German Wings" was unable to attain peak-hour slots. See *Die Zeit*, May 4, 1990, at 32.


\(^{257}\) Id. at 43-45.
the completion of the Single European Market is less than two years away.

The Commission has already made a number of proposals to the Council in an attempt to solve the problems mentioned.258 Additional proposals have also been announced.259 New initiatives regarding to airport fees,260 EC-wide air traffic control, and slot allocation are being proposed.261 Moreover, the Commission is presently attempting to obtain a power of attorney from the Member States to negotiate, on behalf of the EC as a whole, air transport agreements with third countries.262 A comprehensive package of complementary measures will be necessary if the opportunities provided by the Second Package of liberalization are to be realized. Most importantly, one should not forget about the safety of aircraft. In the United States, this aspect of deregulation has proved to be increasingly important in an expanding and competitive market for air transport services.263

IX. CONCLUSIONS

The Second Phase of liberalization of EC air transport has resulted in changes to the existing system in a number of respects. In the areas of market access, tariffs and capacities it constitutes considerable progress towards the creation of more competitive and more market oriented structures. State controls have been dismantled. These are all positive achievements. However, there is still a number of important issues that need to be solved. These issues include, but are not limited to, cabotage rights and reverse discrimination of domestic carriers as well as a technically updated air traffic infrastructure. Thus, a Third Package of air transport liberalization is needed if the Single European Market in the air transport sector is to be completed by January 1, 1993.

258. See, e.g., COM(88) 577 final (Jan. 16, 1989).
259. See COM(89) 373 final (Sept. 8, 1989) at 11.
Maritime Terrorism and Legal Responses

DEAN C. ALEXANDER*

I. INTRODUCTION

The specter of terrorism, known since antiquity, continues to threaten the stability and fabric of modern society in the 1990's.¹ The often cited term "terrorism" has yet to find a universally accepted definition.² This article will define terrorism as "premeditated, politically motivated vio-


lence perpetrated against noncombatant targets by subnational groups or clandestine state agents, usually intended to influence an audience."3 Recent events such as the horrific murder of Leon Klinghoffer during the seizure of the Italian cruise ship Achille Lauro underline the need for practical legal measures to reduce the harmful aspects of this virus.4

The purpose of this article is manifold. Part II describes the role of civil suits brought by states and other victims of terrorism. Part III reviews early international legal responses to maritime terrorism. Part IV explains the factual background to the Achille Lauro incident and Part V summarizes the civil suits which followed that incident. Part VI discusses the rationale and analysis of the Southern District of New York's June 1990 order in the Klinghoffer v. Palestine Liberation Organization (PLO) suit, in which the court determined, inter alia, that the federal court had jurisdiction over the PLO. Part VII assesses the Klinghoffer v. PLO order. Part VIII discusses U.S. legislative proposals to provide U.S. victims of international terrorism (and their families) a civil cause of action in U.S. federal district court. Part IX addresses the recent international response to maritime terrorism, such as the 1988 I.M.O. Convention, and Part X concludes that unilateral, bilateral, and multinational legislative responses are essential to furthering the vital, though slow struggle, against terrorism.

II. THE ROLE OF CIVIL SUITS BROUGHT BY VICTIMS OF TERRORISM

A. OVERVIEW

Professor Harold Koh differentiates between the criminal and civil responses to terrorism.5 Prof. Koh notes that criminal sanctions generally revolve around "the apprehension, prosecution, and punishment of ter-

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4. See infra notes 104-122 and accompanying text.

Furthermore, the criminal paradigm is additionally sub-divided into four tiers: global conventions, regional agreements, bilateral pacts, and national legislation. In contrast, civil responses are subsumed under "all nonforcible, noncriminal means of sanctioning terrorists and states who support terrorism." Prof. Koh notes that civil remedies are primarily questions of legal rather than political theory, and decried at the lack of international framework to compensate victims. Also, Prof. Koh proffers that while criminal prosecution corresponds to deterrence and punishment, civil sanctions afford monetary and economic benefits to victims of terrorism.

Civil remedies to terrorism will ultimately, according to Prof. Koh, be determined by the following considerations: "[w]hat objectives do the recognition and enforcement of civil remedies against terrorism serve and what institutions within the national government are best situated to create and enforce the remedies—the courts, Congress, or the Executive Branch?" Prof. Koh concludes that it is up to the Congress to craft extensive civil statutory schemes against terrorism. Only in this manner, can the development of public international litigation be sustained.

Other authors have also suggested that private sanctions are vital to the war against terrorism. As Prof. Jordan Paust noted, "a realistic approach to law and choice should not focus on questions of whether there should be private involvement in decisions about and sanctions against terrorism, but rather how to make private participation more useful." Prof. Paust advocates the use of the legislative and court systems to deter terrorism. McDougal and Feliciano point to military, diplomatic, eco-

6. Id.
7. Id.
8. Id. at 173. "The array of possible 'civil' antiterrorist responses run the gamut from those remedies directed primarily against terrorist individuals and groups to those intended primarily to sanction their state supporters. Immigration measures and curtailment of travel rights are prime examples of nonforcible, noncriminal actions targeted against individual terrorists. A listing of the available nonforcible, noncriminal sanctions against state supporters of terrorism, by contrast, encompasses nearly every tool of economic warfare currently available to nations; denial of import benefits, export controls, financial embargoes and economic boycotts, withholding of foreign aid, termination of arms sales, and suspension of air flights by both official and nongovernmental institutions, to name by a few" (footnotes omitted). Id. at 175-77.
9. Id. at 175-77.
10. Id. at 173.
11. Id. at 174.
12. Id.
13. Id.
14. See infra notes 15-37 and accompanying text.
16. Id. at 587, 593-5, 597-9, 607-11.
nomic, and ideological solutions to terrorism. Additionally, Prof. Paust discusses a possible cause of action for terrorist victims against common carriers. More specifically, he states that tort law can be utilized by airline passengers to recover damages from airlines for acts committed by terrorist groups on their planes.

Imposing civil liability against airlines could be perceived as an equitable distribution of the risk and a promotion of anti-terrorism efforts. Thus, the idea of civil suits by the Klinghoffers against the owners of the Achille Lauro does not seem novel, nor far-fetched. In fact, Prof. Paust supports civil liability whenever individuals or institutions are intentionally or negligently involved in an act of terrorism. For instance, Prof. Paust cites as an example a gun shop owner supplying illicit dum-dum bullets to terrorists who commit violent acts. He argues that such a vendor should be held strictly liable for the damages resulting from the sale of such an inherently dangerous product. Such civil sanctions would greatly expand the scope of weapons which could be used to combat terrorism.

While private causes of action involve non-state actors, strengthened governmental rules regarding international civil procedure would also assist private suits. Additionally, more government rules are necessary to coordinate resolutions of such suits in light of already existing bilateral and multilateral conventions regarding jurisdiction and choice of law over the offender. Such integration and use of established international law precepts will ultimately enable a victim of terrorism to receive compensation.

Several authors suggest that civil causes of action may already be brought under existing conventions, such as the European Convention on the Compensation of Victims of Violent Crimes (European Convention).

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19. Id. at 597-98.
20. Id. at 598.
21. See infra notes 123-250 and accompanying text.
22. Paust, supra note 15, at 598.
23. Id.
24. Id.
26. Id.
27. Id.
Professor Otto Lagodny points out that the European Convention expedites prosecution of terrorist offenders. More specifically, it denies terrorists the designation of their violent activities as "political offenses," which are excepted from extradition under the European Convention.

As Article I provides in pertinent part:

For the purposes of extradition between Contracting States, none of the following offences shall be regarded as a political offence or as an offence connected with a political offence or as an offence inspired by political motives: . . .

c. a serious offence involving an attack against the life, physical integrity or liberty of internationally protected persons, including diplomatic agents;
d. an offence involving kidnapping, the taking of a hostage or serious unlawful detention;
e. an offence involving the use of a bomb, grenade, rocket, automatic firearm or letter or parcel bomb if this use endangers persons;
f. an attempt to commit any of the foregoing offenses or participation as an accomplice of a person who commits or attempts to commit such an offence.  

Second, Professors Umberto Leanza and Luigi Sico argue that the European Convention assists civil remedies in the fight against terrorism. More particularly, the Convention permits victims to be compensated by the nation where the crime occurred. While acknowledging some immunities, Leanza and Sico note that the Convention provides, "set maximum levels of compensation; specifies damages that may be claimed; outline[s] procedures for placing claims; and guard[s] against double compensation."  

Other authors argue that civil remedies against terrorists can be framed using existing U.S. legislation, namely, the Racketeer Influenced and Corrupt Organization statute ("RICO"). While the RICO statute was not designed to curb terrorism, civil RICO permits private treble damage suits by persons harmed in their property or business against RICO "enterprises" involved in a "pattern of racketeering." RICO stipulates that a "pattern of racketeering" involves the carrying out of several acts including "any act or threat involving murder, kidnapping, arson, or extortion.


29. Lagodny, supra note 28, at 584.
30. Id.
31. ECST, supra note 28, art. 1.
32. Leanza & Sico, supra note 25, at 103.
33. ECST, supra note 28.
34. Leanza & Sico, supra note 25, at 103.
tion" within a ten-year period.37

There has been some use of the civil RICO statute by U.S. Attorneys' Offices against terrorist groups.38 More particularly, the U.S. Attorney Office for the Southern District of New York utilized civil RICO provisions to obtain injunctions, curb the actions, and gain the forfeiture of assets who support terrorist groups.39 In contrast, United States v. Ivic40 attempted unsuccessfully to use criminal RICO against alleged arson and murder by Croatian terrorists.41 In Ivic, the Second Circuit concluded that criminal RICO was inapplicable because the alleged offenses were "neither claimed nor shown to have any mercenary motive."42 Furthermore, in Ivic, the court stated that "RICO's origins, most particularly of the mischief it was meant to remedy, indicate that political terrorism, at least when unaccompanied by any financial motive... is beyond its contemplated reach.43

In a subsequent case, United States v. Bagaric,44 which involved allegations that a Croatian terrorist group was perpetrating an international extradition scheme, the Second Circuit concluded that RICO required that the criminal activities be motivated by only some economic or financial objectives.45 Nevertheless, the Bagaric court concluded that terrorist acts are beyond the reach of RICO.46

Given the apparent limitations of RICO to combat terrorism in the U.S., Irvin Nathan and Kenneth Juster suggest amending RICO in order to enlarge the predicate offenses list of the statute.47 This modification would allow for sanctioning "(1) hostage taking, (2) assault on foreign or federal offenses, and (3) assassination of foreign or federal officials."48 Furthermore, Nathan and Juster articulate that RICO should be amended to eliminate the economic/financial motive to the predicate list.49 If such changes are made to existing law, the authors conclude, the U.S. will

38. Koh, supra note 5, at 175, n.24.
40. 700 F.2d 51 (2d Cir. 1983).
41. Id.
42. Id. at 59.
43. Id. at 63.
44. 706 F.2d 42 (2d Cir. 1983).
45. Id. at 58.
46. Id.
47. Nathan & Juster, supra note 35, at 570.
48. Id.
49. Id.
have another tool to fight terrorism.\textsuperscript{50}

The issue of who in the terrorist organization should be sued must also be addressed.\textsuperscript{51} Although for evidentiary and length of procedure interests it would seem logical to file a civil action against the actual perpetrators, such defendants are unlikely to have the financial resources to adequately compensate the victims.\textsuperscript{52} Instead, it is more beneficial to name the actual terrorist organization and its leaders in the suit,\textsuperscript{53} however, impediments arise in such a scenario as well.\textsuperscript{54} For example, since terrorist organizations are illicit, secret cadres, it is often difficult, if not impossible, to locate and attach their assets.\textsuperscript{55}

Consideration should also be given to the defenses which can be claimed by terrorist organizations.\textsuperscript{56} As has long been the case, terrorist groups view themselves as freedom fighters and, in cases such as the PLO, as sovereign states.\textsuperscript{57} If the latter is recognized as such an entity, then the "terrorist" group (and its leaders) could proffer the defense of sovereign immunity.\textsuperscript{58} As will be discussed below, most terrorist groups which claim to be states, do not possess the attributes which define a state under international law.\textsuperscript{59} Terrorists groups could, however, be ascribed the signification of insurgents under international law.\textsuperscript{60} Viewing a terrorist group as an insurgent would similarly provide this extra-legal organization with the defenses of a sovereign state.\textsuperscript{61}

**B. CIVIL SUITS AGAINST COMMON CARRIERS**

A plaintiff injured in a terrorist incident abroad a common carrier is more likely to obtain a judgement against the charterer of the carrier or against the common carrier itself than against a terrorist group.\textsuperscript{62} National laws often require that the safety of passengers (and their luggage) be guaranteed by the common carrier.\textsuperscript{63} Moreover, international agreements, such as article 3 of the 1974 Athens Convention, state that: "[t]he

\begin{itemize}
\item \textsuperscript{50} Id.
\item \textsuperscript{51} Leanza & Sico, supra note 25, at 99.
\item \textsuperscript{52} Id.
\item \textsuperscript{53} Id.
\item \textsuperscript{54} Id.
\item \textsuperscript{55} Id. at 100.
\item \textsuperscript{56} Id. See generally Roberts. The Legal Implications of Treating Terrorists as Soldiers, 9 CONFLICT 375 (1989).
\item \textsuperscript{57} Leanza & Sico, supra note 25, at 100.
\item \textsuperscript{58} See infra notes 183-190 and accompanying text.
\item \textsuperscript{59} Id.
\item \textsuperscript{60} Roberts, supra note 56, at 375-88.
\item \textsuperscript{61} Leanza & Sico, supra note 25, at 100.
\item \textsuperscript{62} Id. at 100.
\item \textsuperscript{63} Id. at 101. See arts, 409 and 412 (1), Codice della Navigazione (Italy) cited in Leanza & Sico, supra note 25, at 104.
\end{itemize}
carrier shall be liable for the damage suffered as a result of the death of or personal injury to a passenger and the loss of or damage to luggage if the incident which caused the damage so suffered occurred in the course of the carriage and was due to the fault or neglect of the carrier, of his servants or agents acting within the scope of their employment." 64 While the Athens Convention is not yet in force, its basic principles shed light on both contractual liability and tort culpability of a common carrier. 65 For instance, Italian law requires that, to obtain damages, a passenger (in our analysis, a terrorist victim) need only show that the harm occurred during the course of the voyage. 66 In contrast, in a tort-based suit, the carrier’s negligence must be demonstrated. 67 If the negligence standard must be satisfied in order to recover against the carrier, it would obviously be more difficult to prevail since it would be hard to show a direct relationship between the harm caused by the terrorist and the negligence of the carrier. 68

C. CIVIL SUITS AGAINST NATIONS AND THEIR AGENTS

Since it is a state’s responsibility to check immigration and security matters during pre-boarding of maritime vessels, it would appear, at first glance, that state liability attaches if this duty is not met. 69 More specifically, a state could likely be responsible "if the terrorist group was on board the carrier from the time of embarking, or [at] a port of call where terrorists boarded the carrier." 70 Damages accruing from this state responsibility can be based on either direct or vicarious liability. 71 Yet, using tort principles, a nation’s liability for harms to passengers resulting from a terrorist attack can accrue solely if the extra-legal attack was reasonably foreseeable. 72 Furthermore, sovereign immunity laws and the act of state doctrine may indeed be a grave impediment to suits against states by victims of terrorism. 73

III. INTERNATIONAL LEGAL RESPONSES TO TERRORISM

The Achille Lauro incident brings into clear focus several international agreements that could have a useful role in fighting terrorism: The

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64. Athens Convention of December 13, 1974, art. 3 [hereinafter Athens Convention].
65. Id.; Sico, supra note 25, at 101.
67. Id.
68. Id.
69. Id. at 101.
70. Id. at 102.
71. Id.
72. Id.
73. Id.

Although an ancient crime, an authoritative definition of piracy is lacking. Part of this deficiency is due to arguments over the components of the crime which include: 

"[1] whether . . . an intent to rob, was a necessary element, [2] whether acts by insurgents seeking to overthrow their government should be exempt, as were acts by state vessels and recognized belligerents, and [3] whether the act had to be by one ship against another or could be on the same ship." Nevertheless, customary international law views piracy as a crime. More specifically, it encompasses "every unauthorized act of violence against persons or goods committed on the open sea either by a private vessel against another vessel or by the mutinous crew or passengers against their own vessel." In contrast, modern maritime terrorism often involves acts committed on one..."
ship, and involves political rather than monetary goals.\(^8^0\)

Under article I, section 8 of the U.S. Constitution, Congress is empowered to define and punish acts of piracy.\(^8^1\) While early federal court decisions characterized piracy as "robbery and murder on the high seas" and "depredation on the seas,"\(^8^2\) later courts have focused on the utility of sanctioning piracy in order to permit all countries "to navigate [freely] on the high seas."\(^8^3\) Current legislation requires stringent punishment of a convicted pirate.\(^8^4\) Yet because federal legislation defers its definition of piracy to international law, international clarification of the elements of piracy is vital.\(^8^5\)

In order to establish a uniform definition of piracy in the law of nations, the 1958 Geneva Convention sculptured a straightforward description of the crime.\(^8^6\) The Convention provides that piracy includes any of the following:

1. Any illegal acts of violence, detention or any acts of depredation, committed for private ends by the crew or the passengers of a private ship or private aircraft, and directed: (a) On the high seas, against another ship or aircraft, or against persons or property on board such ship or aircraft; (b) Against a ship, aircraft, person or property in a place outside the jurisdiction of any State;
2. Any act of voluntary participation in the operation of a ship or of an aircraft with knowledge of facts making it a pirate ship or aircraft;
3. Any act of inciting or of intentionally facilitating an act described in sub-paragraph 1 or sub-paragraph 2 of this article.\(^8^7\)

Scholars have argued that the language "for private ends" does not necessarily require an intent to rob.\(^8^8\) Yet, questions remained whether this term "was intended to exclude all acts done for political purposes or only acts committed by unrecognized insurgents that would be lawful if committed by recognized belligerents."\(^8^9\) Answers to these questions:

80. Halberstam, supra note 75, at 277-281.
81. Congress is empowered to "define and punish piracies and felonies committed on the high seas, and offenses against the law of nations." U.S. Const. art. I, § 8.
84. "Whoever, on the high seas, commits the crime of piracy as defined by the law of nations, and is afterwards brought into or found in the United States, shall be imprisoned for life." 18 U.S.C. § 1651 (1982). See also 33 U.S.C. § 381 (1982) (discussing President's right to implement public ships to counter piracy).
85. Id.
87. Id.
88. Halberstam, supra note 75, at 278.
89. Id.
seem to be pronounced in the affirmative by the International Law Commission's comments on the draft 1958 Geneva Convention. More specifically, the comment concluded that "the draft convention excludes from its definition of piracy all cases of wrongful attacks on persons or property for political ends, whether they are made on behalf of states, or of recognized belligerent organizations, or of unrecognized revolutionary bonds." 

Despite apparent exemption of terrorist acts from the elements of piracy, Article 16 of the 1958 Convention on the High Seas stipulates, "[t]he provisions of this convention do not diminish a state's right under international law to take measures for the protection of its nationals, its ships and its commerce against interference on or over the high seas, when such measures are not based upon jurisdiction over piracy." The comments to this article explain that this provision stands for the proposition that acts having the characteristics of piracy would be deemed unlawful if carried out by the unrecognized belligerent, while the same acts committed by revolutionaries would be legal. More simply, only when insurgents' piratical activities are aimed at a nation whose government they want to replace, will the attack be defined as non-piracy.

Although international law often differentiates between soldiers and insurgents, an exemption from liability due to an insurgent's arguable piratical actions hurts the world community's fight against terrorism. After all, language by one author describing the insurgent who commits "piracy" as "not the enemy of the human race, but he is the enemy solely of a particular state" is preposterous. Such an "escape" enables the terrorist/insurgent to be absolved of his crimes if he is conveniently labeled an "insurgent." After all, Articles 15 and 16 of the 1958 Geneva

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90. Id.
91. Harvard Research in International Law, Comment to the Draft Convention on Piracy, 26 AM. J. INT'L. L. SUPP. 749, 786 (1932) [hereinafter Harvard Research].
92. 1958 Geneva Convention, supra note 74, art. 16. See Halberstam, supra note 75, at 278-79 (discussing implications of art. 16).
93. Harvard Research, supra note 91, at 857; Halberstam supra note 74, at 279 (reviewing analysis of comments).
94. Halberstam, supra note 75, at 279.
95. W. HALL, INTERNATIONAL LAW 234 (1st ed. 1884).
97. See Halberstam, supra note 75, at 288. "Insurgents who did not confine their attacks to ships and property of the government they sought to overthrow ... were considered pirates." Id. See also The Magellan Pirates, 164 Eng. Rep. 47 (1853) (discussing that depending on whom they attack, persons may be considered pirates or insurgents).
Convention provide that the distinguishing characteristic, given the same facts, between piracy and other crimes depends on whether the activities are for political ends.\textsuperscript{98} Thus, by excluding political acts from this international criminal designation, the world community is, in essence, approving of many national liberation movements' crimes.\textsuperscript{99} Such distinctions in the 1958 Geneva Convention must be reexamined since "personal security of life and property far outweigh the need for radical groups to prey upon the innocent."\textsuperscript{100}

In conclusion, since international law is forever evolving, its metamorphosis must include "[an] exemption for insurgents [which] would not exclude present-day terrorists, since it applied only to insurgents who confined their attacks to a particular state."\textsuperscript{101} Furthermore, as Sir Lauterpacht explained, "it would not seem improper to describe and treat as piratical such acts of violence on the high seas which by their ruthlessness and disregard of the sanctity of human life invite exemplary punishment and suppression."\textsuperscript{102}

\textbf{IV. FACTS SURROUNDING THE ACHILLE LAURO INCIDENT: A CASE STUDY}

On October 7, 1985, four armed men, allegedly members of the Palestine Liberation Front (PLF), a faction of the Palestine Liberation Organization (PLO), seized an Italian registered cruise ship, the Achille Lauro, in Egyptian territorial waters.\textsuperscript{103} The PLO hijackers, posing as passengers,
managed to board the vessel without any opposition. At the time of the seizure, approximately one hundred passengers, including twenty-eight Americans, and a crew of 350 were abroad.

According to some accounts, the seizure and terrorist activity on the Achille Lauro, some thirty miles off Port Said, Egypt, was not supposed to occur. Instead, the hijackers were part of a team, masterminded by Mohammed Abu Abbas, who intended to launch an attack in Ashdod, Israel. Apparently, as the terrorists were in their cabin taking stock of their weapons, other passengers entered their room. Consequently, the cadre was exposed, and the terrorists then decided to take control of the ship.

Upon securing control of the vessel, the PLO terrorists stated that they would blow up the Achille Lauro unless the Israeli government released fifty Palestinians held in Israeli jails. Although the terrorists probably foresaw Israeli nonacquiescence, they nevertheless stressed the seriousness of their demands. To underscore the ramifications of an Israeli refusal to release the jailed Palestinians, the hijackers brutally murdered an elderly, disabled American, Leon Klinghoffer. This unprovoked shooting, and subsequent discard of Mr. Klinghoffer (and wheelchair) overboard, marked the only fatality during the incident.

Negotiations attempted to find a resolution to the incident. Participants in the talks were Abu Abbas of the PLF, Ani el-Hassan, an adviser to PLO Chairman Arafat, Egyptian authorities, and the hijackers. On October 9, 1985, when the terrorists understood that the Israelis would not negotiate, and upon obtaining a guarantee of their immediate release, Egyptian authorities allowed Abbas to remove his comrades and accom-


105. Id.

106. Tagliabue, supra note 103; N.Y. Times, Oct. 11, 1985, § 1, at 1, col. 3.

107. Id.; N.Y. Times, Oct. 18, 1985, § 1, at 1, col. 6; McCredie, supra note 98, at 436.

108. McGinley, supra note 75, at 692.


112. Id., N.Y. Times, Oct. 11, 1985, § 1, at 1, col. 6. At a 1988 press conference in Algiers, Algeria, Abu Abbas, jokingly remarked that Mr. Klinghoffer "was trying to swim for it." Memorial Foundation, infra note 266, at 2.

pany them off the ship. The terrorists were then taken into custody by Egyptian authorities, although they were not arrested. The following day, the Egyptian government claimed that it no longer knew the whereabouts of the Palestinian hijackers. Despite these assurances by the Egyptians, various intelligence sources obtained convincing evidence that the terrorists had boarded an Egypt Air 737 flight to Tunisia. Following this exposition, the Egyptians argued that the hijackers were sent to Tunisia to stand trial before the National Ruling Council of the PLO. Additionally, the purpose of the proposed transfer from Egyptian to PLO forces was, according to Egyptian President Hosni Mubarak, an opportunity for Yasir Arafat to reiterate his denunciation of terrorism.

While the aircraft was in flight to Tunisia, President Reagan put pressure on the Tunisian government, causing the latter to deny the Egyptian plane the right to land. More specifically, President Reagan communicated to Tunisia that “the United States ha[d] reason to believe . . . that the hijackers were on board an EgyptAir plane headed for Tunis [Tunisia] . . . [and][that] the terrorists should not be allowed to land.” The Tuni­sians agreed. At the same time, U.S. Navy F-14 fighter planes forced the Egyptian aircraft to land at a North Atlantic Treaty Organization (NATO) air base in Sigonella, Sicily. At the tarmac in Sigonella, the U.S. Navy tried to obtain custody of the terrorists in order to transfer them to the U.S. to stand trial. Italian authorities intervened and the hijackers were ultimately taken into custody by the Italians. Subsequently, the Italian government asserted jurisdiction over the terrorists, and thus denied a

115. Id., supra note 114, at 33.
117. Id. at 20, 22-23.
119. Kilner, Mubarak, Furious at U.S., Demands a Public Apology, N.Y. Times, Oct. 15, 1985, at A10, col. 1. “If Arafat didn't punish them, then he would be responsible before the whole world.” Id.
122. U.S. Message, supra note 120 at 22; Gwertzman, U.S. Intercepts Jet Carrying Hijackers; Fighters Divert It To NATO Base in Italy; Gunmen Face Trial In Slaying of Hostage, N.Y. Times, Oct. 11, 1985, at A10, col. 6. “President Reagan . . . ordered the dramatic military action after hearing that Egypt had turned down repeated American pleas to prosecute the four gunmen and was flying them to freedom.” Id. (providing quote of Mr. Larry Speaks, White House spokes­man). See McGinley, supra note 75 at 708-713 (discussing jurisdictional claims of PLO to prose­cute Achille Lauro hijackers).
124. Id.
United States request for extradition. While some of the hijackers were awaiting trial in Spoleto, Italy, the Italians allowed Abbas to leave by way of Yugoslavia. Following his departure, Italian prosecutors issued arrest warrants for him. Although three of the thirteen individuals ultimately indicted in Italy in connection with the hijacking were given life sentences in absentia, the three other convicted hijackers were sentenced to 15, 24, and 30 years.

V. CIVIL SUITS ARISING OUT OF THE ACHILLE LAURO INCIDENT

A. KLINGHOFFER CAUSES OF ACTION AGAINST VARIOUS ACTORS IN THE ACHILLE LAURO INCIDENT

The Klinghoffer family has at different periods and in various manners, sued the PLO and other parties based on the Achille Lauro attack. More specifically, Mrs. Klinghoffer brought suits on behalf on herself and her husband in both the Supreme Court of New York and a federal district court, the Southern District of New York. Following her death, Mrs. Klinghoffer’s daughters maintained these suits in both jurisdictions on behalf on their parents and in their own privilege.

To get a better understanding of the scope of the Klinghoffer v. PLO litigation, it is important to review the various suits brought against other actors in the Achille Lauro incident.

1. ALL KLINGHOFFER SUITS EXCEPT THOSE IN WHICH THE PLO IS A DEFENDANT

A. SUIT BY MRS. KLINGHOFFER

This suit, filed in November 1985, alleged various grounds for recovery from the travel and transportation actors involved in the Achille Lauro incident. More specifically, Mrs. Klinghoffer brought causes of action


130. Id. at 107-27.

131. Id. at 107.
against: Commissaria of the Flotta Achille Lauro in Amministrazione Straordinaria; S.N.C. Achille Lauro Ed Altri-Gestione Motonave Achille Lauro in Amministrazione Straordinaria (jointly referred to as “Lauro”); Port of Genoa, Italy (“Genoa”); Club ABC Tours, Inc. (“ABC”); Chandris (Italy) Inc. (“Chandris”); and Crown Travel Service.132

In her complaint, Mrs. Klinghoffer set out the events on the Achille Lauro.133 Moreover, she described in graphic detail the harsh treatment which she (and other passengers) received.134 Specifically, she claimed that while on the Achille Lauro she was battered, assaulted, falsely imprisoned, and threatened with death.135 As a result of this harsh treatment, Mrs. Klinghoffer asserted that she should recover damages arising from acute pain and mental anguish, humiliation, anxiety, fright, depression, and the subsequent physical ramifications.136

Mrs. Klinghoffer proffered two theories for relief against Lauro, the owner of the ship.137 First, due to Lauro’s wrongful acts, recklessness, and negligence, she suffered the aforementioned injuries and damages.138 More specifically, Mrs. Klinghoffer noted that Lauro had failed to offer its passengers sufficient security (i.e., it failed to provide a thorough check and search of passengers, including their passports and belongings, during initial boarding in Genoa (October 3, 1985) as well as during subsequent stops).139 Second, Mrs. Klinghoffer alleged that Lauro caused her severe emotional distress by negligently permitting the terrorists to threaten her life.140

B. ESTATE OF MR. KLINGHOFFER V. LAURO

Pursuant to the Death on High Seas Act,141 Mrs. Klinghoffer, on behalf of her husband, initiated suit against Lauro.142 In that litigation she asserted that her husband’s death was a consequence of neglect, wrongful acts, and recklessness of Lauro.143 In claiming damages, including those to cover funeral expenses, the plaintiff asserted that during the takeover of the ship, Mr. Klinghoffer suffered severe emotional distress and physical pain, particularly when he was shot. Also, Mrs. Klinghoffer

132. No. 85 Civ. 9803 (LLS); id. at 107-08.
133. Id. at 108.
134. Id.
135. Id.
136. Id.
137. Id.
138. Id.
139. Id.
140. Id.
142. No. 85 Civ. 9303 (LLS; Goldie, supra note 128, at 109.
143. Id.
claimed recovery based on general maritime survival statutes and maritime wrongful death legislation.\textsuperscript{144}

\textbf{C. MRS. KLINGHOFFER V. ABC}

In this cause of action, Mrs. Klinghoffer insisted that ABC Tours breached its contractual obligations by failing to provide safe passage on the Mediterranean cruise.\textsuperscript{145} Such wanton behavior, Mrs. Klinghoffer asserted, as coupled with negligent security measures.\textsuperscript{146}

\textbf{D. ESTATE OF MR. KLINGHOFFER V. ABC}

The plaintiff herein alleged that ABC breached its contractual obligations and filed to comply with warranty provisions.\textsuperscript{147} As in Mrs. Klinghoffer's case against ABC, plaintiff asserted that the travel agent failed to arrange an adequately safe voyage and thereby acted outrageously and wantonly.\textsuperscript{148} Also, a negligence claim was brought stating that ABC knew or should have comprehended that the cruise had insufficient security.\textsuperscript{149} Lastly, this action rested on the allegation that ABC did not sufficiently explicate the limited liability asserted on the cruise tickets.\textsuperscript{150}

\textbf{E. MRS. KLINGHOFFER V. CHANDRIS}

In this suit against the charterer and common carrier of passengers on the Achille Lauro, Mrs. Klinghoffer stressed that Chandris was negligent in its failure to provide stringent inspection of persons, luggage, passports, and other security items.\textsuperscript{151} Furthermore, Mrs. Klinghoffer alleged that the negligent acts of Chandris were directly responsible for the emotional distress she suffered.\textsuperscript{152}

\textbf{F. ESTATE OF MR. KLINGHOFFER V. CHANDRIS}

In this cause of action, the Estate of Klinghoffer alleged that the death of Mr. Klinghoffer occurred as a result of wrongful acts, recklessness, and neglect by Chandris.\textsuperscript{153} This suit was also based on the Death on the High Seas Act.\textsuperscript{154}

\textsuperscript{144} Id.
\textsuperscript{145} No. 85 Civ. 9303 (LLS); Id. at 109-10.
\textsuperscript{146} Id.
\textsuperscript{147} No. 85 Civ. 9303 (LLS); Id. at 110.
\textsuperscript{148} Id.
\textsuperscript{149} Id.
\textsuperscript{150} Id.
\textsuperscript{151} No. 85 Civ. 9303 (LLS); Id. at 110-11.
\textsuperscript{152} Id.
\textsuperscript{153} Id. at 111.
\textsuperscript{154} Id.
G. MRS. KUNGHOFFER V. PORT OF GENOA, ITALY

Mrs. Klinghoffer alleged that the port was negligent in not providing appropriate security. More emphatically, there was insufficient inspection of luggage, passports, and passengers when boarding of the Achille Lauro. Furthermore, this subpar inspection led to the emotional distress which the plaintiff suffered.

H. ESTATE OF MR. KUNGHOFFER V. PORT OF GENOA, ITALY

The Estate of Mr. Klinghoffer as in other causes of action, claimed recovery pursuant to the Death on the High Seas Act. Also, the Estate sought compensation for pain and distress caused by the terrorists. Additionally, the Estate appended claims for recovery claiming wrongful death, pursuant to general maritime legislation.

2. KUNGHOFFER v. PLO: SUITS IN THE SUPREME COURT OF NEW YORK AND FEDERAL DISTRICT COURT (SOUTHERN DISTRICT OF NEW YORK)

The Estate of Mr. Klinghoffer also sued the PLO pursuant to the Death on the High Seas Act. Several other theories for recovery were also proffered: (1) recovery pursuant to the wrongful death precept in New York’s Estates Powers & Trusts Law; (2) maritime wrongful death, pursuant to general maritime law; (3) a tort claim of assault, based on the PLO’s intentional acts; (4) a battery claim; (5) an allegation of false imprisonment; (6) claims of intentional and negligent infliction of emotional distress.

Mrs. Klinghoffer asserted similar claims against the PLO, except for those based on wrongful death.

155. Id. at 112.
156. Id.
157. Id.
158. Id. at 112-13.
159. Id.
160. Id.
161. Id. at 113.
162. Id.
163. Id.
164. Id.
165. Id.
166. Id.
167. Supreme Court of New York, New York County, Civil Action No. 27801/85.
B. THIRD PARTY COMPLAINT OF CHANDRIS AGAINST THE PLO AND THE PORT OF GENOA, ITALY

In response to the suits filed against it by the Klinghoffers, Chandris filed third-party complaints, in which it sought indemnity or contribution, from the PLO and the Port of Genoa, Italy. In this third-party complaint, Chandris sought contribution or indemnity from the PLO, based on its negligence, intentional conduct, wrongful acts, and recklessness.

In classifying the PLO as an unincorporated association, Chandris further stated that the terrorist organization "conceived, conspired, organized, authorized and directed its agents, servants, officers, employees and operatives to willfully, wantonly and maliciously" capture the Achille Lauro, and subsequently caused Mr. Klinghoffer's death. Additionally, Chandris proffered that the PLO's activities in the Achille Lauro affair constituted a crime, an intentional tort, and an activity hostis humani generis, thereby making the PLO responsible for damages in excess of $10,000.

Three jurisdictional prongs were used in this case: 28 U.S.C. section 1331 (providing federal jurisdiction due to federal question), 28 U.S.C. section 1332 (establishing federal jurisdiction based on diversity of citizenship), and 28 U.S.C. section 1333 (fixing federal jurisdiction due to admiralty and maritime laws).

Lastly, Chandris stated that the Port of Genoa, Italy, does not possess the sovereign immunity defense, and consequently should indemnify or contribute for its failure to sufficiently inspect the passengers of the Achille Lauro.

VI. THE JUNE 1990 ORDER OF THE SOUTHERN DISTRICT OF NEW YORK IN KLINGHOFFER V. PLO

A. INTRODUCTION

Passengers on the Achille Lauro, filed suits in federal district court in New York, alleging that "the owner and charterer of the Achille Lauro, travel agencies and various other entities" failed to notify passengers or thwart the attack. Among these suits was one brought by Mrs. Marilyn

170. Id.; NYEPTL, supra note 164, at § 11-3.2.
171. Id.
172. Id.
173. Id.
Klinghoffer. 176

In the Klinghoffer action, jurisdiction was proffered on several prongs: the Death of the High Seas Act,177 diversity of citizenship, and state law.178 In response to the suit, the Crown Service Travel, Inc. and Chandris, Inc. impleaded the PLO, calling for contribution or indemnification for reparations imposed against them based on the passengers' suits as well as for punitive and compensatory damages for the PLO's "tortious interference with their businesses."179

The PLO moved to dismiss the suit. They asserted that: (1) there was no subject matter jurisdiction because this case presents a nonjusticiable political question; (2) there was no personal jurisdiction over the PLO; (3) the PLO, assuming that it is an unincorporated association, lacked the capacity to be sued; and (4) service of process on Mr. Terzi, PLO Permanent Observer, in New York was insufficient.180

Judge Stanton, in a pithy ten-page order, denied the PLO's motion to dismiss. He first ruled that the PLO is not a foreign state, but rather an unincorporated association. Next, the court concluded that the subject matter of the case includes tort claims arising from federal admiralty law and, as a result, the political question doctrine is inapplicable.181 Additionally, the court determined that section 301 of New York's Civil Practice Law and Rules (C.P.L.R.) granted it jurisdiction over the PLO, which according to the statute was "doing business" in the state.182 Furthermore, because "substantial, continuous, and purposeful contacts with New York could be attached to PLO activity, the exertion of jurisdiction over the terrorist organization amply accords due process.183 The court denied PLO claims that its U.N. Observer status accorded it diplomatic immunity under the U.N. Headquarters Agreement.184

Next, since the suit was brought under federal maritime law, federal law is applicable for substantive issues, rather than the state law of where the court sits.185 Finally, the court upheld the service of process upon Mr. Terzi finding that his position in the U.N. classified him as an agent of the

176. Id. at 856 n.1. The court noted that upon Mrs. Marilyn Klinghoffer's death, her daughters Lisa Klinghoffer and Lisa Klinghoffer Arbitter, were substituted as plaintiffs. Id.
178. See S.N.C. Achille, 739 F. Supp. at 857 (citing various bases of jurisdiction in Klinghoffer action). "Later, other Achille Lauro passengers filed two actions directly against the PLO alleging diversity of citizenship jurisdiction." Id.
179. Id. at 857.
180. Id. at 858.
181. Id. at 858-60.
182. Id. at 860-63.
183. Id. at 865.
184. Id. at 863-5.
185. Id. at 864-6.
PLO under section 301 of New York C.P.L.R.\textsuperscript{186}

B. \textsc{The Nature of the PLO}

Concerning its classification for litigation, the PLO implored the court to adopt its self-description as a state.\textsuperscript{187} More specifically, the PLO characterized itself as "the nationhood and sovereignty of the Palestinian people."\textsuperscript{188} Consequently, the PLO sought designation as a sovereign nation. Nevertheless, the court found the PLO to be an unincorporated association.\textsuperscript{189} Support for this classification was articulated through the citation of \textit{Motta v. Samuel Weiser, Inc.}\textsuperscript{190} and \textit{Health Care Equalization Comm. v. Iowa Medical Soc'y.}\textsuperscript{191}

More persuasive than the court's finding that the PLO was an unincorporated association, however, was the court's finding that the PLO was not a sovereign state.\textsuperscript{192} The court determined that the PLO lacked the key elements of nationhood, as articulated by international law. International law requires that a state must be "an entity that has a defined territory, and a permanent population, under the control of its own government, and that engages in, or has the capacity to engage in, formal relations with other such entities."\textsuperscript{193} Because the PLO does not comport with the standard definition of a state, for purposes of this litigation, the PLO was classified as an unincorporated association.\textsuperscript{194}

C. \textsc{Subject Matter Jurisdiction}

The court found subject matter jurisdiction on several bases.\textsuperscript{195} Admiralty jurisdiction was established since the Achille Lauro incident involved torts, including wrongful death, on the high seas.\textsuperscript{196} As 28 U.S.C. section 1333 provides: "district courts shall have original jurisdiction, exclusive of the courts of the States of: (1) Any civil case of admiralty or

\begin{footnotesize}
\begin{enumerate}
\item \textsuperscript{186} id. at 867.
\item \textsuperscript{187} id. at 857-8.
\item \textsuperscript{188} id. at 857, (citing Affidavit of attorney for PLO Ramsey Clark sworn to April 27, 1987, ¶6).
\item \textsuperscript{189} id. at 858.
\item \textsuperscript{190} Motta v. Samuel Weiser, Inc., 768 F.2d 481, 485 (1st Cir. 1985) (citing Black's Law Dictionary 111 (5th Ed. 1979)), cert. denied, 474 U.S. 1033, 106 S. Ct. 596, 88 L.Ed. 2d 575 (1988). "An unincorporated association is defined as a body of persons acting together and using certain methods for prosecuting a special purpose or common enterprise." id.
\item \textsuperscript{191} Health Care Equalization Comm. of Iowa Chiropractic Soc'y v. Iowa Medical Soc'y, 501 F. Supp. 970, 976 (S.D. Iowa 1980), aff'd, 851 F.2d 1020 (8th Cir. 1988).
\item \textsuperscript{192} S.N.C. Achille, 739 F. Supp. at 858.
\item \textsuperscript{194} S.N.C. Achille, 739 F. Supp. at 858.
\item \textsuperscript{195} id. at 158-59.
\item \textsuperscript{196} id. at 859.
\end{enumerate}
\end{footnotesize}
maritime jurisdiction, saving to suitors in all cases and all other remedies to which they are otherwise entitled." Further support for the court’s finding admiralty jurisdiction was provided by American Hawaiian Ventures, Inc. v. M.V.J. Latuharhory which noted that “every seizure by force on the high seas is prima facie piracy, and hence, a maritime tort.” The court also determined subject matter jurisdiction exists over the Klinghoffers’ suits since the Death on the High Seas Act provides jurisdiction over causes of actions for wrongful death on the high seas.

D. THE POLITICAL QUESTION DOCTRINE

The PLO also argued that this suit was not justiciable because it involved foreign policy questions which are outside the court’s jurisdiction; such issues, the PLO continued, are best left to other sectors of government. To support this political question argument, the PLO relied upon Tel-Oren v. Libyan Arab Republic. In Tel-Oren, the D.C. Circuit dismissed civil suits arising from attacks on civilians by the PLO, other Palestinian organizations, and Libya. The Tel-Oren court determined that such suits would require political evaluations of “terrorism’s place in the international order” and therefore must be dismissed. The D.C. Circuit reasoned that a judgment on the activities of Libya and the PLO could interfere with U.S. foreign policy, an area exclusively controlled by the President and Congress.

However, Judge Stanton distinguished the facts of Tel-Oren from the Achille Lauro setting, by noting that the potential harmful effects of assessing the justiciability of the Achille Lauro suit were minimal. Moreover, Judge Stanton explained that simply because political ramifications

197. 28 U.S.C. § 1333 (1982). Also, the court determined that pursuant to the "savings to suitors" clause (§1333), plaintiff can bring a cause of action for maritime torts in federal or state court. Id., citing Keefe v. Bahama Cruise Line, Inc., 867 F.2d 1318, 1321 (11th Cir. 1989).
199. Id. at 627.
201. Id. The political question precept was well-described in Baker v. Carr, 369 U.S. 186, 217, 82 S. Ct. 691, 710, 7 L.Ed.2d 663 (1962).
203. Id. at 823.
204. Id. at 824-25.
205. S.N.C. Achille, 739 F. Supp. at 860. "None of those considerations [of those listed in Tel-Oren] is present here. The PLO has condemned the Achille Lauro seizure and stated that it was an act of piracy. It was not at war with either Italy or the United States. No party asserts that the Achille Lauro seizure was legitimate." Id.
and foreign affairs are involved does not mean that political questions exist.\textsuperscript{206} In sum, Judge Stanton held that seizure of the Achille Lauro, resulted in non-political personal and property tort claims. Therefore, the "policy choices and value determinations constitutionally committed for resolution to the halls of Congress or the confines of the Executive Branch"\textsuperscript{207} would not be disturbed.

\textbf{E. PERSONAL JURISDICTION}

The Southern District of New York has stated several times that, in admiralty claims, personal jurisdiction is set according to state law. Consequently, Judge Stanton explained that New York C.P.L.R. section 301 could legitimately confer personal jurisdiction over the PLO.\textsuperscript{208} Although no court had specifically applied section 301 to an unincorporated association, nonresident individuals doing business in New York had been subjected to jurisdiction under this section by a federal district court.\textsuperscript{209} Additionally, New York general associations law permits suits against unincorporated associations by designation of either its treasurer or president.\textsuperscript{210} This vital precept, in conjunction with reports that New York C.P.L.R. 301 jurisdiction could be expanded, even to non-corporate defendants "doing business" in New York, lends support to Judge Stanton's subject matter jurisdiction determination.\textsuperscript{211}

Judge Stanton set out the relevant legal precedent prior to determining the applicability of section 301 and whether the PLO was "doing business in the state."\textsuperscript{212} As described in \textit{McGowan v. Smith},\textsuperscript{213} defendants who engage in continuous and systematic conduct may be classified as "doing business" under section 301.\textsuperscript{214} Furthermore, \textit{Andrulonis v. United States}\textsuperscript{215} illustrated that should a court determine that, under section 301, a defendant is doing business in New York, suits may arise on claims whether or not they are connected to the New York activities.\textsuperscript{216} In

\begin{itemize}
\item \textsuperscript{206} \textit{Id.} at 860. To support this argument, Judge Stanton cited \textit{Baker v. Carr}, 369 U.S. at 212, 82 S. Ct. at 710 ("The doctrine of which we treat is one of political questions, not one of political cases.").
\item \textsuperscript{208} \textit{S.N.C. Achille}, 739 F. Supp. 861.
\item \textsuperscript{209} \textit{Id.}; \textit{Diskin v. Starck}, 538 F. Supp. 877, 880 (E.D.N.Y. 1982).
\item \textsuperscript{210} \textit{Id.}; \textit{N.Y. Gen. Ass'n's Law § 13} (McKinney 1942 & Supp. 1990).
\item \textsuperscript{211} \textit{S.N.C. Achille}, 739 F. Supp. at 862; \textit{1 Weinstein, Korn & Miller, New York Civil Practice ¶301.15, at 3-30 through 31}.
\item \textsuperscript{212} \textit{S.N.C. Achille}, 739 F. Supp. at 862.
\item \textsuperscript{213} 52 N.Y.2d 268, 437 N.Y.S. 2d 943, 419 N.E.2d 321 (Ct. App. 1981).
\item \textsuperscript{214} \textit{S.N.C. Achille}, 739 F. Supp. at 861.
\item \textsuperscript{215} 528 F. Supp. 183, 190 (N.D.N.Y. 1981).
\item \textsuperscript{216} \textit{S.N.C. Achille}, 739 F. Supp. at 862.
\end{itemize}
the present case, the court determined that the PLO's contacts with New York are constant and substantial.217 More specifically, the court noted that the PLO: owns a building in New York City, utilized both as an office and residence; maintains back accounts; has a telephone listing; owns automobiles; and has employees in Manhattan.218 Such purposeful and significant connections with New York adequately abide with the standards set out in section 301.219

F. PLO'S CLAIM OF IMMUNITY

The court did not accept the PLO's claims of immunity from suit due to its position as a U.N. Observer.220 The PLO's suggestion that its actions are immune from scrutiny because of section 15 of the U.N. Headquarters was rejected.221 As the court explained, section 15 of the Headquarters Agreement applies only to United Nations members; the PLO is not such a member. Also, other immunities and privileges accorded U.N. representatives and their staffs are limited to those "performed in the exercise of the [PLO's] observer function" not "to [those] matters completely unrelated to the presence."222 Consequently, the PLO's immunity defense was rejected.223

G. DUE PROCESS

Regarding due process implications of New York C.P.L.R. section 301, the PLO was deemed to have sufficient contacts with New York.224 Thus, the causes of action initiated by plaintiffs in New York would not infringe upon the standard of "traditional notions of fair play and substantial justice," the precept enunciated in International Shoe Co. v. Washington.225

H. CAPACITY TO BE SUED

Because these maritime tort suits are based on either admiralty or diversity jurisdiction, federal maritime statutes, not state legal precepts, are applicable.226 Consequently, jurisdiction over the PLO is available since case law provides that plaintiffs have a cause of action against an

217. S.N.C. Achille, 739 F. Supp. at 863.
218. Id.
219. Id.
220. Id. at 863-64.
221. Id.
222. Id. at 864.
223. Id.
224. Id. at 865.
225. 326 U.S. 310, 316, 66 S. Ct. 154, 158, 90 L.Ed. 95 (1945).
unincorporated association in its own name, despite the lack of provisions by state law. Furthermore, Federal Civil Procedure Rule 17(b) allows both plaintiffs to initiate suit against the PLO in its own name.

I. SERVICE OF PROCESS

The last issue before Judge Stanton was whether Federal Civil Procedure Rule 4 guidelines were followed during service of process on the PLO’s agent Mr. Terzi. First, Judge Stanton stated that Rule 17(b)(1) permits the cause of action against the PLO to be designated in its common name. Second, Rule 4(d)(3) authorized Mr. Terzi to receive service process. Furthermore, federal law stipulates that “service is sufficient when made upon an individual who stands in such a position as to render it fair, reasonable, and just to imply the authority on his part to receive service.” Therefore, the court observed, since Mr. Terzi was responsible for the PLO’s extensive New York functions, service upon the PLO complied with Rule 4(d)(3).

VII. ANALYSIS OF KLINGHOFFER V. PLO

In the Klinghoffer litigation, Judge Stanton ruled that the Death on the High Seas Act was an appropriate springboard to obtain subject matter jurisdiction. Yet, complex arguments regarding the role of state law in Death on the High Seas Act cases demonstrate the need for further development of the law concerning this issue. Section 7 of the Death on the High Seas Act provides that “[t]he provisions of any State statute giving or regulating rights of action or remedies for death shall not be affected by this chapter.”

Recent cases have ascribed that even if the Death on the High Seas Act applies, state courts may have concurrent subject matter jurisdiction. More specifically, in Lowe v. Trans World Airlines, Inc., the

227. Id. at 866 (citing Busby v. Electric Utilities Employees Union, 323 U.S. 72, 73-74, 65 S. Ct. 142, 143-44, 89 L.Ed. 142 (1944)).
228. S.N.C. Achille, 739 F. Supp. at 806 n.9.
229. Id. at 866.
230. Id. at 867.
232. S.N.C. Achille, 739 F. Supp. at 867. Once again, the Court also cited C.P.L.R. § 301, to emphasize that the PLO was “doing business” in the state. Id.
233. Id.
234. See supra notes 192-93 and accompanying text.
237. Goldie, supra note 235, at 129.
Southern District of New York determined that, in causes of action involving suits when deaths take place beyond territorial waters, the Death on the High Seas Act is not the sole jurisdictional statute. In fact, the court in Lowe acknowledged that a plaintiff can bring suit based on state law. Similarly, in Rairigh v. Erlbeck, the court determined that federal and state courts have concurrent jurisdiction in wrongful death suits. Support providing states with jurisdiction for wrongful death suits on the high seas was provided by a recent U.S. Supreme Court decision. More specifically, in Morange v. State Marine Lines, Inc., the Supreme Court of the U.S. concluded that general maritime law acknowledges a cause of action for wrongful death on all navigable waters, including a state's territorial and internal waters, and on the high seas.

Despite the apparent breadth of concurrent jurisdiction. Justice O'Connor in 1986 reiterated the role of section 7 in the Death on the High Seas Act. More particularly, the U.S. Supreme Court advocated in Offshore Logistics v. Tallentire that "the language of section 7 and its legislative history, as well as the congressional purposes underlying DOHSA, mandate that section 7 be read not as an endorsement of the application of state wrongful death statutes to the high seas, but rather as a jurisdictional saving clause. Viewed in this light, section 7 serves not to destroy the uniformity of wrongful death remedies on the high seas but to facilitate the effective and just administration of those remedies." This pronouncement supports Judge Stanton's finding of federal jurisdiction pursuant to the Death on the High Seas Act.

VIII. U.S. LEGISLATIVE RESPONSES TO TERRORISM

A. INTRODUCTION

A bill recently considered by Congress, S. 2465, for the first time creates a civil cause of action for U.S. victims of international terrorist incidents against the perpetrators of this violence. Support for S. 2465

239. Id.
240. Id.
242. Id.
245. Id.
246. DOHSA, supra note 235, at 131-34.
248. Id. at 231-32.
249. Id.
250. See supra notes 192-94 and accompanying text.
was fervently expressed by two senators who introduced the bill in April 1990, Senator Charles E. Grassley and Senator Howell Heflin. At the Senate Subcommittee hearing on July 25, 1990, Senator Grassley explained that the impetus for S. 2465 was the outrage and tragedy faced by families of American victims of terrorism. Namely, Senator Grassley stated:

We must understand that the victims of Pan Am 103, Mr. Klinghoffer, and others, were victims because they were Americans; they died because they were Americans. We must do all we can to assist and comfort the family of American victims. And it also seems to me that we ought to make it clear to the world how we feel about the taking of American lives.

While acknowledging that United States law, including 18 U.S.C. section 2331 (1988), allows for extraterritorial criminal jurisdiction for acts of international terrorism, Senator Grassley pointed out that legislation providing comparable civil remedies do not exist. The Senator concluded by stating that S. 2465 would provide a legislative tool by which American victims of terrorist incidents could have a cause of action against their attackers.

[S. 2465] sends a strong and clear message to the world on how the American legal system deals with terrorists... S. 2465 empowers the victims of terrorism to seek justice. It gives them the right to have their day in court to prove who is responsible for all the world to see. S. 2465 is clear, express and equivocal; this legislation reaffirms our commitment to the rule of law. With this law, the people of the United States will be able to bring terrorists to justice the "American Way." By using the framework of our legal system to seek justice against those who follow no framework and defy all notions of morality and justice.

Additionally, Senator Grassley agreed with the June 7, 1990, court order in *Klinghoffer v. PLO* in which Judge Stanton held that the American judicial system has personal jurisdiction over the PLO. While noting that this case is a landmark event, the Senator declared his concern that Klinghoffer might not be followed. Subsequently, Senator Grassley


\[\text{253. Grassley, supra note 252, at 2.}\]

\[\text{254. Id.}\]

\[\text{255. Id.}\]

\[\text{256. Id.}\]

\[\text{257. Id. at 3.}\]

\[\text{258. Id. at 2.}\]

\[\text{259. Id. at 2-3.}\]
opined that federal legislation, particularly S. 2465, was the only manner in which to empower Americans with litigate responses to terrorism. In this way, "a strong warning to terrorists [is sent] to keep their hands off Americans and an eye on their assets!" 

Senator Heflin, co-sponsor of the bill, similarly stated his support for S. 2465. Pointing to the past decade of American victimization by international terrorists, Senator Heflin pronounced that U.S. criminal sanctions must be complemented with civil remedies. Consequently, Senator Heflin claimed that by amending 18 U.S.C. section 2331, S. 2465 would provide American plaintiffs civil causes of action in U.S. federal courts, for injuries sustained during a terrorist act. Only in this manner, Senator Heflin added, can victims of terrorism obtain some monetary compensation for their physical and mental injuries.

B. COMMENTS ON S. 2465 BEFORE THE U.S. SENATE JUDICIARY COMMITTEE, SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICES

1. TERRORIST VICTIMS' FAMILIES

Adding some pathos and personal experience to the terrorism debate, family members of victims of international terrorist activities were provided with a forum to express their views on S. 2465. The first panel included Lisa Klinghoffer, daughter of Leon and Marilyn Klinghoffer, victims of the Achille Lauro incident. Speaking on behalf of the Leon and Marilyn Memorial Foundation of the Anti-Defamation League, Ms. Klinghoffer stated that S. 2465 serves both symbolic and practical purposes. On a global arena, the bill would support criminal sanctions for international terrorist acts against U.S. citizens, while at the same time, send a clear signal that Americans will not tolerate being the victims of terrorism. Additionally, the bill would exhibit the legislature's commit-

260. Id. at 3.
261. Id.
263. Id. at 1.
264. Id.
265. Id. at 2.
267. Memorial Foundation, supra, note 266, at 1.
268. Id. at 1-2.
269. Id. at 2.
ment to fighting terrorism. On a practical level, the bill would provide U.S. plaintiffs with clear statutory solutions.

Ms. Klinghoffer reviewed the difficulties which her family had in filing suit against the PLO. Since U.S. statutes did not provide an explicit civil cause of action against terrorists, the Klinghoffers were forced to litigate numerous procedural issues. The Klinghoffers finally obtained a ruling allowing for jurisdiction over the terrorist group, but only after much difficulty. The aforementioned bill would cure present deficiencies in U.S. law by also allowing civil suits against state-sponsors of terrorism. Additionally, the bill would provide recovery of treble damages as well as permit the recovery of attorney fees.

The next family member of a victim of terrorism to testify on S. 2465 was Rosemary Wolfe. Ms. Wolfe was the stepmother of Miriam Wolfe, a twenty-year-old college student who was one of the 269 passengers aboard Pan Am 103 when it blew up over Scotland in 1988. In Ms. Wolfe's view, prosecution and punishment of terrorists and their state-sponsors are often not pursued by the U.S. government for political reasons. For instance, Ms. Wolfe noted that although the "smoking gun" from Pan Am 103 can be traced to both the government of Iran and Ahmed Jibril, it is a lack of political resolve which prevents these terrorist perpetrators from being brought to justice. The lack of faith in the U.S. government's will to adequately punish terrorists led her to conclude that "[f]amilies of the victims of terrorism need . . . civil recourse in the courts. For this may be our only recourse."

Another group representing the families of victims of Pan Am 103 described their support for S. 2465. Mr. Paul Hudson testified on be-

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270. Id.
271. Id.
272. Id. at 2.
273. Id. at 4.
274. Id.
275. Id. at 4.
276. Id.
277. Wolfe, supra at 266.
278. Id. at 1.
279. Id. at 2-3.
280. Id. "Mr. Sofaer, legal adviser to the Secretary of State from June of 1985 until last month, acknowledges that Iran had responsibility in the bombing of Pan Am 103 over Lockerbie on December 21, 1988. Yet, for the past year and a half our government has refused to point the finger of blame. The madmen who murdered our precious children and all our love ones, including my stepdaughter Miriam Wolfe, go free and unpunished. In the process, we refuse to deal with Iran's involvement. Can Iran's involvement in the bombing of Pan Am 103 be acknowledged by U.S. officials only once they have resigned?" Letter to the Editor, Wolfe, Denying Iran's Role in Pan Am Flight 103, Wash. Post, July 13, 1990, at A20.
281. Wolfe, supra note 266, at 3.
282. See Hudson, supra note 266.
half of the families and noted that S. 2465 would empower victims of terrorism and break down the shields which have protected terrorists from U.S. civil justice. 283 Furthermore, Mr. Hudson stressed his concern that the U.S. government should act as co-plaintiff in civil litigation against terrorists, although control of the suit should remain with the victims' families. 284 Without the strict support of this legislation, as well as U.S. government approval, subsequent suits against extra-legal force could yield "tragedy as well as frustration." 285

2. DEPARTMENT OF STATE

The Department of State's position on S. 2465 was presented by Mr. Alan J. Kreczko, Deputy Legal Advisor. 286 Mr. Kreczko noted that the benefits of the Grassley-Heflin bill are manifold. 287 First, the legislation will give victims of terrorism civil remedies in U.S. courts, and present disincentives for terrorists. 288 Consequently the breadth of statutory tools against terrorism would be augmented. Second, the potential of civil liability and asset confiscation could deter terrorist groups from both soliciting and maintaining assets in the U.S. 289 Third, the Grassley-Heflin bill could be mimicked by other national legislatures, thereby expanding international resolve against terrorism. 290 Fourth, this civil cause of action could be pursued in instances when criminal prosecution, due to a higher evidentiary standard, would be precluded. 291

While acknowledging general support for this legislation, Mr. Kreczko asserted that further revisions were needed before the State Department could fully support the bill. 292 More specifically, Mr. Kreczko expressed his doubts about the practicability of the legislation, since he believes that few terrorists could be caught travelling to the U.S. or holding assets in U.S. based banks. 293

The major concerns, as expressed by Mr. Kreczko, are credible and weighty. 294 Serious concern exists regarding the possibility that the

283. Id. at 1.
284. Id. at 2.
285. Id.
287. Id. at 5.
288. Id.
289. Id. at 5-6
290. Id.
291. Id.
292. Id. at 5-6.
293. Id. at 6.
294. See infra notes 295-307 and accompanying text.
Grassley-Heflin bill would be used in suits against sovereign nations and their officials. Thus, the State Department favored the addition of a provision, section 2336(b), which would prohibit the bill from applying to foreign states, defined under the Foreign Sovereign Immunities Act as well as "any offices or employees thereof." The State Department's rationale was several fold. Most obviously, the feasibility of civil suits in U.S. courts against foreign countries or officials, based on their alleged terrorist acts, could generate severe terrorism against U.S. interests, including U.S. allies. A pronouncement by U.S. courts over foreign states would be highly disfavored by a majority, if not all, of the foreign states. Moreover, Mr. Kreczko argued that such jurisdiction is violative of the international principle of sovereign immunity recognized by U.S. law. He similarly argued that a provision must be placed in the Grassley-Heflin bill which would prevent plaintiffs from skirting through suits against foreign government officials.

Another argument voiced against a change in the sovereign immunity precept vis-a-vis the Grassley-Heflin bill stems from the reciprocity of other legislation. For instance, foreign countries, or their citizens, as defendants to potential S. 2465 claims could respond with reciprocal statutory schemes which would ultimately serve to label the U.S. or its citizens as terrorists. Another drawback to allowing civil suits in U.S. courts against nations or their officials charged with being terrorists is that such strategic and highly sensitive positions should be articulated by the U.S. government, rather than by private individuals.

Finally, Mr. Kreczko explained the State Department's uneasiness with the possibility that frivolous and gadfly suits could arise based on alleged terrorist activities by foreign officials and their governments. For instance, this tool could be utilized by dissident groups and others to gain publicity while at the same time harming U.S. relations with other governments. Also, numerous lengthy suits initiated against foreign governments and their officials could ultimately cause a severe financial

295. id. at 6.
296. id.
297. id. at 7.
298. id.
299. id.
300. id.
301. id. at 7-8.
302. id. at 8.
303. id.
304. id. at 8-9.
305. id. at 9.
306. id.
strains on them.307

3. **DEPARTMENT OF JUSTICE**

The Department of Justice ("DOJ") also provided its view on S. 2465.308 Mr. Steven R. Valentine, Deputy Assistant Attorney General, Civil Division, explained that the DOJ generally supported S. 2465's design to redress harms to Americans caused by terrorists through civil litigation.309 Yet he stated that the DOJ also had reservations concerning several provisions of the Grassley-Heflin bill.310 This apprehension dealt with those suits that could result in conflicts between civil actions by private citizens and the law enforcement efforts of the United States.311

The DOJ feared that civil suits proposed under 18 U.S.C. section 2333 of the bill would obstruct criminal litigation.312 Civil suits under the bill would involve the testimony of vital government witnesses who could compromise ongoing investigations or prosecutions.313 Moreover, during discovery proceedings, delicate information could be exposed, and prosecutors would be forced to reply to time consuming civil discovery requests.314 Thus, the DOJ proposed that a provision be included in the bill to allow "the Attorney General to certify that discovery of the government's criminal investigative file in a terrorist incident ... will compromise the criminal investigation or national security interests."315 Such a certification would be forwarded to the court where the civil suit would be pending and thus preclude the discovery of such information.316

Further safeguards proposed by the DOJ include amendments which would insure that, if a civil cause of action interferes with national security interests or a returned indictment concerning the same amendment as the civil action, "the Attorney General can, upon good cause shown, request the court were [sic] the civil litigation is pending to stay that litigation until completion of the criminal proceedings or the elimination of the predicate

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307. *Id.*
309. *Id.* "We support the major concepts embodied in S. 2465. The Department [of Justice] supports legislation to provide a new civil remedy against terrorists and a federal forum for the families and relatives of victims to pursue claims for compensatory damages. Such a cause of action will assist in compensating victims, and have a deterrent effect on the commission of acts of international terrorism against Americans." *Id.* at 6.
310. *Id.* at 7.
311. *Id.* at 7.
312. *Id.*
313. *Id.*
314. *Id.*
315. *Id.*
316. *Id.*
national security interest concern."317 The DOJ also recommended that the Attorney General should have the authority to serve complaints and summons in civil suits.318 Potential detriment could result, however, since the Attorney general's participation in civil suits would be limited. A stay of civil litigation would not exclude the commencement of a lawsuit within the statute of limitation period proposed in 18 U.S.C. section 2335.319 Additionally, a stay of the civil suit would actually assist the U.S. plaintiff because he could take advantage of proposed estoppel terms of 18 U.S.C. section 2333(b).320

Furthermore, the DOJ echoed the State Department's position that the bill should neither apply to governments nor their officials.321 The DOJ also stated that S. 2465 provisions which permit jurisdiction against foreign nation's officials to sue derivatively for acts of the foreign state must be modified. The DOJ also shares the State Department's concern about the potential for reciprocal action by other nations.322

The DOJ proposed two other minor additions. First, it recommended that district courts should have original and exclusive jurisdiction in suits falling under 18 U.S.C. section 2333.323 Second, it proposed to modify 18 U.S.C. section 2333 to permit the decedents, survivors, and heirs of terrorist victims, as well as those individually injured, to bring suit.324

4. ACADEMIC TESTIMONY

Further comments on S. 2465 were provided by Professor Wendy Perdue of Georgetown University Law Center.325 Prof. Perdue's comments centered on jurisdictional issues.326 This technical advice focused on defendants in litigation, venue, and forum non conveniens.327 Prof. Perdue noted that recovery of damages from terrorists will be related to the scope of reachable assets in the United States.328 She stated that if a reasonable recovery is envisioned, liability must reach "foreign governments or government run enterprises that engage in or support terror-

317. Id. at 8.
318. Id.
319. Id.
320. Id. at 9.
322. Valentine, supra note 308, at 9.
323. Id. at 10.
324. Id.
326. Id. at 6-8.
327. Id.
328. Id. at 6.
"ism," rather than just the individual terrorist perpetrators. Prof. Perdue acknowledged that such a scenario would require modifications to the Foreign Sovereign Immunities Act.

Prof. Perdue further remarked that suits could be brought, *inter alia*, where "all plaintiffs reside." Since a provision could result in duplicate cases being tried separately, Prof. Perdue recommended that a preferable venue scheme would be "where any plaintiff resides." Similarly, she found fault in the bill's language that "[venue is proper where] the defendant resides, is found, or has an agent." She suggested that jurisdiction should be defined as the place "where any defendant resides or is found." Prof. Perdue explained that there is a lack of clarity in the language relating to where the terrorist would be served with process. Furthermore, she suggested that the service of process provision would be amended to read as follows: Proper service exists in any district where the defendant resides, is found, or has an agent. Finally, Prof. Perdue stated that the *forum non conveniens* provision, section 2334(c), would revise the confusing alternative forum guidelines ("mere convenient or more appropriate") to the standards proffered in *Gulf Oil Corp. v. Gilbert*.

C. **S. 2465 AS PASSED IN OCTOBER 1990**

On October 1, 1990, the Senate unanimously passed the revised version of S. 2465, discussed on July 25, 1990, at the Senate Subcommittee on Courts and Administrative Practice. The bill was passed as an amendment to the Military Construction Appropriations Bill.
As the preamble to S. 2465 indicates, the bill "provide[s] a new civil cause of action in federal law for international terrorism that provides extraterritorial jurisdiction over terrorist acts abroad against United States nationals." The bill supplements existing legislation which extends criminal sanctions to international terrorist activities. Specifically, proposed 18 U.S.C. section 2333(a), would permit U.S. nationals, or their estates, survivors, or heirs, whose person, business, or property has been hurt due to an international terrorist incident, to sue in federal district court and obtain treble damages, as well as the cost of the litigation, in conjunction with attorney's fees. Moreover, special maritime or territorial jurisdiction is provided through 18 U.S.C. section 2334(b).

The bill provides that proper venue over potential defendants is "where any plaintiff resides or where any defendant resides or is served, or has an agent." The bill also states that service of process may occur "where the defendant resides, is found, or has an agent." Witnesses in a 18 U.S.C. section 2333(a) cause of action could also be served in the same procedure as the defendant. These broad provisions would substantially ease prospective plaintiff's jurisdictional and venue problems. Moreover, said provisions address Prof. Perdue's concerns with the ambiguous language of early versions of the Grassley-Heflin bill regarding service of process.

Prof. Perdue's misgivings relating to forum non conveniens also appears to have been addressed by proposed section 2334(d). For instance, this provision would provide that a court not dismiss a section 2333 action merely because a plaintiff chose an inappropriate or inconvenient forum. However, if the court determines that three thresholds have been met, then dismissal is proper. The circumstances which justify expulsion of the suit include: "(1) The action may be maintained in a foreign court that has jurisdiction over the subject matter and over all

341. See supra notes 255, 263 and accompanying text.
343. Id. § 2334(b).
344. Id. § 2334(a).
345. Id. § 2334(c).
346. Id. § 2334(a).
347. Once venue difficulties are lessened, fewer obstacles will exist to U.S. nationals who sue terrorists in the U.S. as the Anti-Terrorism Act of 1990 would have provided.
348. See supra notes 335-67, and accompanying text.
349. See supra note 338 and accompanying text; Anti-Terrorism Act, supra note 340, at 18 U.S.C. § 2334(d).
351. Id.
the defendants; (2) the foreign court is significantly more convenient and appropriate; and (3) [the] foreign court offers a remedy which is substantially the same as the one available in the courts of the United States.\footnote{352} It is necessary to note that proposed sections 2334(d)(1)-(3) are drafted in a highly pro-plaintiff, anti-case dismissal approach. A case in point is present under section 2334(d)(3)'s language that would not permit dismissal unless the plaintiff could obtain similar remedies elsewhere.\footnote{353} At the same time, it is unlikely that U.S. nationals could receive civil damages for acts of international terrorism committed against them, their property or business.\footnote{354} Additional ammunition to a plaintiff's cause of action is available under 18 U.S.C. section 2333(a). That provision prevents a defendant from disclaiming culpability relating to essential elements of a criminal charge, once he has been found guilty in a criminal proceeding.\footnote{355} This benefits plaintiffs by using criminal actions to strengthen civil suits.\footnote{356}

The revised Senate bill tried to soothe some of the concerns regarding possible foreign reciprocal legislation as well as foreign sovereign immunity.\footnote{357} For instance, in order to quell fears that S. 2465 would be utilized by some parties with suits alleging "war crimes,"\footnote{358} proposed 18 U.S.C. section 2337 did not permit proposed suits "for injury by reason of an act of war."\footnote{359} Also to avoid potential difficult foreign policy concerns in suits against the U.S. government, its officials, foreign governments and its officers, proposed section 2337 provides a blanket provision denying suits against government officials.\footnote{360} It provides in pertinent part:

No action shall be maintained . . . against (1) the United States, or an officer or employee of the United States or any agency thereof acting within his official capacity or under color of legal authority; or (2) a foreign state, an agency of a foreign state, or an officer or employee of a foreign state or an agency thereof acting within his official capacity or under color of legal authority.\footnote{361}

Notwithstanding the fact that the Bush Administration agreed with the basic thrust of the Grassley-Heflin bill in October 1990, it repeated concerns expressed by the Department of Justice and Department of State

\footnotesize{\begin{itemize}
\item \footnote{352} Id. § 2334(d).
\item \footnote{353} Id. § 2334(d)(3).
\item \footnote{354} See supra notes 302-3 and accompanying text. Since the Department of State fears that the U.S. (or its officials) will be sued under reciprocal legislation, and such an existing foreign law was not cited, it is presumed that they do not exist.
\item \footnote{355} Anti-Terrorism Act, supra note 340, at 18 U.S.C. § 2333(a).
\item \footnote{356} Id.
\item \footnote{357} See supra notes 302-3, 321-2, 354 and accompanying text.
\item \footnote{358} Id.; Anti-Terrorism Act, supra note 340, at 18 U.S.C. § 2337.
\item \footnote{359} Anti-Terrorism Act, supra note 340, at 18 U.S.C. § 2337.
\item \footnote{360} Id.
\end{itemize}}
officials. After S. 2465 was incorporated into the Military Construction Appropriations Act, the Department of Justice reiterated its opposition to the proposed anti-terrorism legislation.

These sentiments were expressed by Assistant Attorney General Rawls, reaffirming Deputy Assistant Attorney Valentine’s testimony in calling for a provision in the bill permitting the Attorney General certificate to preempt discovery of prosecution files on terrorist incidents when disclosure would compromise an investigation. Furthermore, the Assistant Attorney General Rawls suggested adding a provision permitting the Attorney General, upon good cause, to request a judge to delay a civil suit until the summation of the criminal case. Indeed, such a stay would be requested only when the criminal case is based on the same terrorist incident as the civil suit.

The House of Representatives version of S. 2465 was introduced by Rep. Feighan and Rep. Hyde. Due to sharp objection by Rep. Brooks, Chairman of the House judiciary Committee, “the Anti-Terrorism Act of 1990” was abandoned in committee. Despite this defeat and some shortcomings, another legislative measure, encompassing similar components of S. 2465, will likely be introduced in the next Congress.

IX. RECENT INTERNATIONAL RESPONSE TO MARITIME TERRORISM

Following the grave attack of the Achille Lauro, governmental discussions commenced to establish another response to international terrorism, an agreement on maritime terrorism. Rather than mimicking the definitional focus of piracy in the 1958 Geneva Convention and the 1982 Law of the Sea Convention, the I.M.O. Convention outlined the arena in which states should have jurisdiction. The I.M.O. Convention also out-

361. See Rawls, supra at 339; Farman, supra at 339.
363. Id.
364. Id. at 2.
365. Id.
367. Id.
368. For strengths and weaknesses of legislation see supra notes 251-360 and accompanying text.
371. I.M.O. Convention, supra at 75.
lined the activities that individual states had to sanction, and provided the rule that required states, upon finding a maritime offender, to either prosecute or extradite.

The preamble to the I.M.O. Convention stipulates that the document is drafted in order “to develop international cooperation between States in devising and adopting effective and practical measures for the prevention of all unlawful acts against the safety of maritime navigation, and the prosecution and punishment of their perpetrators.” Article 3 of the I.M.O. Convention sets out the offenses by first describing the substantive offense and then establishing a secondary list which includes threatening, attempting, and being an accomplice or an abettor to the defined offenses. Article 3 of the I.M.O. Convention states:

1. Any person commits an offence if that person unlawfully and intentionally:

(a) seizes or exercises control over a ship by force or threat thereof of any other form of intimidation; or

(b) performs an act of violence against a person on board a ship if that act is likely to endanger the safe navigation of that ship; or

(c) destroy a ship or causes damage to a ship or to its cargo which is likely to endanger the safe navigation of that ship; or

(d) places or causes to be placed on a ship, by any means whatsoever, a device or substance which is likely to destroy that ship, or cause damage to that ship or its cargo which endangers or is likely to endanger the safe navigation of that ship; or

(e) destroys or seriously damages maritime navigational facilities or seriously interferes with their operation, if any such act is likely to endanger the safe navigation of a ship; or

(f) communicates information which he knows to be false, thereby endangering the safe navigation of a ship; or

(g) injures or kills any person, in connection with the commission or the attempted commission of any of the offenses set forth in subparagraphs (a) to (f).

Article 3, paragraph 1, subparagraph g, would apply to the Achille Lauro case, in light of the brutal murder of Mr. Klinghoffer. Such an international legal framework to fight maritime terrorism in indeed important.

With reference to the location of the ship during a terrorist attack, article 4 provides that the I.M.O. Convention is triggered “(1) if the ship is navigating or is scheduled to navigate into, through or from waters beyond the outer limit of the territorial sea of a single State, or the lateral

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372. 'd.; Treves, supra note 370, at 70-1.
373. Treves, supra note 370, at 79.
374. I.M.O. Convention, supra note 75, at preamble.
375. 'd. art. 3.
376. 'd.
limits of its territorial sea with adjacent States . . . [or] (2) when the offender or the alleged offender is found in the territory of a State party other than the State referred to in [the earlier portion of the sentence].

Thus, the international nature of a voyage, as well as its direction pursuant to article 4 of the I.M.O. Convention, is established by the overall itinerary of its voyage. Additionally, paragraph 2 provides that an alleged criminal is located on a vessel which is “navigating for is scheduled to navigate) at the time the offence was committed.

Another pertinent article of the I.M.O. Convention is article 6, which outlines when a state has jurisdiction over the offender. This Article provides:

1. Each State Party shall take such measures as may be necessary to establish its jurisdiction over the offences set forth in article 3 when the offence was committed:
   (a) against or on board a ship flying the flag of the State at the time the offence is committed; or
   (b) in the territory of that State, including its territorial sea; or
   (c) by a national of that State.
2. A State Party may also establish its jurisdiction over any such offence when:
   (a) it is committed by a stateless person whose habitual residence is in that State; or
   (b) during its commission a national of that State is seized, threatened, injured or killed; or
   (c) it is committed in an attempt to compel that State to do or abstain from doing any act.

Article 6 of the I.M.O. Convention provides use of several of the five bases of jurisdiction available in international law, namely; nationality, “determining jurisdiction by reference to the nationality of the offence”); territoriality (“determining jurisdiction by reference to the place where the offence is committed”); protective principle (“determining jurisdiction by reference to the national interest injured by the offence”); passive personality (“determining jurisdiction by reference to the nationality or national character of the person injured by the offence”); and universality principle (“determining jurisdiction by reference to the custody of the person committing the offence”). In article 6, paragraphs 1(a) through (b) and 2(a), it appears that the territoriality principle is cited. In contrast, it seems that the nationality concept is enunciated in article 6, paragraph 1(c). Also, in article 6, paragraph 2(b) the passive personality precept is util-

377. Id. art. 4; Treves, supra note 370, at 73-4.
378. Id.
379. Id.
380. I.M.O. Convention, supra note 75, art. 6.
381. Halberstam, supra note 75, at 296 n.12.
lized. Lastly, in article 6, paragraph 2(c), the protective principle is implemented.\textsuperscript{382} It must be remembered that the crime of piracy, although not mentioned by the I.M.O. Convention, is viewed by most nations as affording universal jurisdiction.\textsuperscript{383}

Turning again to the \textit{Klinghoffer} case, under article 6, paragraph 2(b), the U.S., would have jurisdiction over the Achille Lauro.\textsuperscript{384} Thus, the I.M.O. Convention greatly strengthens government responses to maritime terrorism by providing a means for criminal prosecution of the perpetrators of such acts.\textsuperscript{385}

Also, article 8 of the I.M.O. Convention deals with the obligation or authorization of a nation to establish jurisdiction over an incident.\textsuperscript{386} Article 8 provides that "[t]he master of the ship of a State Party (the "flag State" may deliver to the authorities of any other State Party (the "receiving State") any person who he has reasonable grounds to believe has committed one of the offenses set forth in article 3."\textsuperscript{387} Despite hortatory language, this provision codifies the requirement that alleged offenders be handed over to proper authorities for prosecution. Furthermore, article 8 describes that refusal to accept delivery of the offender must be explained in full by either the flag nation or receiving nation.\textsuperscript{388}

As in article 7 of the Hague Convention on Suppression of Unlawful Seizure of Aircraft and the Montreal Convention Against the Taking of Hostages, article 10 provides that a State in which an offender is found must either extradite him or immediately initiate prosecution.\textsuperscript{389} As a result, the obligations of a state signatory to the I.M.O. Convention would be to either commence criminal proceedings against a terrorist offender or extradite to a nation which would prosecute. If the I.M.O. Convention would have been in force at the time of the Achille Lauro incident, and had Egypt been a signatory, then Egypt's obligations under international law would have been strictly set out.\textsuperscript{390} Keeping in line with the provisions of article 10, article 11 states that extradition can occur either with or without an extradition treaty.\textsuperscript{391}

In sum, the I.M.O. Convention is a vital and necessary step that the world community has taken to demonstrate its resolve against terrorism.

\begin{thebibliography}{99}
\bibitem{382} Id.
\bibitem{383} See generally McCredie, supra note 98, at 443-5.
\bibitem{384} I.M.O. Convention, supra note 75, art. 6.
\bibitem{385} See generally I.M.O. Convention, supra at 75.
\bibitem{386} Id. art 8; Treves, supra note 370, at 81.
\bibitem{387} I.M.O. Convention, supra note 75, art. 6.
\bibitem{388} Id.
\bibitem{389} Treves, supra note 370, at 81-2.
\bibitem{390} I.M.O. Convention, supra note 75, art. 11.
\bibitem{391} Id.
\end{thebibliography}
X. CONCLUSION

The foregoing discussion and analysis leads to several conclusions. First, the increasing role of civil litigation to respond to terrorism is both real and vital. As the *Klinghoffer* litigation illustrates, terrorist groups' accountability can be set forth effectively through the civil courts. Second, U.S. legislative proposals, such as S. 2465, will certainly strengthen the legal tools available to the victims of terrorism. Third, multilateral legal instruments such as the I.M.O. Convention, are additional guidelines which can be used to combat terrorism. In sum, national and multilateral legislation, rooted at decreasing the specter of terrorism, must continue to flourish in the 1990's. Otherwise, the perpetrators of extra-legal violence will continue to carry out their destructive activities, and thereby threaten the fabric of modern society.
Book Review


by DAVID W. BARNES and EDWARD A. DAUER*

There is an institution, now well known among American law professors, that invites small groups of academic lawyers to spend a few weeks in the summer learning about the theories and applications of microeconomics. The participating law professors are treated during their summer stay to two most notable offerings. The first is the True Faith of neoclassical economics. The second is a meal service of gourmet achievements rivaled by none in the otherwise genteel poverty of academic life.

And so it was that on one day not long ago, when Paul Stephen Dempsey was participating in this Pareto in the Pines, that a particularly sumptuous meal was served to the group then assembled. But on that very same day an editorial written by Dempsey had appeared in a major daily newspaper, an essay openly doubting the classical faith that Heaven is an unregulated marketplace. With great ceremony the uniformed waiters placed before Dempsey a silver dome, and with a flourish lifted it to show his meal—a plain, boiled hot dog. Such are the wages of apostasy.

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There is little doubt that Paul Dempsey has become the leading and perhaps most trenchant critic of deregulation, particularly so as to the transportation industry and even more particularly with respect to aviation. But it is not clear to us on a reading of these books, his two most recent contributions to the deregulation debate, how the Defenders of the Faith could justifiably find his work troublesome. Dempsey’s approach is no assault upon the neoclassical framework. It lies, for the most part, squarely within the theory. It attacks only the factual premises on which the neoclassical theory’s policy prescriptions are based. Dempsey does not dispute the axiom that “Nonregulation achieves economic efficiency and consumer welfare when certain specified conditions prevail.” He tried instead only to prove that the requisite conditions simply do not prevail. And although his work does not constitute any new, broadly applicable approach to policy formulation, it does teach us something valuable about the linkage between empirically-dependent theories and the implementation of public policy.

We will be discussing these two books together, not always bothering to distinguish between the two. They are quite similar in their conclusions if not their styles;\(^1\) and our focus is much more on the arguments than on the details of either particular work. Our discussion is organized into four main parts. It begins with a brief restatement of Dempsey’s empirical argument, and a critique of some of its greater and lesser points. Second is a challenge to the argument from the perspective of antitrust law and economics. Third is a suggestion for an alternative to the conventional choices in regulatory policy. And last is a concluding note on the relationships among argument, scholarship, and public policy.

I. THE BEST LAID PLANS OF MICE AND MEN

To a first approximation, uninhibited competition among the sellers in a market is generally a good thing. Suppliers compete to satisfy consumers’ preferences for quality and service, they offer a range of goods at prices near or at their marginal costs of production, and our collective resource efficiency is optimized at the same time that the range of individual choice is maximized. Fantasyland is, however, subject to being spoiled by several stubborn realities.

One is that as a matter of public choice, marginal-cost pricing and allocative efficiency are not the only desiderata we might embrace. Some

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1. P. DEMPSEY *The Social and Economic Consequences of Deregulation*, (1989) [hereinafter the Book] differs from *Flying Blind: The Failure of Airline Deregulation* [hereinafter REPORT] in two main ways. For one, while the Report addressed the situation of deregulation in aviation, the Book carried the same case in the other recently deregulated modes of trucks and buses and trains. And for the other, while the Report was presumably written for a policy-maker audience, the Book seems to have been addressed to the much wider general public.
things are not produced through competition—things like our wanting differently—situated people to have equal access to important services, even though the differences in their situations makes the costs of delivering those things very unequal. Transportation services to small towns might be an example. A market, in other words, is one very useful method of collective choice. But it does not produce all of the collective goods we might want to have.

A second source of trouble for unrestrained competition, is that it assumes a certain competence in its notion of consumer sovereignty—that consumers have adequate information about comparative goods and comparative prices, for example, and that the externalized costs of every purchase are as obvious to the demand side as the more patent and immediate costs are. This may not be true from time to time, for such things as investments in the transportation infrastructure which lessen or magnify the safety risks of the service. This is one form of what economics calls "market failure."

And a third is that unrestrained competition may itself be unattainable. Where there are significant economies of scale in the production of some particular service or good, there can be great advantages to the existence of a few very large firms rather than a large number of smaller ones. The limiting case is the "natural monopoly," in which the increased costs from decreased scale are so great that having two competing firms in one market would result in returns to at least one of them being insufficient to retain its capital investment. Absent some form of outside intervention, after a while only one would remain and the advantages of competition would be lost.

A fourth reality is that unrestrained competition can be destructive of both resource efficiency and consumer sovereignty. Where the fixed costs of production are a relatively high proportion of total costs and production capacity cannot be increased or decreased rapidly, supply may be less than optimally responsive to demand. In periods of excess capacity, producers are ill-served by forms of competition that drive prices to a level insufficient to cover total costs. Conversely, in periods of insufficient capacity, consumer demand is unfulfilled. Where that condition is endemic to the industry and coordination of pricing and capacity strategies by otherwise independent firms would be prohibited by the antitrust laws, then the market may be exhibiting a form of "failure" that often calls forth regulation by government.2

At various points in Dempsey's work there are arguments for the existence of all four of these reasons for government regulation of the

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transportation industry: Market failure through consumer incompetence, inexorable economies of scale in transportation, a broad and deep public policy based on the recognition that transportation is the linchpin infrastructure of nearly all of modern economic life, and the circumstances for destructive competition. Without equal access to reliable transportation, whole segments of society—the aged, the remote, the infirm, the emerging—would be unfairly hampered in their chances for the fullest measure of participation. Government regulation therefore seemed to be a natural; and so it did become, for nearly every transportation mode, the system of the century. Airlines, for example, entered their maturity in a regulated environment, and until a scant ten years ago had never operated in any other way.

Then, for reasons which can only be surmised, in the years immediately following the Vietnam War the great experiment began: At various dates and with various paces, the several modes of transportation began to be deregulated. Believing perhaps that regulation was also immunization from the demands of the marketplace, the Congress was convinced by Alfred Kahn at the Civil Aeronautics Board (CAB) and by Edward Kennedy in the U.S. Senate that through deregulation and the pricing flexibility it offered to the supplying firms, there would be product innovation, increased economic efficiency, and service options dictated by actual consumer demand.

Economists had failed to find the likelihood of significant economies of scale, at least for the motor carriers and the airlines; natural monopolies and unnatural competition were unlikely to spoil the vision. And even if there were to be but a few or even a lone supplier in some part of the market, that seller would behave itself because if it did not, another "potential" entrant was always there at the edge of the playground, ready to come in and share in the monopoly rents until the market became competitive again. Thus both the traditional and the newer "contestability" arguments against regulation had the upper hand.

Dempsey, nunc pro tunc, was not convinced. Regulation of the transportation industry, he argues, is a necessary answer to the inevitable Hobson's choice between price-discriminating monopolists on the one hand, and "an unstable pack of anemic bankrupt carriers" engaged in "unrestrained competition" on the other. Whether that inevitability does prove to be the case or not, Dempsey's argument for why it must be the case is not fully convincing.

Transportation services, he says, are unique. What they produce is "an instantly perishable commodity." When the airplane leaves the gate, the empty seats (on that flight) are lost forever; ditto for half-loaded trucks.
and trains. Unlike a can of beans in a grocery, transportation capacity cannot be stored and sold another day. And as a result the transportation industry is perhaps uniquely vulnerable to excess capacity and ruinous price wars. By that argument we are not convinced: First off, we are not certain why the perishability point matters, even if it is true. And second, we wonder whether it is in fact true—at least in its claim to uniqueness.

Dempsey would say that the marginal cost of filling another seat on an airplane is trivial compared to the fixed costs of the flight, and so competing firms are driven to fill those seats at distress prices. Prices therefore spiral downward until the revenues cover only the marginal costs and make no contribution to the fixed costs. Then, systematically, the only way out is for the carriers to seek relief in the construction of monopolistic opportunities.

The reasoning is ambitious. For one thing, to be driven to monopoly practices as a relief from the pressures of competition is a move that every business would like to make, if it could. There is no explanation here of why transportation can do so more easily than anyone else can. Or at least not a reason which relates to the regulation debate.

And for another, such cost-cutting behavior need not result in a carrier’s gross revenues declining below the full costs of production, in the longer run. If the fixed costs were not covered by the first few seats of a flight, there would be no incentive to offer any seats at all so long as the marginal seats generated only marginally useful revenues. Thus as an act of pricing an entire flight—or of scaling an entire airline, if we believe that all costs are variable in the long run—the distress pricing of the seats at the end of the queue of demand can still generate gross margins somewhere between zero and a positive number, as a matter of long-run planning. In an equilibrium, therefore, there is no extraordinary consequence to there being even a large disparity between average and marginal costs, and we do not see why that situation alone should necessarily be destabilizing. It just means that airlines, like everybody else, usually cannot earn profits beyond the competitive rate of return to invested capital. While the argument might succeed if there was a reason to doubt the possibility of equilibrium after a period of rollicking oscillations, neither the Book nor the Report addresses the problem in that way.

Even more troublesome, perhaps, is the fact that in experiencing this empty-seat phenomenon the transportation industry is hardly unique. This problem is just a specific example of the more general circumstance of less-than-full-capacity-operations, of which the familiar peak-load dilemma is also a variant. It is true that a seat unfilled is in some sense lost forever. But that is equally true of a lathe which operates at only 85% of

3. Book, supra note 1, at 42; Report, supra note 1, at 12.
its rated output because its owner cannot sell the products of the last 15% every day. The unused productive capacity of that lathe is also lost forever. Likewise for a grocer's freezer case only half full. The energy cost of keeping 300 steaks cold is no greater than that of 150, and the wear and tear on the freezer hardly varies at all. Computers in an accounting firm; automobiles in a real estate agency; empty seats in a law school class on Regulated Industries; any number of excess capacity opportunities exist in any number of different settings. Yet in none of them do we see the phenomena which Dempsey ascribes to them—and calls inevitable—in transportation.

Perhaps the Hobson's choice is real; we cannot be sure, because not all of the data are in. But we would not be inclined to regard that dilemma as an inevitable fact of life. If it were to be so, it would probably not be so just for the reasons Dempsey suggests.

The empirical arguments are better. Concentration in the industry has declined. Since deregulation of the airlines in 1978 and 1979, some 200 carriers have either exited or been acquired;\(^4\) only 74 remain. Single-carrier concentration at major airports is up from 33.8% in 1977 to over 73% ten years after.\(^5\) All but four hub airports are now dominated by a single airline. And for the typical city-pair—the only relevant characteristic from the point of view of an individual traveller—the situation can be fairly characterized as "a move from a regulated monopoly to an unregulated duopoly."

The theory of protection derived from contestability, or potential entry, is shown to be flawed on a number of counts: (1) Airlines operate through reservation systems, and the concentration (from scale economies?) in that part of the business makes new entry difficult if not impossible. (2) New entrants have to land somewhere, yet the number of gates (and at some airports, landing slots) is limited in all but the longest of runs. (3) There are fewer labor cost advantages to new entrants now that the pre-existing airlines have been able to avoid the most costly aspects of the older union contracts. (4) Frequent flyer programs exploit the absence of coincidence of interest between the business traveller and the person who actually pays the fare. (5) Monopolist advantages allow the existing carrier to cut its fares to stifle the potential entrant, thereby making investments in new entrants less attractive.

We have no quarrel with the empirical validity of each of those facts. We would, however, append the caveat here that, like so much of the remaining analysis, we believe (and will shortly suggest) that none of those factors is inevitable in itself, and that each is addressable in a way.

\(^4\) BOOK, supra note 1, at 86-87; REPORT, supra note 1, at 12-13.

\(^5\) REPORT, supra note 1, at 17.
more finely-tuned than comprehensive regulation would be. But for the moment we will accept Dempsey's conclusion, that there has been no live birthing of a new generation of competitors among airlines in the decade after deregulation.6

The crux of the argument, however, is not about the absolute values of the concentration indices themselves. What really counts is whether the absence of a flourishing competition has sacrificed any of the consumer interests which either competition was expected to create or which regulation was intended to preserve. Dempsey addresses these questions in three areas: pricing, service, and safety.

A. Pricing

Its analysis of pricing and price discrimination is where the Report shines best. There is an impressive array of data which seem hardly controvertible. Pricing in the airline industry today reflects the competitive circumstances from route to route, almost wholly unconnected with relative costs. Hence travellers in smaller towns and over less well-travelled routes pay prices well above the costs of producing the service, while passengers travelling dense and popular big-city pairs pay prices wildly and disproportionately less. Deregulation was touted as a way of increasing efficiency, even at the cost of removing the subsidy that big-city routes were providing to the smaller and more costly ones. What has happened, however, is simply that the subsidy has been reversed. And price discrimination (through stay-there-on-Tuesday-and-come-back-the-preceding-day special discount fares) has become a contact sport.7

The news is bad in the aggregate too. Through an ingenious correction to fare prices, designed to account for changes in the fuel prices borne by the airlines, Dempsey shows clearly that the much ballyhooed reductions in fares which occurred immediately after deregulation became effective, amount to nothing a decade later. For the decade preceding deregulation, fuel-price-corrected real revenues per passenger mile declined at a 2.7% annual rate. During the decade after deregulation, the decrease has been at less than 2.0%. Consumers are therefore paying now some 2.6% more than they would have paid under a continuation of the pre-deregulation trend line.

We can forgive (but not fail to mention) the obvious criticism, that because the Report contains no analysis of why the reduction from 1967 to 1977 occurred, there is little reason to conclude that it would have continued at the same rate had deregulation not intervened. On the other hand, we should not fail to mention a strength of the argument, which is

6. REPORT, supra note 1, at 21-24; BOOK, supra note 1, at 89-91.
7. BOOK, supra note 1, at 95-96, 99; REPORT, supra note 1, at 27.
that because the hub-and-spoke system has actually added miles to the
typical trip between point A and point B, even a flat-rate-per-mile price
curve would result in some prices being higher after deregulation than
before. We will worry some other time about the really interesting ques-
tion: if prices are relatively high, why are profit margins so dangerously
low?

B. SAFETY

Lower profit margins caused by destructive competition have jeop-
ardized margins of safety. This is an emotionally powerful argument; few
scenes capture the headlines more grippingly than a smoking airplane
carcass littered with body bags. The trouble with it is, that with respect to
aviation, there may be no facts to confirm the theory.

Other than establishing that the average age of the commercial air-
line fleet has grown in recent years (though without offering a comparison
with the regulated years), there is almost no data here. There has been a
10% decline in the number of mechanics per airplane among the major
carriers over the last ten years. But have there been offsetting increases
in technological capability, or even productivity? Better machinery can
easily make magnafluxing for cracks a far less labor intensive job, and
ten years is a long time. Would these reductions have occurred, deregula-
tion or not?

More to the point, one might well ask what the optimum number of
mechanics per airplane actually is. Is it possible that under regulatory
protection the machinists' unions were able to contract for more positions
than optimal safety really required? That discussion is not in either the
Report or the Book. It is enticing to know about changes in the number of
mechanics. But it would be compelling to know the marginal returns to
increased safety as the number grows and lessens.

Although the in-flight safety record has not produced a corpus delicti
sufficient to indict deregulation, Dempsey reports that "the number of
near-misses has soared." Presumably, though he doesn't say so, he
means the number after deregulation compared to the number before.

As the old pilots' saying goes, one mid-air collision could ruin your
whole day. But attributing it to deregulation is quite another matter. For
one thing, if that scary datum is true and if it involves IFR-only8 scheduled
carriers, then a good part of the blame may lie not with airline deregula-
tion, but with the understaffed and undersupported air traffic system,
which suffered a major blow in the Air Traffic Controllers discharge in
early 1980, immediately after deregulation took hold. Post hoc does not

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8. "IFR" means "Instrument Flight Rules"—a system in which aircraft fly under the control
of ATC (Air Traffic Control), regardless of in-flight visibilities.
always mean propter hoc. Another possibility: the National Transportation Safety Board, to stay with the near-miss business for a moment, introduced in recent years a safety violation self-reporting program through which a pilot can attain immunity from prosecution by submitting a voluntary report of his own airspace transgressions. Has that increased the reported number of near-misses? Likewise, with respect to a handy little device now installed in Air Traffic Control radar computers and called the "snitch." This annoying virus will blow the whistle on an air traffic controller who does not do something himself right now about a violation of the minimum separation standards. 9 Could that also have affected the reported rate?

And FAA is the world's largest user of vacuum tubes, we're told. Maybe so. But how is that a consequence of deregulation? The average flight experience of starting pilots is less today than it was a few years ago. Also true. But most pilots for the majors traditionally got their training in the military. We have not had a war lately. The last one ended during a regulated era. Would the average age have been higher if the airlines had not been deregulated? Seems unlikely.

The actual airline accident data themselves do not support Dempsey's fears of compromised safety. He says that we have not had more lives lost only because pilots have been so terrified by the consequences of deregulation that they pay more attention to what is going on around them. And that even though there has been a reduction in safety margins, the whole business is so "over-engineered" that we have not yet pierced the outer moat. How do we know what the optimal behavior of pilots and airlines actually is? We do not know that only by knowing that certain counts declined when regulation was removed. The argument here is not necessarily wrong; it is just seriously incomplete.

C. SERVICE

This is a mixed bag. Focussing again on the case of the airlines, Dempsey sees adverse consequences attributable to deregulation for both big cities and little towns. The empirical case for service degradation on the city routes is the most virulent and least rigorous of all of the facts reported: "The planes are filthy, delayed, cancelled, and overbooked, our luggage disappears, and the food is processed cardboard." Moreover, to support their price discrimination efforts the airlines engage in consumer fraud, bait-and-switch advertising, unrealistic scheduling and revenue-based cancellations, which sounds like what every

other business might try to do absent a focussed supervision by, for example, the FTC.

For smaller towns the argument is a little better. It has two parts—service; and again, safety. On the service score the data do support the conclusion that noneconomic routes have suffered since deregulation. The air carrier measure is that of seats departing, which is down some 17% since 1979. Our comment here, which we shall come back to again a bit later, is that while deregulation may have created that loss, reregulation may not be the best way to recoup it. Under regulated prices, the CAB required below-cost pricing subsidized by excessive pricing on other routes flown by the same carrier. Hence some flyers supported others. But there is another way: With an aggressive EAS (Essential Air Service) policy, government can provide focussed subsidies to carriers who would be attracted to service the targeted small town routes, at a cost not to other flyers but to all citizens in general. That, we suspect, may be a more rationally and finely-honed way to address this particular half of the problem.

The safety argument also goes beyond what the facts support. Since deregulation, Dempsey reports, the safety of flyers in small towns has been compromised by the fact that only the far less safe commuter lines will serve them.

Dempsey alleges that small town flyers have since deregulation been subjected to airline service which uses “less sophisticated planes, smaller, unpressurized, devoid of... radar [and] sophisticated flight instruments... and fly at altitudes most vulnerable to weather hazards and mid-air collisions.”

Little of what is true in that argument can be traced to deregulation; and much of it probably does not matter. Weather radar is just as easily installed in a 10-place King Air as it is in a Boeing 767, and its cost is so small compared to that of the airframe itself—and its utility in keeping the flights departing on time is so great—that we would be amazed to find it installed any less frequently. Likewise with “sophisticated flight instruments.” An ILS glide slope receiver is an ILS glide slope receiver. The FAA requires all such instruments to work within certain operating tolerances, and with the exception of the CAT III carriers, there is no difference in avionics that really matters much between a 727 and a Merlin. Most of the gizmos on the 727 have to do with that particular airplane’s characteristics, not with the requisites for safe navigation. Perhaps the

11. Quoting solely from Congressional testimony.
12. A Category I ILS allows landing with, generally, a 250 foot ceiling. Category II and Category III allow for even smaller margins. To fly a CAT II or CAT III ILS, the pilot must be specially qualified and the aircraft must be specially equipped.
removal of cross-subsidies has affected the equipment flown (which is itself a fact not established with comparative data), but there is no reason to leap from that to degradation of safety performance.

As to collision avoidance, the fact is that most of the lives lost in mid-air collisions have occurred where at least one of the airplanes was a major-carrier jet. This has little to do with altitudes. Commuter aircraft fly well above the airspace beneath 10,000 feet where the general aviation Sunday drivers are; and every airplane eventually has to descend to a low altitude to land, jet or not. Moreover, on-board TCAS (Collision Avoidance Systems) have only been available for two years. Their cost will in only a few more years be low enough that they will be available as standard equipment on every airplane, even the GA bug-smashers.

If there are differences between the equipment flown by the commuters and that flown by the majors, it is not likely the result or a consideration of deregulation. No 727 has ever or will ever land at Block Island, R.I. No 767 ever at Aspen, Colorado. Regulation and profit margins have little to do with runway lengths. And as to the minimum safe equipment, there are scores of pages of dense text in the Federal Aviation Regulations dictating what each airplane must have and how well it has to work. If safety considerations resting in equipment are the problem, economic regulation is not the answer. Regulation of the equipment might be. That already exists, and despite deregulation it continues.

II. REGULATION OR OVERSIGHT?

Despite these several quibbles, Dempsey is undoubtedly the master of the facts. We are not. But the burden of his work is a plea for renewed regulation of the transportation industry. If we were to accept every fact contained in the Book and the Report as true, the kind of governmental response which is appropriate might still be an open question.

A. The Regulatory Alternative

Dempsey's preferred response to excessive concentration, predatory and discriminatory pricing, and safety and service deterioration is regulation. He characterizes his preference as "regulation at the margins,"13 tailored to suit the particular characteristics of the industry and the social needs that it serves.

Dempsey's main course would still be, however, entry and rate regulation. Entry regulation would keep some firms out, to prevent excess capacity from interfering with productive efficiency14 and allowing other firms to operate as the only suppliers in some certain markets. Entry reg-

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ulation would encourage entry into other markets—by restricting the number of hubs a particular airline might employ, for instance, or forbidding domination of a geographic area by a particular carrier—in order to end the problems associated with concentration, and to stimulate pricing and service innovations.15 Entry regulation could also achieve other goals: The threat of license revocation, for example, would deter carriers from discriminatory pricing and from failing to fulfill their safety obligations.16

Rate regulation would keep rates in a “just and reasonable” zone, allowing flexibility for the firms to price anywhere between predation (which is presumably below cost, though Dempsey does not specify exactly what that level is) and monopoly. This would shield smaller competitors from the effects of low prices and “prohibit [...] consumers from being exploited” by high prices.17 “This,” he reports, “keeps the market flush with competitors and ensures that healthy competition is the driving force behind pricing, a result which benefits consumers.”18 This minimalist tenor of entry and rate regulation is that of allowing competition to flourish wherever it can, in markets where competition does not create excess capacity and within a broad pricing range. The Report parces this down even further, imposing rate regulation only where an airline has sufficient market share to exert market power.

Consumer protection regulation and increased safety regulation are served up as the antipasto while required service to small communities is the dolce. According to the Book, consumer protection is enhanced by regulatory prohibitions and rules forbidding overbooking and penalizing cancellations, missed connections, and bad service (down to regulation of seat width and distances between seats on long flights).19 Professor Dempsey adds to the list of remedies a conclusion that “the government must intervene to protect consumers against false and misleading advertising,” referring specifically to “bait and switch” practices.20

In the Book, Dempsey concludes his safety chapter by relying on regulating rates to ensure that well-managed carriers earn sufficient profits to keep their equipment in safe condition, and on license revocation (“the Damocles sword” of entry regulation) to ensure that unsafe carriers have their operating permits revoked.21 The Report takes a broader picture, recommending—in addition to entry and rate regulation—refurbish-

15. REPORT, supra note 1, at 51.
16. BOOK, supra note 1, at 223.
17. BOOK, supra note 1, at 224.
18. Id. at 224.
19. Id. at 239.
20. REPORT, supra note 1, at 56.
21. BOOK, supra note 1, at 125.
ing the air traffic control system, updating FAA equipment, building new airports and expanding existing ones, and regulating landings and take-offs to reduce congestion. 22

For the dessert, Dempsey offers better access to the transportation network of the United States to small town entrepreneurs and to the rural poor and elderly than would be available if they had to pay its full costs. In this area, both the Book and the Report recognize regulatory and non-regulatory alternatives. Rate and entry regulation are the solution to the purported lack of sufficient service to small towns only if political pressures make direct subsidies from the federal budget infeasible. 23 It is not clear which one Dempsey prefers, 24 though his recognition of a non-regulatory alternative reflects what may be a trend, as illustrated by these examples, towards increasing open-mindedness to alternatives to regulation. (The Report was prepared two years after the Book.)

If we take this trend to its logical conclusion, and consider non-regulatory solutions to all of these problems, then perhaps we would truly have "regulation at the margins," reserving regulation for those areas where the kind of governmental "supervision" or "oversight" embodied in the antitrust laws and consumer protection law are inapplicable.

**B. THE ROLE OF NON-REGULATORY ALTERNATIVES IN THE TRANSPORTATION INDUSTRIES**

From the most fundamental perspective, there are two circumstances in which relying on rigorously enforced antitrust and consumer protection laws is inappropriate: natural monopoly and destructive competition. With apologies to Alfred Kahn, who has laid out the structural foundations for these two theories of regulation in elaborate detail, 25 the essential requirement for a natural monopoly is that there be insufficient demand in the relevant geographic market to support the profitable supply of a service by two firms at an efficient level of cost. A natural monopoly is not to be identified with every monopoly that results from the acts of a competitor who excludes or precludes competition. Natural monopoly is a structural relationship between demand and the cost of supplying the service, while an "ordinary" monopoly may result from the behavior of a competitor. Antitrust law can deal with the latter but not the former; a

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22. REPORT, supra note 1, at 56-57.
23. BOOK, supra note 1, at 240; REPORT, supra note 1 at 54.
24. "If we are to abandon any notion of entry regulation and cross-subsidization at the federal level (and perhaps we should not) . . . " REPORT, supra note 1, at 54.
25. A. KAHN, THE ECONOMICS OF REGULATION: PRINCIPLES AND INSTITUTIONS (1971). Kahn has addressed many of the issues discussed in this part of the review in great detail. In particular, he discussed the applicability of the destructive competition justification for regulation to the transportation industries.
naturally monopolistic market cannot, by its structural nature, be made competitive. Some form of regulation is necessary, if the sole participant is to behave "as if" in a competitive regime.

As we noted earlier, the structural characteristic of an industry beset with destructive competition is that productive capacity does not adjust efficiently to changes in demand. Dempsey focuses on the problems of overcapacity. The inability to readily contract capacity when demand declines may lead managers to cut their profit margins very thin, or even to sell output or services at a loss if that strategy helps them avoid the even larger losses that would accompany shutting down production entirely. Faced with high fixed costs which, by definition, they must pay whether they produce or not, all of the firms in an industry may compete particularly fiercely, giving sharp price reductions where competition is present (appearing to discriminatorily price to the disadvantage of customers in areas where competition is not as challenging), pricing below cost to minimize losses (appearing to predatorily price to the disadvantage of their smaller competitors). If this overcapacity persists, the firms will earn insufficient profits to invest in maintenance of their infrastructure, safety equipment, or innovation.26

Like natural monopoly, the problems in a destructive competition industry are structural; and the vision of excess capacity—plant and equipment sitting idle or under utilized because there is no way to dispose of it—does not seem to fit airlines or motor carriage. Such an industry is not to be identified with every industry in which one observes discriminatory pricing, pricing below cost, or insufficient investment in maintenance, safety, or innovation. These characteristics may result from structural conditions but they may also result from the anticompetitive behavior of the firms. Antitrust law can deal with the behavior, but is ill-equipped to deal with the underlying, fundamentally technological, structural conditions. The caution we are offering here is twofold. First, behavior that looks like destructive competition might be that, or it might be a short-term swing of the industry toward a new condition of happy stability. Accusing bloodletting by competitors of being destructive competition requires more than just pointing out the blood. Second, while it is true that an

26. It would appear that if demand conditions do not change, this overcapacity problem would eventually correct itself as old capacity outlived its useful life. But increases in demand, whether due to cyclical influences or underlying changes in the economy, may give signals to independent entrepreneurs that entry into the industry or increases in capacity will be profitable. If the decision to enter is a wise one in the long run, then the cost to consumers is the high prices charged by existing firms during the long period before the increase in output is achieved. If the decision to enter turns out to be unwise, because the increase in demand was temporary, then a new round of price cutting induced by excess capacity occurs. Price regulation in such an industry prevents the losses during periods of excess capacity and the high prices during period of insufficient capacity.
airline seat is wasted in some sense when the airplane leaves the gate with that seat empty, the same is true of every empty hotel bed when twilight falls. Yet we do not observe destructive competition in that rather similar industry. Once again, the argument ultimately for regulation therefore requires more than observing that marginal costs are low relative to fixed costs.

The bottom line in a "regulation at the margins" approach must therefore be a consideration of whether the industry is one in which government antitrust oversight will never be successful in making the market competitive, because of its structural conditions. If the natural monopoly or destructive competition arguments apply, one must then decide whether the regulatory solution creates more distortions than would occur by either leaving it alone or by adopting the ill-equipped antitrust solution. If a correction of the ills by either regulation of antitrust is appropriate, the choice of remedies must take into account whether the political will and expertise of regulators or antitrust enforcers is more likely to lead to the desired correction.

Evidence that firms are exhibiting the kind of behavior associated with natural monopoly, or that industries are showing effects that may be the result of structural destructive competition, are the best clues for where to look for situations where regulation is necessary. Dempsey excels in gathering this evidence. His journalistic flair presents a most enticing case that there is something wrong with the performance of these industries; and his view is amply supported in a number of instances, at least in the Report, by the testimony of fairminded deregulators who have recognized problems with the way in which deregulation occurred. The next necessary step, however, is to show that these industries, or selected markets within them, are structurally impervious to oversight. Only then should we conclude that regulation is more appropriate.

C. THE EVIDENCE FOR THE INAPPROPRIATENESS OF OVERSIGHT

1. EXCESSIVE CONCENTRATION: Figure 8.1 in the chapter on concentration lists the numerous mergers that have occurred since the Airline Deregulation Act of 1978. Figure 8.2 does the same for the railroads, while the rest of the chapter covers motor carrier and water carrier acquisitions. Professor Dempsey's discussion of the antitrust analysis by the Civil Aeronautics Board leads us to conclude that his recommendations would benefit from a serious reconsideration of antitrust as an alternative to regulation.

Dempsey reports that the administrative law judge evaluating the

27. E.g., REPORT, supra note 1, at 9-11, 24.
28. BOOK, supra note 1, at 134-139.
Texas International-National Airlines merger had decided that the combined statistical market shares created by the merger would exceed the percentage limits allowed by the Supreme Court's per se illegality test in *United States v. Philadelphia National Bank*, 374 U.S. 321 (1963), in at least one market, and was therefore illegal under Section 7 of the Clayton Act, the antitrust provision governing mergers. The regulators at the CAB, however, chose to follow what Professor Dempsey describes as the more "functional" approach of *Brown Shoe v. United States*, 370 U.S. 294 (1962), and *United States v. General Dynamics*, 415 U.S. 486 (1974), which takes such considerations as the product and geographic market definitions, cross-elasticities of demand, and entry barriers into account in deciding whether the large market share is likely to lead to the improper exploitation of that market position by the newly merged firms.29

It is a relatively minor point that, in fact, every merger case including *Philadelphia National Bank* has required an analysis of product and geographic market definitions (of which cross-elasticities of demand is often a part) and neither *Brown Shoe* nor *General Dynamics* depended in any significant way on either the presence or absence of entry barriers. Moreover, *Brown Shoe* and *General Dynamics* are generally considered to be polar opposites in antitrust jurisprudence; and regulators of the breed that Professor Dempsey would rely on in the future would have to have been extraordinarily ignorant of antitrust law and policy to have relied on them both.

*Brown Shoe*, in fact, took an even stronger anti-merger posture than *Philadelphia National Bank*. Compared to the 30% market share per se illegality threshold established in the bank merger, the merger of the shoe companies resulted in only a 5% share of shoe manufacturing in the United States yet was still held illegal. While it was true that in some local retail shoe markets the resulting concentration was much higher, the court's finding of illegality did not depend on that. Rather than being "functional," the approach of *Brown Shoe* is typically characterized as that of "incipiency," which reflects a concern that increasing concentration be prevented as soon as a trend appears in the industry, even before it could possibly have had ill effects. If the CAB had really understood and applied such a standard, they might very well have disapproved every airline merger that occurred.

In addition, while *General Dynamics* did establish an approach that went beyond mere market shares and did allow the merger of large companies, it had a peculiar set of facts, bearing no relationship to entry barriers. The shares of coal contracts owned by the merging parties in that case may have exceeded the per se threshold in the relevant market, but

29. BOOK, supra note 1, at 135.
all of that coal had already been committed to purchasers and could not possibly affect future competition. If Dempsey has accurately described their analysis, he can hardly find reassuring the ignorance exhibited by the regulators. Dempsey would, after all, fain rely on regulators than on the specialists in antitrust enforcement at the Justice Department or the Federal Trade Commission.

More significantly, most of the rest of Professor Dempsey’s discussion excoriates the regulators in the CAB and the Department of Transportation for approving merger after merger while giving at least modest credit to those in charge of “oversight”—the antitrust specialists at the Justice Department—for recognizing the anticompetitive effects of several of the mergers. It is hard to imagine how one can conclude from this recitation that regulatory control by an agency specializing in an industry could be recommended over an “oversight” control by a department specializing in antitrust.

Professor Dempsey does recommend that statutory criteria for mergers be tightened. He also argues that the Justice Department, using the same criteria, would have challenged some of the mergers to which he objects. Additionally, ease of entry—the grounds on which many of the airline mergers were approved—is a theoretically sound reason for approving a merger and would undoubtedly be a part of any acceptable statutory criteria for assessing the legality of mergers. The increasing concentration in the airline industry was due in substantial part, as Professor Dempsey points out, to incorrect factual predictions by the experts regarding contestability, and apparently not to inadequate statutory criteria. This applies as well to shippers with monopsony power, enabling them to force truckers to carry their goods for unprofitable rates, as it does to airlines that dominate hubs.

We are therefore left to wonder whether antitrust is inherently inappropriate in preventing undesirable concentration. Dempsey’s argument regarding the inability of antitrust law to contain undesirable increases in concentration relies on a regulatory failure, and a detailed and persuasive argument it is. He does not argue, in this context, that antitrust is fundamentally unsuited to the structural characteristics of the transportation industries. In fact, his rate regulation solution looks a lot like expedited antitrust review. Only where there is proof of excessive concentration in a particular airline market, for instance, would a consumer complaint trigger a review of rates to see if the airline was exploiting its monopoly position. Precisely because so many of Dempsey’s arguments are redolent

30. Book, supra note 1, at 240; Report, supra note 1, at 53.
32. Report, supra note 1, at 8-10.
33. Report, supra note 1, at 52.
of antitrust solutions, we are convinced that antitrust approaches to many of the ills of the transportation sector deserve to be explored more fully.

2. PREDATORY PRICING: Professor Dempsey begins his chapter on Pricing with claims of predatory pricing in competitive markets and discriminatory rates in monopoly and oligopoly markets.\textsuperscript{34} Regulation is his answer to both. Rate regulation that defines a "zone of reasonableness" would simply prohibit rates below cost and above a monopoly price.\textsuperscript{35} For price discrimination, the Book asserts that "for the sale of important infrastructure services, such as transportation, it is only economic regulation that protects the public against the pernicious effects of pricing discrimination."\textsuperscript{36} The Report, written after the publication of the Book, takes a more open-minded approach towards solutions for discrimination: "It is time to consider either amending the Robinson-Patman Act to prohibit discrimination in the sale of services, or reestablishing the regulatory mechanism for its prohibition."\textsuperscript{37} Because the oversight solutions to predatory and discriminatory pricing are quite different, we will discuss them separately.

A price is predatory only if it is chosen with the intent to drive out competitors. It is not necessarily below cost, since a profitable price that undercuts the lowest profitable price of the competitors may also drive them out. This kind of predatory pricing is undesirable only if it is likely to lead to monopoly or oligopoly. As long as the market can attract and sustain a sufficient number of competitors, i.e., is not a natural monopoly or oligopoly, price competition is desirable, as Professor Dempsey recognizes.\textsuperscript{38} The principal reason why many jurisdictions do not make such a price illegal is that it is hard to tell whether the price is predatory or competition enhancing. Without knowing whether an industry is naturally monopolistic, it is hard to object to any prices above cost unless there is intrinsic evidence of intent to monopolize through pricing strategies.

Of greater moment are those price levels that are below cost, but that cannot be justified by legitimate pro-competitive reasons, such as reducing prices for a short period to meet the bona fide low price of a competitor if that is necessary to sustain a firm's place in the market. Of concern to economists is below cost pricing that (1) is part of a firm's strategy to drive competitors out of the market and then to capitalize on the predatory firm's monopoly position, or (2) is the result of structural conditions that portend the long periods of unhealthy profits which characterize destructive competition. If strategic pricing is the problem, then antitrust is

\begin{itemize}
\item[34.] BOOK, supra note 1, ch. 5, at 95.
\item[35.] BOOK, supra note 1, at 224.
\item[36.] BOOK, supra note 1, at 220.
\item[37.] REPORT, supra note 1, at 53 (emphasis added).
\item[38.] BOOK, supra note 1, at 224.
\end{itemize}
designed to deal with it. To establish the argument that oversight is not an appropriate substitute for regulation, it must be demonstrated that the structural conditions necessary for destructive competition exist.

Allegations of predatory pricing have arisen in innumerable industries including waste disposal, meat packing, consumer electronics, gasoline and petroleum products, bread, frozen pies, dairy products, newspaper advertising, and eggs, to mention only a few. The traditional antitrust solution to strategic below cost pricing is the application of Section 2 of the Sherman Act, current version at 15 U.S.C. Sec. 2 (1982). If the short term losses in one market are supported by monopoly pricing in another market, discriminatory pricing and therefore the Robinson-Patman Act are implicated, as discussed below. But even in the simple predatory pricing case, the Sherman Act prohibitions against monopolization (in the event the strategy is successful) and against attempts to monopolize (in the event the strategy is unsuccessful) are specifically tailored to separate strategic cases from the short-term, potentially pro-competitive, price cutting by fashioning rules designed to determine the reasons behind pricing policy.

Since predatory pricing is alleged to occur in as many different industries as it does, its existence is not necessarily a sign that the industry's structure is naturally monopolistic or destructively competitive and therefore deserving of regulation. We might interpret Professor Dempsey's allegations of predatory pricing in the transportation industries, then, as a recommendation that antitrust scrutiny of predatory practices be heightened. Federal and state authorities as well as private plaintiffs can bring suit against strategic below-cost pricing. If Professor Dempsey were to identify a weakness in the current interpretation of antitrust theories relevant to predatory pricing, which would be a constructive and logical next step in his analysis, reregulation would be a preferred solution only if (1) political considerations would not permit sufficiently rigorous antitrust scrutiny but would permit sufficient regulatory scrutiny and regulation could be sufficiently flexible to distinguish strategic and non-strategic predatory pricing, or (2) a particular industry were shown to be naturally monopolistic or destructively competitive.

3. DISCRIMINATORY PRICING: Professor Dempsey's catalog of price differences that reflect the lack of competition rather than the cost of providing the service certainly captures the imagination. In 1982, US Air apparently charged its passengers $24 more to fly between Buffalo and Albany than they would pay if they remained on the same plane and flew

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39. Some of the differences may in some measure be explained by differences in cost but, as the example in the text illustrates, others are apparently due to competition. It would be valuable, in analyzing the effect of deregulation, to separate the two.
the 100 additional miles to Boston. Apparently there were greater competitive pressures on the Buffalo-Boston run. Assuming that there were monopoly profits derived from the Buffalo-Albany passengers, those profits might support, at least temporarily, below-cost pricing for the Buffalo-Boston passengers. But even without below cost pricing, monopoly profits in one market distort consumer choices and lead to allocative inefficiency.

Professor Dempsey addresses this question as if it were either simply a price discrimination problem or a price discrimination/predatory pricing problem. His recommended solution, commendably open-minded to an antitrust-based oversight regime, is either broadening the Robinson-Patman Act to cover services (the Federal law only applies to goods, although some state laws currently prohibit price discrimination with regard to services), or regulating rates. The Robinson-Patman Act appropriately recognizes defenses related to the cost of supplying the goods and to meeting the legitimate price of competitors in selected markets, but proper structuring of pricing decisions may make this latter defense a weak protection against US Air-type cases where a firm charges discriminatory rates because of competitive pressure.

This suggestion—that the Robinson-Patman Act may be weak protection against rate discrimination—clearly requires more analysis of the way in which the "meeting competition" defense is applied. But even a detailed analysis would miss the fact that price discrimination in the regulated industries seems to be intimately tied to the concentration in some markets. US Air would not have been able to cover losses in the Buffalo-Boston run, if indeed the prices were non-compensatory, if they did not either have hopes of eventually dominating that route for a long enough period to recapture the losses (which seems implausible), or if they were not willing to apply monopoly profits derived elsewhere to lessen the impact on their annual profit statement. Recapturing the losses by monopoly profits as a result of the discriminatory pricing that drove out competitors would almost certainly be a violation of the prohibition against monopolizing in Section 2 of the Sherman Act while Section 7 of the Clayton Act, 15 U.S.C. sec. 18 (1982), is designed to prevent just the very sort of merger (with Piedmont) that may have lead to US Air's mo-

40. Book, supra note 1, at 43-44.

41. Economists often conclude that it is irrational to support losses in one market with profits in another when it would be more profitable simply to stop competing in the unprofitable market. In the transportation markets, however, it may be either that the losses would be of such short duration that maintaining a presence in the market would be justified or that marketing in the transportation industry requires that one appear to be a major carrier with connections to many points. That marketing necessity may require maintenance of an unprofitable route to maintain both the appearance and reality of having a large route system.
nopoly in the Buffalo-Albany run in the first place. Since United States v. E.I. Du Pont de Nemours & Co.,\textsuperscript{42} it has been clear that long after an acquisition has occurred the merger can be challenged, and that the legality of the merger depends only on whether, at the time of the suit, "there was a reasonable probability that the acquisition is likely to result in a substantial lessening of competition." There is no need to accept the results of these mergers now if the undesirable competitive consequences of price discrimination result. The antitrust option again appears to be a solution that deserves more consideration.

Professor Dempsey points out that only three of the hubs in which one carrier is dominant directly resulted from mergers,\textsuperscript{43} but this does not diminish the relevance of antitrust law. Mergers in other regions that could have been prevented by more rigorous application of Section 7 of the Clayton Act decrease the number of potential entrants into every market. Numerous antitrust cases rely on the doctrine of elimination of potential competition as grounds for challenging a merger. Moreover, the antitrust laws are directed at many types of behavior other than mergers designed to achieve a monopoly. Refusal to lease gates to competitors or even monopolization of those gates may, under proper factual (and, of course, political) circumstances, be a violation of the Sherman Act. As the discussion of predatory pricing reveals, acts intending to result in monopoly, whether successful or not, may violate the Sherman Act. Before concluding that regulation is needed to prevent price discrimination, it seems appropriate to examine the antitrust legality of the behavior that put transportation firms in the position to engage in the behavior. Like predatory pricing, price discrimination occurs in a wide variety of industries. The mere existence of the practice is not an argument for switching from oversight to regulation.

Professor Dempsey's own recognition of the oversight option, as in his recommendation to expand coverage of the Robinson-Patman Act to cover services, could be the first step in a more thorough consideration of the larger antitrust picture.

4. Service Deterioration: For all modes of transportation except airlines, Professor Dempsey's concern in the Service chapter of the Book is with deterioration of service to small communities, discussed in an earlier section. For airlines, there is also a deterioration in the quality of the product consumers now purchase. Some of the evidence is unconvincing: apparently half of those surveyed in one study thought service had deteriorated and half did not think so. But a long list of consumer complaints are described, ranging from concern about flight delays and can-

\textsuperscript{42} 353 U.S. 586 (1957).

\textsuperscript{43} Book, \textit{supra} note 1, at 230.
cellations, overbooking, and misleading advertising to sardine-sized seats, rude customer service, and unappetizing food. This litany exposes two questions. The first is, why would companies who make their money from pleasing their customers be willing to do so poorly? The second is, what should be done about it?

One of the supposed beauties of the competitive process is that firms compete to satisfy customers in both price and service dimensions. Unless it is demonstrated that competition does not work in a particular industry (because of the industry’s natural monopoly or destructive competition structure), it seems a fair initial presumption to conclude that the failure to provide adequate service, in all of its dimensions, is due to a lack of competition. Professor Dempsey certainly agrees that there is a lack of competition and an excess of concentration. Addressing the concentration problem is at least plausibly an oversight problem, as our discussion has already illustrated.

A deeper look at the types of practices about which consumers complain reveals two different sorts of things. The first sort seems to be the kind of complaint that competition would cure. Because these problems are so apparent to airline passengers who care, if they really were significant to customers and would make a difference in airline selection, airlines would compete with better food, friendlier staff, and larger seats. There is, however, a second sort of service problem: unfair competitive practices of a type observed even in very competitive industries like used car sales and trade schools. The truth of some of the claims made by advertisers are hard to test. It is hard to determine whether some of the performance characteristics of a product are due to the particular item purchased. It is difficult for the consumer to discern whether the performance by one competitor is superior to another. Into this category of practices fall those complaints like misleading flight scheduling, overbooking, and misleading advertising. These deceptive practices are the customary jurisdiction of the Federal Trade Commission, which has developed expertise in a variety of industries while exploring the unfairness to competitors of particular business practices. Unless deception is so much more complicated in the transportation industries that it requires a specialized agency, a proposition Professor Dempsey has not established, prevention of these practices does not seem to justify a regulatory agency rather than conventional oversight by the FTC.

It may be in the area of service that Professor Dempsey is least devoted to regulatory alternatives. In both the Book and Report, he describes the ills as well as particular proposed cures, but does not call for

44. Book, supra note 1, at 109-110.
a regulatory authority to issue directives.45 Given our "supervisory" analysis, this is probably appropriate, particularly for addressing the complaints that exist even in competitive industries. For these problems, the nature of governmental intervention does not even depend on whether the industry is naturally monopolistic. For the category of service preferences that a truly competitive market would satisfy, the question, as with so many other current ills of the transportation industry, is whether a truly competitive market can ever occur.

5. SAFETY: Only one of Professor Dempsey's cluster of recommendations for improving safety really involves regulation. The Book's primary recommendation is to ensure that carriers can afford safety (and to withdraw permits if they do not spend their wealth that way) while the Report adds the regulation of landings and take-offs and a series of infrastructure expenditures by the Government to reduce hazards. The additions offered in the Report seem to be appropriate governmental expenditures, assuming, as we have, that there are defects in these areas, and regulating landings and take-offs for safety purposes seems to be an obvious part of individual airport management. Naturally, however, the suggestion of rate and entry regulation to ensure profitability draws our critical attention.

As we will develop in more detail below, it is uncertain whether the ills of the industry are the results of deregulating transportation systems that have operated in a regulated market for so long, or are the inevitable effects of the industry's structural characteristics. Once again, the existence of ills such as unprofitability does not alone prove the existence of such structural characteristics.

It seems quite plausible that any industry, suddenly released from behavioral constraints, either technological or, as in this case, regulatory, will go through a period of instability regardless of whether regulation was appropriate in the first place. Evidence of that instability might be the entry of numerous firms that do not possess the ability to survive in the market, numerous bankruptcies as some firms survive and others fail in the changing conditions, and even low profitability of surviving firms while the new entrants challenge their right to customers. This is the critical question: whether a mass of data that richly paints an instability is proving the need for a return to regulation, or is simply the evanescent consequence of deregulation, whether initially justified or not.

Economists expect that there will be some turnover in firms and shifting of market shares and relative profitability in any dynamic market. Such changes might even describe healthy competition. A market released from legal constraints would be expected to exhibit even more

45. Book, supra note 1, at 238; REPORT, supra note 1, at 54-55.
"turmoil," as Alfred Kahn describes it, even if eventually it will stabilize and become a more typical competitive market. Evidence from what might be only a "shake-out period" may demonstrate that the rapidity of deregulation and the lack of supervision after deregulation was an error, but it alone is not proof that the market is structurally characterized by destructive competition. We recognize that the turmoil of rapid entry and exit, of bankruptcies and of periods of low profitability, is costly to the economy. But laissez-faire describes a market free from legal constraints, not one free from costs. Finding the appropriate mechanism for reducing those costs involves looking beyond the symptoms to the cause, which may be the lack of regulation, as Professor Dempsey assumes, or it may be the instability induced by deregulation, or the lack of proper oversight during the change from one to the other. The next logical step, once again, is to examine the structural characteristics of the various markets involved. Unless the transportation industries are shown to be structurally different from other industries, the usual remedy of more competition, guaranteed by government oversight of the competitive process, rather than less, as would occur under regulation, seems the appropriate way to ensure both productivity and profitability.

6. SERVICE TO SMALL TOWNS AND ECONOMIC EFFICIENCY: If carriers are not required to service unprofitable routes, they will not do so. This disadvantages entrepreneurs located in small towns who cannot get their products to market. If carriers have higher costs in servicing some routes than others, businesses along the higher cost routes will have to pay more and will, therefore, be at a competitive disadvantage relative to those whose location was chosen to reduce the costs of satisfying customers. Undoubtedly true. What do we do about it? Unlike the other problems that Professor Dempsey identifies, many policy makers do not even see this as a problem. Some even believe that a market that gives firms incentives to minimize the costs of satisfying consumers is working correctly.

The difficulty with analyzing Professor Dempsey's proposals in this area is that the answers depend on political and distributional opinions. Deregulation may in fact have been a product of the political judgment that small towns did not deserve subsidies from large towns. The subsidies had been provided by cross-subsidization; shippers in large towns paid artificially high rates so that shippers in small towns could pay artificially low rates.46 If deregulation was intended to eliminate the cross-subsidies and wealth transfers, it was apparently a booming success, not a failure. The shrinking of the scheduled air service network is happening as it may have been intended. The evidence of deterioration of service to

46. Book, supra note 1, at 204.
small towns is therefore hardly surprising, nor is the evidence of the substi-
tution of more efficient, smaller commuter planes for larger, less-effi-
cient jets and the reduced satisfaction of passengers who used to enjoy
subsidies. Of course they are complaining, but it is about the withdrawal
of a benefit for which others were paying.

Occasionally, Professor Dempsey's arguments reflect both his distri-
butional preferences and a concern for "discriminatory" rates.47 If this
means discriminatory by Robinson-Patman standards, reread our discus-
sion above. If "discriminatory" just reflects the higher costs of serving
the remote shipper, then the concern is a distributional judgment, not an
economic fact.

It appears from the Book that the reduction in service is greater than
what was expected.48 Congress responded politically, which seems to
be appropriate in a democracy, and has maintained the direct subsidy to
carriers serving uneconomic markets.49 This solution does not seem to
require regulatory supervision, so far as one can tell from either the Book
or the Report, and Professor Dempsey's support for it is a respectable
distributional preference, whether we agree with his favorite forms of
charity or not.

In the Report, Dempsey takes exactly the proper course in dealing
with the allocative inefficiencies inherent in subsidizing one activity by arti-
externally enhancing the costs of another. To policy analysts who believe
that pursuing allocative efficiency is the only justification for government
intervention, Professor Dempsey's distributional preferences will never be
convincing. It is unquestionably the case that supporting artificially low
prices in one market through artificially enhanced prices in another dis-
torts consumers' choices. Without that distortion, consumers' decisions
would be based on the actual costs of allocating resources to one use
rather than another. As Professor Dempsey says, however, "society fre-
quently views the achievement of objectives other than allocative effi-
ciency as warranting some sacrifice of the latter."50 While Congress
apparently agrees with him, this ordering of objectives does not support a
call for regulation. Dempsey does not demonstrate that establishing ser-
vice territories through entry regulation51 is preferable to direct subsidies.
Hiding the subsidies through higher prices to lower cost shippers only
creates the illusion of a budgetary saving.

47. REPORT, supra note 1, at 54.
48. BOOK, supra note 1, at 202.
49. Id. at 204.
50. REPORT, supra note 1, at 54. See also, BOOK, supra note 1, at 78 ("[S]ociety frequently
\ views the achievement of objectives other than allocative efficiency as more important than fidelity
\ to the ideology of laissez faire").
51. REPORT, supra note 1, at 54.
III. IS TRANSPORTATION REALLY SPECIAL?

Throughout the previous section we have described the authority of antitrust and fair trade enforcers, both public and private, to address many of the ills which Dempsey describes. In some cases the antitrust enforcers appear to have done a better job than the regulators did in curbing anticompetitive behavior, but in example after example the regulators have failed to do a satisfactory job of controlling the industry even after deregulation. Even those that cannot be addressed by what we have called "oversight" do not obviously require reregulation unless the markets involved can be described as naturally monopolistic or destructively competitive. But this is the big question: "Do these industries possess the structural characteristics of natural monopolies or markets in which competition is destructive?" What is Professor Dempsey's evidence?

As we discussed above, evidence of low profits, predatory pricing, discriminatory pricing, and bankruptcies may be symptoms of natural monopoly or destructive competition, but they are equally consistent with anticompetitive behaviors witnessed in other industries that no one suggests regulating. According to the Book, when the transportation industries were initially regulated there was a lot going on that had nothing to do with the inherent structural nature of the industries. Railroads suffered from overcapacity due to government support of railroad expansion; and the Interstate Commerce Commission was a response to political shenanigans, watered stock and other forms of financial piracy, and differences in rates that caused what even Professor Dempsey refers to as "blind antagonism" towards the railroads.\textsuperscript{52} The motor carriers were initially regulated during a period of excess capacity, during the Great Depression of the 1930's, at least partially in response to Congress's desire (undoubtedly encouraged by the railroads whose excess capacity problems were aggravated by increasing truck competition) to create equality in the regulatory scheme. It seemed unfair to regulate railroads but not their competitors.\textsuperscript{53} In addition, the depressed business conditions that created the excess capacity also created extraordinary conditions in all industries and so massive government intervention was invoked.\textsuperscript{54} Airline regulation soon followed, to continue the parallel regulatory structure and to promote national defense interests.

During this initial regulatory period, the economy witnessed many of

\textsuperscript{52} Book, supra note 1, at 8-10.
\textsuperscript{53} Id. at 17.
\textsuperscript{54} Professor Dempsey claims that under regulation the industry grew and prospered. Id. at 18. Towards the end of the 1930's, however, everything prospered as the world came out of the Depression and prepared for war.
the ills of the eighties that Professor Dempsey describes so dramatically. The excess capacity, caused not by the inherent structural nature of the industry but by exogenous factors, government subsidies, intermodal competition, and depressions, naturally led to unprofitability, price cutting, and predation. Currently we observe many of the same ills, quite possibly created not by the inherent structural characteristics of the industries but by the shock of sudden deregulation without appropriate oversight. Railroads suffer unprofitability from intermodal competition that had been deferred or limited by regulation. Even efficient motor carriers are going bankrupt because they have lost a great share of the "equity" that they used to possess in the form of their operating certificates. Entry barriers resulting from failure to enforce the antitrust laws regarding mergers or predatory pricing in the airline industry prevent the competition necessary to ensure profitable pricing and service. This is indeed "cruel restructuring" but it is not necessarily the result of either natural monopoly or destructive competition.

A. DESTRUCTIVE COMPETITION

Professor Dempsey's destructive competition arguments come in one iterated form: Transportation is an industry inherently vulnerable to overcapacity because an empty seat or a partially filled trailer or railroad car is an "instantly perishable commodity."

We have already offered our own doubts about at least the uniqueness of that condition, and have suggested that it alone does not account for the special evils he is seeking to correct. There must be something more.

The "something more" that the Report reveals may be the extremely low marginal costs of production in the transportation industries. As long as an additional seat or portion of a truck can be sold at a price that covers the incremental cost of providing it, it will be more profitable to sell a bit of transportation below its full cost than not to sell it at all. Because it is more profitable, transportation companies will predictably offer lower rates as they find empty space just before the flight. Hotels will give a better room rate if they have empty space at midnight. Symphonies sell rush seats just before the show. We could understand regulating hotels and symphonies under this logic, but airline pricing does not follow this pattern. To the contrary, airlines charge higher prices to people who try to make reservations just before take-off. The airlines have figured out

55. Id. at 34.
56. Id. at 41, quoting Frank, Airlines, Forbes, Jan. 4, 1982, at 198.
57. REPORT, supra note 1, at 52, for instance.
58. We do not mean to suggest that airlines are pricing irrationally. Airlines are pricing by an inverse elasticity rule, assuming that those who make plans at the last minute, business peo-
ahead of time, apparently, who those people would be who would fly at a vastly reduced rate and, as it happens, those passengers for whom travel is relatively more discretionary are also able to make reservations ahead of time. There must be something more going on that distinguishes the transportation industry.

Traditionally, the basic requirement for a destructive competition industry was relatively high fixed cost. For railroads, the regulation of which started the move towards "parallel" regulation of motor carriers and airlines, 22% of costs are fixed.\(^{59}\) It is particularly easy to imagine destructive competition among railroads whenever overcapacity exists, because compared to the costs of fuel and an engineer (and however many conductors the contract requires) the fixed costs of tracks and roadbeds loom large and a price that would cover any portion of those fixed costs in addition to the energy and labor costs would be better than not selling the service at all. "Losses" from this strategy could go on for a long time, since the immovable roadbed cannot very quickly be sold off to someone with a more profitable use for it. As long as there is a market for gates at airports, for airplanes, or for trucks and buses, however, it is hard to see from the arguments presented in the Book or the Report how unprofitable overcapacity could continue for very long.

The economic argument offered in the previous paragraph is not original; the deregulators had it in mind when deregulating the airlines and motor carriers in the first place. And like so many other economic arguments, it has a tremendous capacity for assuming too much about the characteristics of the industry. It seems as though there is a better market for used gates, planes, and trucks than for railroad track but we are not the fact experts. Evidence showing that competition is fierce does not, however, automatically mean that assumptions are wrong, if the evidence is also consistent with another theory—in this case, that the airlines have engaged in behavior that could be prevented by rigorous and conventional antitrust enforcement.

**B. NATURAL MONOPOLY**

As we have said, the essential requirement for a natural monopoly is that there be insufficient demand in the relevant geographic market to support the profitable supply of a service by two firms at an efficient level of cost. Analogously, a natural oligopoly might occur in the market where there is insufficient demand to support more than a few firms efficiently.

\(^{59}\) Book, *supra* note 1, at 69.
Under either of those circumstances, it is reasonable to suppose that the firms in the market will not behave competitively. The behavior of particular concern is enhanced prices in such markets where there are no potential entrants waiting to enter and satisfy consumers by offering lower prices—that is, where markets are not "contestable."

Professor Dempsey's discussion of contestability illustrates quite nicely the difficulty of translating economic assumptions into reality. Particularly bedeviling for those who predicted that entry or the threat of entry would eliminate monopoly profits, is the ability of airlines to respond immediately to price cutting. A new airline that cannot capture customers by undercutting the price of existing competitors will not be as easily attracted to enter the market. Combined with the spotty history of upstart airlines, the apparent anticompetitive behavior of existing firms, and the barriers to entry allegedly created by frequent flyer plans, it does in retrospect seem futile for policy makers to have relied on new airlines to challenge the old.

The contests for business take place market by market, however, and many of the entry barriers that would survive rigorous application of the antitrust laws do not apply to existing carriers, which might expand their minor presence in the market or enter a market in a limited way without incurring the costs of starting up a new airline. The domination of gates, for instance, might not withstand antitrust scrutiny while the frequent flyer barrier may not be as insurmountable for existing carriers. It might still be too early to give up the contestability argument since antitrust law has not been given a chance to remedy the anticompetitive behavior.

Even if a market is contestable, however, competition will not succeed where there is insufficient demand to support a number of competing airlines. It is these naturally monopolistic or oligopolistic markets that present the greatest resistance to antitrust oversight. Since evidence that monopoly prices are being charged or that there is high concentration in many markets is consistent with either anticompetitive behavior or natural monopoly (or oligopoly), we need to find some way to distinguish the cases before reregulation can confidently be recommended.

The natural monopoly question is a structural one, requiring an analysis of the cost structure of providing the service and of the level of demand in the market. This needs to be done market-by-market until one learns enough to generalize about the types of city-pairs, for instance, in which rate supervision is necessary. This is undoubtedly too extensive.
and too technical a task for either Professor Dempsey's Book or Report. We do not fault him for its omission. But as a matter of policy selection, the choice between applying antitrust remedies or regulatory remedies to a particular market certainly requires it. The absolute size of competitors does not compel the conclusion that a natural monopoly exists nor does evidence of collusion between them; a full consideration requires an examination of minimum optimal size relative to demand in a market. Evidence of concentration is not enough alone, particularly where there is also evidence that the firms in the market obtained their market shares by illegal predatory pricing, or where the concentration data is national rather than market specific. "Regulation at the margins" requires consideration of where oversight fails. The limited information on whether there actually are any naturally monopolistic markets, as there surely must be, makes one question the proof that regulation is required at all.

Professor Dempsey identifies the expense and evidentiary difficulty of antitrust litigation as a reason why regulation is preferred. But a sensible principle of policy analysis, inquiring into the justifications for government intervention in the market place, must include a comparison of the costs of intervention with the costs of letting the ills in the market persist. The relevant corollary is that the costs of antitrust oversight must be compared systematically with the costs of regulation. That would involve more than comparing the costs of running the Antitrust Division of the Justice Department to the costs of running the Interstate Commerce Commission or Professor Dempsey's new Federal Transportation Commission. It would require as well a comparison of the relative flexibilities of the oversight and regulatory alternatives. The Book reveals that the CAB "turned a deaf ear" to World Airways begging for an end to predatory pricing in the transcontinental market, where fares fell to $99 one way. Professor Dempsey had started to identify in more detail, in the Report, the political considerations involved in selecting regulators who would be neutral and unbiased. But it may be that the political problems are less severe in antitrust enforcement, where federal enforcers are appointed by the executive branch but state enforcers are inclined to be of all political stripes and private plaintiffs have no uniform political axe to grind at all.

Professor Dempsey also criticizes the antitrust remedy as being lim-

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63. BOOK, supra note 1, at 12 (size of railroads).
64. id. (Evidence of extensive pooling arrangements to suppress rate wars).
65. id. at 84-85. (Economies of scale combined with entry barriers are said to create a natural monopoly but there is evidence that trucking firms created entry barriers and obtained economies of scale by predatory practices).
66. id. at 86-87.
67. id. at 222.
68. id. at 43.
69. REPORT, supra note 1, at 57.
ited to damages, which may compensate the victim of an antitrust injury but fails to restore competition to the marketplace. As a result, he says, "the public's interest in a healthy competitive environment goes unsatisfied." In fact, antitrust remedies available to the government include a full range of equitable remedies including divestiture of assets acquired under a merger, which could restore a competitor to the market, and perhaps more significantly, injunctive relief, which can stop anticompetitive behavior before the competitor is eliminated. Proof of an actual anticompetitive effect is not required. In fact, a case for attempted monopolization can be made out even if the attempt has not been successful. The treble damages remedy is designed to more than compensate the victim, in order to give private plaintiffs the incentive to vindicate the public's interest in a healthy competitive environment and deter would-be violators. Rate and entry regulation is not always better than that. In this case, it may not be nearly as good.

IV. A POSTSCRIPT ON DIALOGUE

The arguments that Dempsey supports in the Report and in the Book present an opportunity for us to comment on a set of questions rather different from the analytical business that we have just been through. While they are not questions raised uniquely by Dempsey's work and no one else's, the elegance of his presentations and the grandness of his grasp of the data do bring certain heuristic problems clearly into view. They have to do with the nature of economic argument, and with the linkage between empirical investigation and policy choice.

By their nature, policy choices create and distribute benefits and risks. An interstate highway system advantages many, and creates an irreducible risk of harm to others. Keeping new drugs from the market for a time protects some future purchasers but denies likely benefits to others who will die in the meantime. Safer cars could be mandated, but at the cost of other sacrifices and distortions. Some people like guns. Others like butter. The solution is never just mathematical. Such is the nature of policy choice.

Policy debate therefore occurs on various levels, two of which might be described as subjective versus objective, opinion versus fact, advocacy versus science. The Preface to the Book carefully warns the gentle reader that Dempsey is presenting only one side of the debate, that the reader should add Dempsey's contribution to the opinions of others to get the full picture. Because this caveat is never repeated in the Book itself (nor anywhere in the Report), and because it is so important to a proper

70. Book, supra note 1, at 222.
interpretation of Dempsey's argument, we think it appropriate to highlight some of the reasons why Dempsey's warning should be taken seriously.

If we were to describe the rules that might ideally govern the terms of a policy debate, an attempt to match the style of argument to the nature of the choices in review, we might begin with the following four desiderata:

First, debate should recognize the difference between analytical propositions and policy judgments—between, that is to say, questions for which facts are answers, and questions for which facts are wholly secondary to the choice of preferences.

Second, all data not derived from controlled experimental designs would require additional argumentation to demonstrate that the correlations were causal, and that the causes are germane to the choices than in issue. Post hoc, again, isn't always propter hoc.

Third, there would be a distinction observed and respected, between objective or scientific inquiry on the one hand and "advocacy" on the other. This is not to say that advocacy cannot be scholarly or objective in many senses of the word, nor that advocacy isn't useful in the application of science (nor even that it is ineradicable), but only to suggest that once an argument is labelled by convention or by signature, certain conventional limits should attach.

Fourth, there would be, in an objective inquiry, a rule against impassioning the assembly with characterizations of facts that, while true, have the effect of motivating by their color and the susceptibilities of the audience rather than by their content and the strength of their meaning.

Facts are important, no doubt about it. The judgment about trading off humane values against economic efficiency requires some measure of how much of the one jeopardizes how much of the other, and of how various methods of titrating the two might adjust the marginal advantages. Unless there is to be a decision at one end point or the other, measurements of marginal costs do provide one useful starting point for the argument.

But they hardly conclude it. Vast piles of facts, about the benefits of cheaper transportation and the costs of injuries, about the distributions of gains and the focus of harms—about the values of subsidies to small towns at the cost of efficiencies to others—will never solve the problem of whether one ought to have a subsidy for this group or that, nor of how much. The facts are there to demonstrate the consequences of the policy choices, not to make them. There is a danger, though, that while more and more facts add more and more clarification and definition of the pref-
ference choices, at some point their mass overwhelms the dialogue. But the preference questions are still not resolved.

There is also, in this heuristic catalogue, the risk of confusion about the meaning of disproving a non-exclusive hypothesis. Or if you like, call it the burying of the burden of proof. During a debate an advocate expounds a theory which predicts that doing X will be very, very good. An opponent then destroys with facts the credibility of that one theory. Strictly speaking, the net effect should be zero—the pendulum still dangles in the middle. It has not thereby been established that doing X will be very bad.

Dempsey makes rather much of the facts which prove that Alfred Kahn was wrong in his theory of contestable markets and in his predictions of limits on economies of scale. While broken promises may be reasons for voting the scoundrels out of office, they are not in our view facts which prove the contrary of what the promisors had wanted to achieve. Dempsey’s facts may (or may not) have destroyed one set of arguments in favor of deregulation. But unless he is able to establish that those discredited arguments are the only legitimate reasons for moving in a particular direction, the reader should not accept the contrary positions without more. Disproving a negative is a contribution; it is not a conclusion. And rigor with facts is not necessarily more important (though it is easier) than rigor with preference is.

Even within the realm of the facts there are limits. A true empirical investigation requires an experimental group and a control group, each measured before and after the introduction of the experimental variable. If differences appear in the two “afters” which cannot be explained by any factors other than the variable being tested, it is legitimate to conclude (infer, actually) that the variable and its results are causally connected.

The real world does not allow for controlled experiments very often. The uncontrolled types are about all we have, most of the time. One of those is the before and after, without the control group. If the after is different from the before in a way that is explained by the introduction of the tested variable, we can infer some causal linkages, but with much less certainty and with the need for far greater caution than would be true for a true experimental design. In other words, post hoc is not necessarily propter hoc. It might be, if everything else can be ruled out. But not necessarily.

Deregulation occurred, and the commercial fleet is older than it was before. Is deregulation the cause of that aging? Maybe, but Dempsey does not give us enough data to be able to tell. What was the aging per year during regulation? Were the demand and supply functions different across time for other reasons, so that after a certain amount of new air-
craft purchasing the market would go soft for a while because the demand had just been satisfied?

Likewise for near misses, cardboard food, luggage in perdition, younger flight crews. . . These all occurred after deregulation began. Dempsey would have us believe they occurred because deregulation began. And he does propose a plausible theory—under competition, profit margins are slimmer and so investment in these commodities is systematically reduced. What little revenue there is, he implies, is spent just keeping the planes aloft. But it is also true that the air traffic control system is very different now from what it used to be, for reasons that have nothing to do with deregulation.

What we do need to know is what would have happened anyway. That much of the argument is not in either the Book or the Report. And without it, a two-celled design is a precarious sort of animal. There are male flight attendants now, and older female flight attendants. There were not many of those before 1980. Is that change a consequence of deregulation? Or could it be from some entirely different cause? How can we tell?

The critical question has to do with the difference between deregulation on the one hand, and nonregulation on the other. The fact is, that since its adolescence the airline industry at the least—and trucks and trains even more so—has never been unregulated. Airlines accepted regulation in return for subsidies (early mail contracts); railroads took it in return for protections. And so, as Dempsey records, regulation has been the only way of life the industry has ever known. What we have, then, after 1980 or so, is not an unregulated industry, but a deregulated one.

Consider just one possibility. Under regulation, where pricing is at least in part a function of costs, the management of an airline has less incentive to incur labor unrest than would be true in an industry completely unprotected from the realities of a competitive marketplace. It is therefore possible (though we do not say that it actually happened) that the costs of labor for airlines and trains were allowed to rise to supra-competitive levels. "Featherbedding," we believe it has been called. With deregulation and the competition it brings, airlines saddled with long-term labor contracts will face very serious perturbations in a competitive environment, problems which they might not have faced had they never been regulated in the first place.

How much of the mess we are in, described by Dempsey's data, is attributable to neither regulation or nonregulation, but rather to the change from the one to the other? As the Republicans in the White House have said of the economy, we cannot overcome in a night the effects of a binge that lasted a generation.

Exactly how the case could have been made is not something that
we are able to comment on. But the fact that it needs to be made seems clear to us at least. One airline, America West, has grown up after deregulation and seems to be among the most successful in the industry. Are there other examples which, along with America West, could have been used as a sort of surrogate fourth cell in the experimental design? It seems likely; but in any case, it certainly does seem necessary.

The point is simply that the data do not compel reregulation if they can be as easily explained by the fact of deregulation as they could be by the fact of nonregulation. Policy-makers should be alert to this crucial difference—a special variant of the general maxim that bad enough should be left alone.

We offer one final criticism, or caveat in the assessment of the importance of this generally well-done work. The assemblage of the facts, the interweaving of analytical and policy arguments, the failure to take advantage of opportunities (albeit limited) for a more compelling heuristic structure, sum to a style which deserves some note.

There is a difference between scientific inquiry and advocacy. Advocacy presumes a forum with a neutral and capable decision-maker, in which each contesting point of view needs and deserves a champion. The champions have no duty to be objective; that is the job of the forum. Advocacy is inherently partisan. Decision-making, perhaps especially decision-making in the realm of social preference, ought to have advocacy as at least a part of its method.

Scientific inquiry is something else again. It purports to be objective. Its purpose is to investigate agreed-to issues, or to use data to clarify issues for policy-makers to consider. Its obligation is comprehensiveness—the statement not of one argument, but of all. The presentation not of data that would establish a single point of view, but of data which portrays a more complete picture, which essays the consequences of all the reasonable alternatives.

Science, moreover, because of its purpose to inform rather than to persuade, avoids the presentation of facts in ways colored toward a certain point of view, or designed to move the reader by tugging at hidden fears or foibles.

In these works we read, more in the Book than in the Report, phrases such as "the social Darwinist grave of bankruptcy." We are told that "Under deregulation, management philosophy in the airline industry is dominated by the predatory insight of P.T. Barnum, 'There's a sucker born every minute.'" And "Too many of us have seen the crushed accordions of twisted steel and bent chrome on our interstate highways that were passenger automobiles before they were squashed by huge diesel-powered trucks pulling giant trailers. . ." Dempsey begins his summary with this: "The industry's unrealistic scheduling, funneling of aircraft into
hub and choke bottlenecks, and filling of cockpits with near adolescent pilots, have significantly narrowed the margin of safety and sent the number of near-misses skyrocketing. Airline service has gone to Hell in the 80's. We are herded aboard aerial slums, served cardboard food, overbooked, bumped and misconnected. Our luggage is routed through the Twilight Zone, never again to be seen during our natural lives."

There are more, but those will do. We are, it must be said, generally admirers of Dempsey's literary style. And we are most certainly not attempting to say that such a style—the style of advocacy rather than the style of neutral science—is inappropriate. No science has ever advanced without its passions and its partisans. Especially in the field of policy debate, advocacy is very much to be called for and prized. But the style does justify the warning of the Preface: Consider this to be just one version of the picture, one glimpse of the problem and its array of potential solutions. Just one glimpse.

But what a glimpse it has been! We have been shown twisted heaps of metal and bloodless competitors lying in the Darwinian grave of bankruptcy, apparently choked to death on cardboard food, whose airplane seats have left the gate, their value lost forever. Small towns and big subsidies and the spirit of America bent 'neath the burden of the inelastic supply curve. But, and more seriously, we have also seen how even an elegant theory—such as that which led us to deregulation—can lead us astray when its dependence on empirical accuracy is disappointed by the failure of empirical estimates. If Dempsey has done nothing more, he has certainly taught policy makers exactly that weakness, and therefore the need for modesty about the course the theory commends.

None has limned the facts so well and few have argued a case more elegantly than Dempsey has in these two works. While in the end we prefer our supervision to his regulation, we applaud his contribution to a perplexing and lively debate. Well done, dear friend.