

**STATEMENT OF SUSAN L. KURLAND
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before the

**COMMITTEE ON COMMERCE, SCIENCE, & TRANSPORTATION
U.S. SENATE**

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Chairman Rockefeller, Ranking Member Hutchison, and Members of the Committee:

Introduction

I appreciate the opportunity to appear before you to discuss the current and future state of the airline industry and the role of the Department of Transportation (DOT) in the industry's ongoing restructuring. This hearing is in response to the proposed United/Continental merger, a potential combination that has understandably captured the interest of this Committee and the American people.

State of the Airline Industry

Let me begin with a brief overview of the state of the airline industry to provide an understanding of the economic environment in which this transaction has been proposed. In the more than 30 years since deregulation, market forces have shaped airline fares and services. During that time, the industry adjusted to a deregulated environment and changing market conditions, facing the expected – fluctuations in supply and demand – but also the unexpected – terrorist attacks, epidemics, and now, with volcanic ash, a natural disaster. Through the various business cycles, carriers have taken steps to cut costs, manage capacity, and cope with volatile fuel prices. Many have adapted well, but not all have succeeded, with an unfortunate number having to file for bankruptcy protection and several exiting the industry altogether.

Following several consecutive years of losses from 2001 to 2005, the industry returned to modest profitability in 2006 and 2007, only to confront rapidly increasing fuel costs and then a global recession. 2008 and 2009 were some of the most challenging years in the history of U.S. aviation, primarily because the global recession helped push operating revenues for the nine largest U.S. airlines down an unprecedented 17% year-over-year. While costs also increased significantly during the first quarter of 2010, airline revenues continue to rebound in large part on the basis of increased passenger volumes.

Each one of the nine largest U.S. carriers increased their revenue, year-over-year, despite the fact that all but one of them decreased or held capacity constant. For the first quarter, the nine largest airlines, whose revenue totaled nearly \$27 billion, collectively earned a small operating profit of

\$17 million, excluding special items. While modest, that represented a substantial improvement from the total operating loss of over \$1 billion during the first quarter of 2009.

For the second quarter of 2010, most analysts are predicting stronger results, as passenger and shipper demand that vanished during the height of the global recession is returning across all sectors for all carriers. The turn-around from this time last year is encouraging.

Consumers have reaped enormous benefits in the more than 30 years since airline deregulation. During this period, air transportation has been transformed from a luxury that few could afford, to a service that provides average families and small businesses of America with affordable access to destinations across the globe. Adjusted for inflation, air fares have continued to decline throughout the deregulated era, as new carriers, particularly low cost carriers, have entered the market and business models of new entrants and incumbent carriers alike have adapted to meet changing consumer needs and brought innovations and efficiencies to the marketplace. In expanding consumer and business access from local to global, air transportation has become an important driver of economic progress for the citizens and companies of this increasingly mobile nation.

We foresee the industry continuing to evolve along several basic trends. First, carriers, while conscious of costs, are aggressively pursuing new sources of revenue. Second, over time, low-cost carriers have expanded significantly. Third, legacy carriers are continuing to seek ways to become more efficient producers, including through stronger alliance partnerships.

DOT's Authority to Review Merger Transactions

I am sure you understand that I cannot discuss the specifics of the proposed United/Continental merger, or any proposed transaction that is before us for review. However, I would like to shed some light on DOT's role in the review of an airline merger.

The Department of Justice (DOJ) has the lead role in reviewing proposed airline mergers, given its statutory authority to enforce the antitrust laws. Utilizing its special aviation expertise, DOT typically examines the proposed merger and shares its analysis and views with the Antitrust Division. This practice is consistent with Congress' determination that the deregulated airline industry should generally be subject to the same application of the antitrust laws as other unregulated industries. Each transaction we review is considered on a case-by-case basis consistent with anti-trust principles and practice.

The purpose of our antitrust laws is to ensure that consumers receive the benefits of competition, and this is the prism through which the Department analyzes airline mergers. I can therefore assure you that the Department is committed to fostering an environment that embraces competition and provides consumers with the price and service benefits that competition brings.

We also recognize that the airline industry is very dynamic. Cyclical economic conditions, the competitive environment, infrastructure access and capacity, and industry innovation all need to be taken into account to allow the industry to adapt to rapidly changing economic conditions.

Should DOJ decide not to challenge a particular transaction on antitrust grounds, DOT would then consider a wide range of follow-on issues that fall within its jurisdiction, including international route transfers, economic fitness, code-sharing, and possible unfair or deceptive practices.

As to international routes, the carriers would be expected to apply for DOT approval of a route transfer to consolidate the international routes they individually hold under one certificate as part of the merger process. By statute (49 U.S.C. 41105), DOT may approve a transfer of such routes only if we find that it is consistent with the public interest. As part of that analysis we must examine the transfer's impact on the viability of each airline party to the transaction, competition in the domestic airline industry, and the trade position of the United States in the international air transportation market.

We would only decide an international route transfer case after we had established a formal record and given all interested persons the opportunity to comment. If DOT determines that the transfer would be contrary to the public interest on competitive grounds or for another reason, DOT could disapprove the transfer in whole or in part. Alternatively, DOT may condition its approval on requirements that would protect the public interest.

Because a proposed merger of major carriers would involve a significant change in the structure of at least one of the existing carriers, DOT would institute a fitness review of airline management, financials and compliance disposition.

While the transfer application is pending, the merging carriers could request that DOT grant them an exemption from the provisions of 49 U.S.C. 41105 to allow them to consummate the merger at their own risk pending DOT's decision on their transfer application. DOT has sometimes approved such exemption requests in the past, conditioned upon the air carriers remaining separate and independently operated entities under common ownership until the transfer application case is decided.

DOT may also review any code-share arrangements concluded between the merging carriers. In DOT's experience, code-share arrangements would likely be necessary during the early phases of integration after the transaction is closed.

Finally, at DOT, we take our responsibility for consumer protection seriously. For example, if carriers in pursuing or implementing a merger were to engage in unfair or deceptive practices, we would not hesitate to act to protect affected consumers based on our 49 U.S.C. 41712 authority.

Conclusion

Airlines are the circulatory system of national and global communities – linking friends and family, suppliers and producers, retailers and manufacturers, facilitating business partnerships, and fostering educational and cultural exchanges of all types. Every American has both a personal and an economic interest in access to safe and affordable air travel. It is therefore easy to understand why so many people take an interest in airline mergers.

Our consideration of aviation economic policy focuses on what is best for a healthy and a competitive industry, for its workers, and for the communities and consumers that it serves. Our goal must be to strike what is often a very difficult balance in the face of a complex and dynamically changing industry. Importantly, in doing so we must also consider the longer term, collective impact on all stakeholders, most importantly America's traveling public.

Mr. Chairman, this concludes my testimony. I would be happy to answer any questions you may have.