

ORIGINAL

Public Version  
DEPT. OF TRANSPORTATION  
DOCKET

BEFORE THE  
DEPARTMENT OF TRANSPORTATION  
WASHINGTON, D.C.

2005 FEB -8 P 4: 28

Joint Application of )  
 )  
 ALITALIA-LINEE AEREE ITALIANE-S.P.A. )  
 CZECH AIRLINES )  
 DELTA AIR LINES, INC. )  
 KLM ROYAL DUTCH AIRLINES )  
 NORTHWEST AIRLINES, INC. )  
 SOCIÉTÉ AIR FRANCE )  
 )  
 Under 49 U.S.C. §§ 41308 and 41309 )  
 for approval of and antitrust immunity )  
 for alliance agreements )

OST-2004-19214 -48

Joint Application of )  
 )  
 DELTA AIR LINES, INC., )  
 KLM ROYAL DUTCH AIRLINES, )  
 NORTHWEST AIRLINES, INC., )  
 SOCIÉTÉ AIR FRANCE, )  
 ALITALIA-LINEE AEREE ITALIANE-S.P.A., )  
 CZECH AIRLINES )  
 )  
 for statements of authorization under )  
 14 C.F.R. Part 212 (blanket codesharing) )

JOINT APPLICANTS'  
SUPPLEMENTAL INFORMATION RESPONSE

February 8, 2005

Communications with respect to this document should be sent to:

Michael F. Goldman  
Silverberg, Goldman & Bikoff, LLP  
1101 30<sup>TH</sup> Street, NW, Suite 120  
Washington, DC 20007  
(202) 944-3305  
for SOCIÉTÉ AIR FRANCE

Jean-Michel Barthelemy, Vice President -  
European and International Affairs  
Jean-Marc Bardy, General Counsel  
SOCIÉTÉ AIR FRANCE  
45, rue de Paris, F-95747  
Roissy CDG Cedex  
Paris, FRANCE

Paul V. Mifsud, Vice President -  
Government and Legal Affairs, USA  
2501 M Street, NW  
Washington, DC 20037  
(202) 861-5867  
for KLM ROYAL DUTCH AIRLINES

Richard D. Mathias  
Zuckert, Scutt & Rasenberger, L.L.P.  
888 Seventeenth Street, N.W.  
Suite 600  
Washington, DC 20006-3309  
(202) 298-8660  
for ALITALIA-LINEE  
AEREE ITALIANE-S.P.A.

Allan I. Mendelsohn  
Sher & Blackwell  
1850 M Street, NW  
Suite 900  
Washington, DC 20036  
(202) 463-2508  
for CZECH AIRLINES

Robert E. Cohn  
Alexander Van der Bellen  
Shaw Pittman LLP  
2300 N Street, NW  
Washington, DC 20037  
(202) 663-8060  
for DELTA AIR LINES, INC.

D. Scott Yohe, Senior Vice President -  
Government Affairs  
Delta Air Lines, Inc.  
1275 K Street, NW, Suite 1200  
Washington, DC 20005

John J. Varley, Vice President -  
Associate General Counsel  
J. Scott McClain, General Attorney  
James A. Coblin, Senior Attorney  
Delta Air Lines, Inc.  
1030 Delta Boulevard  
Atlanta, Georgia 30320

Andrea Fischer Newman  
Senior Vice President, Government Affairs  
Megan Rae Rosia, Managing Director  
Government Affairs and  
Associate General Counsel  
901 15<sup>th</sup> Street, NW, Suite 310  
Washington, DC 20005  
(202) 842-3193  
for NORTHWEST AIRLINES, INC.



regard to such confidential documents, and the confidential information sections of this Response, the Joint Applicants each invoke and incorporate by reference the Rule 12 Motions previously submitted in this proceeding. MIDT traffic data responsive to item 25 is provided in electronic format on compact disk.

Responses to the Department's clarification questions are set forth below. Accordingly, the record is now complete, and the Joint Applicants urge the Department to immediately issue a Scheduling Order establishing the due date for answers and to proceed with prompt approval of the Joint Application.

#### Clarification Questions

8. **Please explain (i) what relationship the Joint Applicants will have with Korean Air Lines (KE) if the Joint Application is approved, and (ii) whether the exclusion of KE from the application will create an "immunity gap" with respect to KE, comparable to that which Joint Applicants contend currently exists between NW/KL, on the one hand, and DL/AF/AZ/OK, on the other hand.**

(i) Delta, Air France, Alitalia and CSA have an immunized alliance relationship with KE that has been reviewed and approved by the Department. See Order 2002-6-18. Northwest is not part of that alliance, nor is KE a party to this Joint Application. Because there is no immunity covering both Northwest and KE, the two alliances will be managed separately. Delta, Air France, Alitalia and CSA will continue to engage in immunized international alliance activities with KE. Northwest will be excluded from discussions or coordinated activities with KE that require antitrust immunity. Similarly, KE will be excluded from discussions or coordinated activities with Northwest that require antitrust immunity.

(ii) The exclusion of KE from this application does not create the potential for an immunity gap comparable to that resulting from the merger of Air France and KLM. Air France and KLM have already completed a merger transaction to form Air France-KLM, an airline holding company that is the parent of two operating airlines. There has been no equivalent corporate merger involving KE. Thus, the common ownership interest and the corporate decision-making structure that results from the Air France-KLM merger, which creates the current gap in immunity between the existing SkyTeam ATI and Northwest/KLM immunized alliances, has no equivalent with respect to KE.

Due to the existing and fully integrated Northwest/KLM transatlantic alliance – and the need for Air France-KLM to be able to act in concert when dealing with its immunized alliance partners – a further grant of immunity is necessary to bridge the two immunized alliances and preserve the benefits of the existing SkyTeam ATI and Northwest/KLM alliances.

By contrast, KE is not part of a corporate combination with any SkyTeam or Northwest/KLM alliance member. Furthermore, no transpacific services are operated by any of the European alliance partners, nor are any transatlantic services operated by KE. Delta will not coordinate any competitively sensitive activities with both Northwest and KE in any market where those carriers compete with each other. Accordingly, competitively sensitive commercial activities involving KE on the one hand and Northwest on the other hand will be

completely segregated without losing the benefits of the existing antitrust immunized alliances.

**9. Please explain (i) what relationship the Joint Applicants will have with Continental Airlines (CO) if the Joint Application is approved, (ii) what discussions or communications have occurred with CO concerning its inclusion in or exclusion from the Application for Antitrust Immunity, and (iii) whether the Joint Applicants contemplate a separate application for antitrust immunity that would integrate Continental into the Expanded SkyTeam ATI Alliance, and, if so, when such an application would be forthcoming.**

(i) If the Joint Application is approved, the Joint Applicants will have the same relationship with Continental as they have today. Delta, Northwest and Continental have a non-immunized domestic marketing alliance, which is subject to terms and conditions agreed to by those carriers, the Department, and the Department of Justice. Continental has joined the SkyTeam Alliance, but is a non-immunized alliance member that will only engage in non-competitively sensitive activities with other SkyTeam members, such as arms-length codesharing, frequent flyer program participation and reciprocal lounge access.

In short, the Joint Applicants will continue to compete with Continental, just as they do today, and will not coordinate with Continental on competitively sensitive matters.

(ii) Northwest had several discussions with Continental regarding the Joint Application, including a meeting in Houston on April 5, 2004. In such discussions, Northwest explained its view that the Air France-KLM merger transaction necessitated an application for antitrust immunity to ensure that the benefits of the existing antitrust immune alliances were not jeopardized. After a

series of telephone calls over the course of the following month, Continental indicated it would not oppose the parties proceeding with the Joint Application so long as the Application did not interfere with Continental's pursuit of codesharing approval with Air France, and with the understanding that a subsequent application for antitrust immunity to include Continental would be submitted when and if the carriers had an agreement to proceed with such an application.

During the same period of time, Air France and Alitalia also had discussions with Continental. Air France requested in a conversation with David Grizzle, Continental's Senior Vice President-Marketing Strategy and Corporate Development, that Continental set forth its views in writing on whether the filing for a six-carrier ATI application made sense to Continental, and if not, why not. In response, David Grizzle prepared the April 26, 2004, letter, produced at Bates No. DL 00411-413.

Air France and Alitalia had a further meeting with Continental on May 10, 2004. At this meeting, Continental agreed that it would not object if the parties proceeded with their six-carrier immunity application at this time, with the understanding that a subsequent seven-carrier immunity application would be submitted to the Department when and if the seven carriers agreed to pursue such an immunity application. It was also agreed that Air France and Continental, and Alitalia and Continental, would complete promptly their respective negotiations of codeshare agreements, which would be submitted to the Department for approval

in advance of the instant immunity application. Air France also committed to seek the necessary consents from Delta and Northwest for such codesharing.

(iii) Any decision by the Joint Applicants and Continental to include Continental in the Expanded SkyTeam ATI Alliance would require a new and separate application for antitrust immunity. Although the Joint Applicants contemplate that Continental may be included in a future application for an expanded immunized SkyTeam alliance, no such decision has been made, and the Joint Applicants cannot predict when or if such a decision would be made. If and when such a new application is filed, the Department and interested persons will have the opportunity fully to evaluate the competitive effects and consumer benefits of a proposed expanded alliance in the context of then current (and potentially substantially changed) market conditions.

10. **How would Your analyses of the competitive impact of the transaction change (relative to the existing base case) if CO were included in the Application for Antitrust Immunity (Exhibits JA-1 to JA-10)? (Please describe the methodology and disclose all assumptions and data sources used in the revised analysis whereby CO is included.)**

The Joint Applicants respectfully submit that this is not a proper inquiry for the Department to undertake in connection with its review of the Joint Application. Continental is not a party to the Joint Application. Therefore, consideration of the competitive impact of an alliance that included Continental would be hypothetical, at best, and procedurally improper, at worst. If there comes a time when Continental seeks antitrust immunity with the six Joint Applicants, the carriers will have to file an application with the Department, and

the Department will have the opportunity to consider that application in the context of the market conditions prevailing at the time. Prejudging that outcome would prejudice the carriers, especially Continental – which is not a party to this proceeding.

Recent developments suggest that it is not only possible, but probable, that market conditions will change materially in the near future. One such development is emerging new low fare entry in the transatlantic. Skylink Airways, for example, has applied to the Department to serve eight transatlantic markets, including BWI/IAD to Austria, Belgium, Germany, France, Italy and the Netherlands. Another potential low fare entrant, Atlantic Express (which is currently in the certification process) plans to operate in B757 aircraft in the transatlantic. Blackstar Airlines sought authorization to serve points between the U.S. and Germany and France. Although Blackstar has temporarily withdrawn its application to obtain financing, it has been reported that Blackstar expects to secure financing this year and reapply. Other existing U.S. and European carriers are plainly positioned to enter the transatlantic and could readily do so if circumstances warranted. JetBlue, for example, has its main base of operations at JFK and already provides international services to the Caribbean. There is also the potential for new low fare entry through code sharing, such as the recently-approved application of America West and Royal Jordanian Airlines for antitrust immunity.

In these circumstances, an inquiry regarding the possibility of Continental joining the immunized alliance in the future lacks any predictive utility. It is also inconsistent with the Department's precedent. The Department has previously rejected efforts to "add" carriers to proceedings involving requests for antitrust immunity. Thus, when the Department considered Continental's impact on the proposed Northwest/KLM/Alitalia alliance in 1999, the Department said:

Continental's relationship with any of the applicants in this case is not decisional because there is no linkage between Continental and the new alliance with respect to the services we are proposing to authorize today. Continental is not a party to the proposed alliance; there is no evidence that it has reached any agreement regarding any future participation; and we have no reason to doubt its assertion that . . . [it] will compete with the proposed alliance.

Order 99-11-20 at 14.

The Department appropriately determined, as it should here, that "to ensure that we are in the position to evaluate the relationship between Continental and the alliance partners, we will require them to file for prior approval of any agreement which alters Continental's existing relationships with any of the alliance partners, if those changes affect the authority that we are proposing to grant." *Id.*

Nonetheless, the Joint Applicants have provided such analysis below. However, in accordance with clear Department precedent, this speculative analysis of Continental's possible future inclusion "is not decisional" in this case. *Id.*

The following exhibits would change if Continental ("CO") were included in the Application for Antitrust Immunity:

In JA-2, the total market size (represented by bookings) served by SkyTeam + KL/NW + CO would be 38.6 million, and the total market size (also represented by bookings) that would be served by SkyTeam + KL/NW + CO and not fewer than 3 competitors due to ATI would be 36.2 million.

In JA-4, SkyTeam ATI + KL/NW + CO would account for 32%, Star ATI would account for 20%, BA would account for 13%, AA ATI would account for 11%, and the remaining Independents would account for 24% of transatlantic traffic.

In JA-5, SkyTeam + KL/NW + CO would overlap on ten nonstop routes, based on 2004 OAG schedules. The additional nonstop routes would be Amsterdam-Houston, Brussels-New York, Frankfurt-New York, Madrid-New York, Paris-Houston, Milan-New York, Paris-New York, and Rome-New York.

In JA-6, the SkyTeam + KL/NW + CO share for Italy will be 62.3%, for the Netherlands will be 59.7%, for France will be 55%, and for the Czech Republic will be 51.9%.

In JA-7, the grant of antitrust immunity to SkyTeam + KL/NW + CO would not reduce below 3 the number of competitors for 94% of passengers in transatlantic city-pair markets. Only 57 of the city-pair overlap markets have

above 5,000 bookings per year, and 37 of these markets have fewer than 10,000 bookings per year.

In JA-8, 99.7% of transatlantic passengers with three or more competitive options today will still have three or more competitive options when competition provided by all carriers is included – not just carriers with more than 5% of bookings.

Except as otherwise noted, the same data and assumptions that were used in the preparation of the JA Exhibits for the Joint Application were used in responding to this Clarification Question.

11. **Please explain why antitrust immunity is necessary for the Parties to proceed with the Alliance Agreements when DL, NW, and CO operate a domestic marketing alliance without such antitrust immunity protection.**

The Alliance Agreements contemplate a fundamentally different type of alliance than the domestic Delta/Northwest/Continental marketing alliance. Because the Delta/Northwest/Continental domestic marketing alliance does not have antitrust immunity, the participants in that alliance remain vigorous domestic competitors, and the alliance is expressly designed and conditioned to ensure that the participants will continue to compete against one another just as they did before the alliance was allowed to proceed. The carriers thus do not coordinate on fares, route planning, capacity, frequency or on other competitively sensitive matters. Rather, cooperation among the carriers is limited to that necessary to achieve codesharing, reciprocal lounge access, reciprocal frequent flyer miles

accumulation and redemption and to create for codeshare passengers as seamless a travel experience as possible within the constraints imposed by the antitrust laws.

By contrast, the members of the SkyTeam and Northwest/KLM ATIs currently coordinate across a range of competitively sensitive matters within their immunized alliances and, as explained in the Joint Application, plan to extend that cooperation within an expanded SkyTeam alliance once immunity is achieved.

While the benefits of domestic codesharing in the Delta/Northwest/Continental marketing alliance to the carriers and consumers are substantial, for reasons more fully explained in the Joint Application, they are dwarfed by the benefits that can be achieved in an international antitrust immunized alliance, and even more by the benefits that can be achieved in an immunized common bottom line alliance like the Northwest/KLM Joint Venture. The Department has recognized as much in its approval of prior immunized alliances (each of which also involved reciprocal codesharing), including in its approval of antitrust immunity for the SkyTeam ATI Carriers (“Our recent evaluation of international alliances shows that they stimulate traffic ... and thereby increase competition and service options in the overall international market and increase overall opportunities for the traveling public and the aviation industry.” Order 2002-6-18 at 7) and for the Northwest/KLM alliance (Order 93-1-11). With separate grants of antitrust immunity, SkyTeam and Northwest/KLM are now producing the very substantial

consumer benefits that the Department recognized could not be produced by arms-length codesharing alone.

It is to both to *preserve* these benefits – greatly in excess of the benefits being achieved by the non-immunized domestic Delta/Northwest/Continental marketing alliance – and to *attain* even greater benefits through the ability to coordinate in an expanded SkyTeam alliance that the Joint Applicants have filed the instant immunity application. As explained in the answer to Question 8, Air France and KLM have merged, and approval of the Joint Application is needed to bridge the current gap in immunity between the Northwest/KLM and SkyTeam ATI alliances and to preserve and enhance the benefits secured for the traveling public under the two existing ATIs. *See also* Responses to Clarification Questions 12, 13 and 18.

**12. Please explain (i) whether and why approval of the Application for Antitrust Immunity is necessary for the *development* of a comprehensive revenue/profit sharing arrangement between or among the Parties, (ii) whether and why approval is necessary for the *implementation* of such an arrangement, and (iii) whether any or all of the Joint Applicants have plans to implement such an arrangement, and, if so, what form such an arrangement would take and when it would be implemented.**

(i) The Joint Applicants believe that antitrust immunity is necessary for development of a comprehensive revenue/profit sharing arrangement among the six Parties. In order for the Parties to develop such an arrangement, they will have to be able to exchange and discuss current and future competitively sensitive information – such as route profitability data, market expansion plans, assumptions about future fares, and anticipated competitive responses by other

carriers -- that relates to future developments in the marketplace. They will also have to explore and negotiate various potential formulations of such an arrangement. The information sharing necessary to the negotiation is precisely the kind that can present problems under the antitrust laws and for which the Parties need antitrust immunity in order to proceed.

Furthermore, as was the case in the NW/KLM Joint Venture, it is likely that the carriers will proceed in incremental steps toward comprehensive revenue/profit sharing. Such steps are likely to include limited revenue sharing on particular trunk routes, or bilateral or multilateral arrangements that do not involve all of the Joint Applicants. As the carriers gain experience with limited profit sharing and confidence in their ability to work through the issues that must be resolved in order to achieve a common bottom line, is it likely that they will be in a position to negotiate a comprehensive revenue/profit sharing agreement. These incremental steps toward an comprehensive agreement require antitrust immunity to negotiate and implement.

The antitrust laws do not prohibit all exchanges of information between and among competitors. Information exchanges can be procompetitive (such as where they make a market more transparent) or competitively sensitive (such as where they facilitate coordinated conduct by competitors with respect to price or output.)<sup>1</sup> In distinguishing between the former and the latter, courts have

---

<sup>1</sup> See H. Hovenkamp, XIII Antitrust Law ¶ 2111b-c (2d ed. 2005).

indicated that information exchanges that are made available to buyers and sellers and pertain to past, rather than future, conduct are less likely to present such concerns. By contrast, such exchanges that involve only sellers of a product or service and address likely future pricing and output decisions are potentially quite problematic, raising the prospect of not only civil liability but also criminal prosecution.<sup>2</sup>

Here, of course, the Parties will have to discuss and agree upon future pricing and capacity in order to develop a sensible revenue/profit sharing agreement that they believe will produce substantial public benefits. They should not be forced to choose between forgoing such efforts or subjecting themselves to potential after-the-fact antitrust exposure. The only way in which they can proceed is with antitrust immunity.

(ii) The Joint Applicants believe that antitrust immunity is necessary for the implementation of such an arrangement for reasons set forth in the Joint Application and in responses to other clarification questions posed by the Department.

In the Joint Application, the Parties described the nature of the consumer benefits that they envision providing (Joint Application at 29-32), the reasons why those benefits cannot be obtained through unimmunized codesharing (Joint Application at 32-38), and why they cannot pursue them without antitrust

---

<sup>2</sup> See, e.g., *United States v. Container Corp. of America*, 393 U.S. 333 (1969); *United States v. United States Gypsum Co.*, 438 U.S. 422 (1978).

immunity because of potential antitrust exposure (Joint Application at 38-45). In the response to clarification question 18, the Joint Applications set forth in greater detail the extent and nature of consumer benefits that cannot be achieved without antitrust immunity.

Agreements between competitors to share revenues or profits can raise antitrust concerns. Such arrangements can be challenged under the per se rule or the rule of reason.<sup>3</sup> The antitrust concerns expressed by the Joint Applicants are neither novel nor unprecedented. In numerous proceedings involving requests for antitrust immunity, applicants have made similar arguments in support of antitrust immunity, and the Department has expressly relied upon such antitrust concerns in granting those requests. *See, e.g.*, Order 96-5-26 at 26; Order 2001-12-18 at 18 (“the record suggests that the Joint Applicants could be subject to extensive and burdensome antitrust litigation if we did not grant their request. The record also persuades us that they will not proceed without it.”). Antitrust immunity is thus necessary for the implementation of a revenue/profit sharing agreement.

(iii) The Joint Applicants want to begin the process that would be necessary to develop and implement a revenue/profit sharing agreement. This will involve a series of steps and appropriate due diligence by each of the participating carriers, in order to develop a comprehensive and meaningful multi-carrier revenue/profit sharing agreement. Without antitrust immunity, this

---

<sup>3</sup> *See, e.g., Dagher v. Saudi Refining Inc.*, 369 F.3d 1108 (9th Cir. 2004).

process cannot move forward, because the carriers are unwilling to exchange competitively sensitive information and expose themselves to potential antitrust risk.

**13. Please discuss the extent to which the following are contingent on the establishment of a comprehensive revenue/profit sharing arrangement between or among the Parties: (i) consumer benefits of this transaction, (ii) additional codesharing beyond that contemplated in the codeshare agreements submitted to DOT as part of the Joint Application for Statements of Authorization, and (iii) introduction of any additional capacity identified in Your response to question 17 below.**

(i) Many of the potential consumer benefits of this transaction will be realized by the grant of antitrust immunity to the expanded SkyTeam alliance. First, antitrust immunity will preserve the existing substantial benefits produced by the SkyTeam and Northwest/KLM alliances, by bridging the two antitrust immunized alliances, facilitating continued cooperation within the existing alliances, and closing the current gap in immunity. Second, antitrust immunity will permit enhanced cooperation among the members of an expanded SkyTeam alliance generating consumer benefits beyond those produced by the existing alliances. Additional consumer benefits will be realized as the Joint Applicants move toward further integration and revenue/profit sharing arrangements. Revenue and profit sharing creates incentives for the carriers to maximize the benefits to consumers of the alliance as a whole, rather than to maximize each carrier's individual bottom line. A common bottom line joint venture, such as Northwest/KLM, allows joint venture decision-making to approach that of a

single firm.<sup>4</sup> And, as the Northwest/KLM experience demonstrates, such decision-making leads to expanded output, greater efficiency in scheduling and planning, and reduced costs of operation – all of which translate into increased consumer benefit.

(ii) The limited codesharing contemplated by the Codeshare Agreements aptly illustrates the need for antitrust immunity to realize the consumer benefits that can be achieved by comprehensive codesharing. The limited codesharing provided for reflects the interplay of individual carrier incentives that characterize non-immunized arms-length relationships. In such non-immunized relationships, individual carriers seek to maximize the number of passengers they carry. They therefore are often unwilling to incur the risks of dilution or diversion or to accept the disproportionate allocation of costs and benefits that flow from more expansive codesharing even though such comprehensive codesharing is to the benefit of all carriers combined and maximizes benefits to consumers. Moreover, they cannot negotiate the necessary trade-offs without significant antitrust risk. Antitrust immunity will enable the Joint Applicants to engage in more extensive reciprocal codesharing across their networks as they are able to discuss and make trade-offs that otherwise could present antitrust risks, including through the formation of “mini-JVs” to develop new routes by sharing the costs and benefits of codesharing behind and beyond those routes. As the Joint Applicants move

---

<sup>4</sup> Delta and Air France submitted last fall a Financial Settlement Mechanism Agreement (“FSM”) as an implementing agreement to their alliance.

toward closer integration and revenue/profit sharing, the disincentives to comprehensive codesharing will further diminish (and eventually disappear) as each carrier will have incentives to maximize the benefits to the expanded alliance as a whole.

(iii) The introduction of new capacity identified in response to Question 17 is dependent on obtaining antitrust immunity. For reasons discussed above, absent antitrust immunity the carriers will be unwilling to incur the antitrust risks from cooperating to discuss and agree on competitively sensitive matters that would allow them to optimize capacity, frequency, pricing and traffic flows on potential new routes. Further, the increased codesharing that will be made possible by antitrust immunity and the ability to flow passengers over the most efficient and convenient routings will increase traffic flows, providing the economic incentives for further expansion of such conduits between domestic and foreign gateways. As the Joint Applicants move toward greater integration and revenue/profit sharing, they expect that they will be able further to optimize and expand an increasingly integrated network.

14. **Please discuss how, absent a revenue/profit sharing arrangement, the Joint Applicants will manage conflicting interests with respect to capacity allocation, scheduling, pricing, revenue and inventory management (distinguishing between local nonstop and flow traffic), and sales and marketing strategies.**

If the Joint Applicants are granted antitrust immunity, and absent a revenue/profit sharing agreement, the parties would be able to address and resolve conflicting interests with respect to capacity allocation, scheduling,

pricing, revenue and inventory management, albeit less efficiently than with a revenue/profit sharing agreement. Revenue/profit sharing agreements tend to eliminate areas of dispute and thereby either eliminate conflicts or make it easier to resolve conflicts. The Joint Applicants intend to progress towards a revenue/profit sharing agreement that will reduce inherent conflicts, enhance efficiencies in dealing with disputes, and encourage cooperative activities beneficial to the carriers and to consumers.

The SkyTeam antitrust immunized alliance partners currently operate in an environment with immunity, but without a comprehensive revenue/profit sharing agreement. The Global Airline Alliance Agreement among the SkyTeam alliance partners sets forth principles and objectives of the alliance and the mechanism for resolving disputes. See Bates No. DLKE ATI302 0227-280 (OST-02-1842). In addition, Delta, Air France, Alitalia and CSA have entered into a Codes of Conduct Agreement Bates No. 02570-2582. That agreement sets forth specific goals, objectives and procedures with respect to the coordination of the respective alliance matters.

If conflicting interests arise, the parties work to resolve those conflicts through consensus negotiation at the working staff level. If resolution is not achieved, the issue might go to more senior management to resolve. In the end, the Alliance Agreement contains a formal dispute resolution mechanism.

Revenue and/or profit-sharing agreements provide an agreed framework for sharing the economic benefits of the alliance and for allocating each member's share of financial contributions and benefits, thus providing each carrier an incentive to maximize the efficiency of the joint system as a whole rather than its own system independently. As a result, revenue/profit-sharing agreements eliminate many of the disputes that create the need for formal dispute resolution.

In sum, while Delta/Air France/Alitalia/CSA have managed disputes arising out of conflicting interests through negotiations without a full revenue/profit sharing agreement, decisions in such a setting are made significantly less efficiently than they would be if the carriers shared a common bottom line and opportunities for beneficial cooperation are lost that would not be forgone if the carriers' incentives were more fully aligned. As stated in the Joint Application, the benefits of greater integration and a common bottom line are fully recognized, and the Joint Applicants plan to move in that direction. (Delta and Air France, for instance, submitted last fall a Financial Settlement Mechanism Agreement as an implementing agreement to their alliance.) The addition of Northwest/KLM as a member of the Expanded SkyTeam ATI Alliance, providing the other members with the benefit of their experience as successful airline joint ventures, will enhance the other Applicants' efforts to achieve deeper and more efficient alliance integration.

15. Please describe (i) what criteria will be used to determine the markets in which You will codeshare, (ii) whether the four digit flight number limitation and number of potential

**codesharing partners involved will limit the Joint Applicants' potential codesharing and, if so, how the Joint Applicants will allocate flight numbers.**

(i) Additional codesharing between the Joint Applicants beyond that detailed in the codeshare agreements filed with the Joint Application for Statements of Authorization dated September 24, 2004, depends on receiving joint antitrust immunity. Codeshare criteria under antitrust immunity have not yet been established, but the Joint Applicants hope to engage in as much codesharing as is technically feasible under antitrust immunity, to maximize new service offerings.

(ii) The four-digit flight number limitation will not significantly limit the consumer benefits from potential codesharing between and among the Joint Applicants. At present, none of the Joint Applicants' flight number usage approaches the maximum of 9,999 four-digit flight numbers. In addition, some of the Joint Applicants have individually developed tools to significantly improve efficiency in the usage of codeshare and operated flight numbers, with minimal or no impact to consumers on the flight segments operated or marketed.

Maximizing the usage of through-flight numbers is one such method to improve flight number efficiency.

- 16. Please provide the traffic and revenue effects on each of the Joint Applicants and on other airlines/alliances of expanded cooperation between the Joint Applicants, for the first year after DOT approval, under each of the following scenarios:**

**DOT approves Codeshare Authority but does not approve Your Application for Antitrust Immunity**

**DOT approves Codeshare Authority and Your Application for Antitrust Immunity but the Joint Applicants do not have a revenue/profit sharing arrangement in place**

**DOT approves Codeshare Authority and Your Application for Antitrust Immunity and the Joint Applicants have a comprehensive revenue/profit sharing arrangement in place.**

**Under each scenario, identify the extent to which the traffic and revenue for the Joint Applicants will be stimulated versus diverted from other carriers/alliances. Under each scenario, please describe the methodology and disclose all assumptions (including assumptions about competitive responses) and data sources used to produce estimates. Under scenarios (i) and (ii) identify all routes selected for codesharing and modeled by the Joint Applicants. Under scenario (iii), address the impact, if any, that flight number scarcity played in the selection of markets for the codesharing modeled.**

*[Confidential Section]*

**REDACTED**

---

REDACTED

---

**REDACTED**

---

REDACTED

## REDACTED

*[End Confidential Section]*

17. Please explain what changes You would make to Your U.S.-International capacity (relative to Your summer and winter 2004 schedules, in both existing markets and new markets) within the first two years after DOT approval if (a) You received Codeshare Authority but did not receive ATI and (b) You received both Codeshare Authority and ATI. In answering both (a) and (b), provide detail at the city-pair market level and identify the relevant carriers, seats per departure, and frequencies.

None of the Joint Applicants has finalized plans for adding new routes to its system or for the addition of capacity to existing routes for the two years after Department approval of ATI, much less made determinations concerning frequencies or the aircraft gauge that would be employed on any such new or existing routes.<sup>9</sup> Such consideration as has been given to adding new routes or capacity has been based on the assumption that antitrust immunity will be granted so that carriers will be able to discuss and agree on competitively sensitive matters that would allow them to optimize capacity, frequency, pricing and traffic flows on such new routes without incurring unacceptable antitrust risk. Further, as discussed above, antitrust immunity will permit comprehensive reciprocal

---

<sup>9</sup> Carriers are constantly making changes to their schedules. For example, Delta intends to introduce Atlanta-Moscow service this summer, and Air France will fly Detroit-Paris. The Joint Applicants do not know whether antitrust immunity will be granted before or after the effective dates for those services.

codesharing, providing increased traffic flows and creating the economic incentives for further expansion of service among the Joint Applicants' networks.

In fact, transatlantic services offered today by one or more of the Joint Applicants could be *reduced* even if codeshare authority is granted – but without the necessary antitrust immunity. This is because, absent immunity, carriers are less likely to introduce comprehensive reciprocal codesharing and are less likely to dedicate substantial capacity to codeshare service marketed by their alliance partners. For example, KLM's Atlanta-Amsterdam service, operated as part of the Northwest/KLM Joint Venture, may be vulnerable to cancellation. KLM cancelled that service in 2001 but recently reinstated service in the expectation that cooperation with Delta would generate sufficient traffic to make the flight profitable. Without codesharing authority and antitrust immunity, Delta and KLM will not be able to explore freely various options – including schedule coordination and pricing initiatives – that would best allow continuation of this service. *See also* Responses to Clarification Questions 16 and 18.

**Individual Carrier Plans-**

**[Confidential Section]**

**REDACTED**

**REDACTED**

REDACTED

REDACTED

REDACTED

*[End Confidential Section]*

18. Please explain specifically which consumer benefits that will result from the Alliance Agreements cannot be achieved without antitrust immunity. For each type of consumer benefit noted, please describe how the Joint Applicants are currently cooperating in that area, and how that cooperation would change if You were granted ATI.

In the Joint Application, the Joint Applicants identified various kinds of consumer benefits that would result from their alliance. See Joint Application at 29-32. While some kinds of benefits are achievable to a limited degree without antitrust immunity, they are achievable on a much more significant scale only if the Joint Applicants have antitrust immunity to negotiate and implement the agreements that are necessary to maximize codesharing (*see* section 1, *infra*), and still other types of benefits are available only if the Joint Applicants have antitrust immunity to agree upon various schedule and service adjustments necessary to make the alliance work efficiently (*see* section 2, *infra*). In both instances, the ability to maximize consumer benefits depends upon the carriers being able to reach agreements that benefit the alliance as a whole, even if individual carriers have to make sacrifices that they would not if they were acting individually. To do this, they must have antitrust immunity (*see* section 3, *infra*).

(i) The benefits from an airline alliance flow primarily from combining the route networks of the participating carriers. With codesharing, through-route baggage check-in, and reciprocal frequent flyer programs, carriers participating in an alliance can offer passengers many of the conveniences and benefits traditionally associated with online service and can offer more flights across a larger network. The magnitude of those benefits depends, of course, on the size of the city pairs and the number of flights on which the alliance carriers cooperate.

The city pairs that can benefit from an alliance can be divided into two broad categories. First, there are city pairs that none of the alliance's carriers presently serves on an online basis but that alliance carriers could serve by codesharing. In the present matter, the Joint Applicants believe there are approximately 8,700 such city pairs. Joint Application at 30. Second, there are city pairs that one or more of the alliance carriers presently serves online but that the alliance carriers could serve more conveniently and/or more frequently by codesharing. In the present matter, the Joint Applicants estimate that over 37 million transatlantic passengers travel in city pairs that could potentially benefit in terms of convenience and frequency enhancements from the alliance they have proposed. Joint Application at 30-31.

The realization of those benefits depends upon alliance carriers reaching agreements to codeshare on a significant number of city pairs and to operate their

flights in the way best designed to attract passengers to the alliance carriers.

However, there are substantial impediments to reaching such agreements absent antitrust immunity. Without such immunity, carriers have conflicting incentives that are difficult to reconcile. Each carrier would like to enter into codesharing agreements that increase its own traffic, but each carrier is reluctant to enter into codesharing agreements that risk diversion of traffic to other carriers. As a result, such agreements tend to be quid-pro-quo trades that proceed incrementally and slowly, as is evidenced by the codesharing agreements that have been filed by the Joint Applicants in connection with this very proceeding. Those agreements provide for codesharing behind gateways only to so-called unique points plus a limited number of beyond points.<sup>10</sup>

These impediments to broad codesharing grow exponentially as the number of carriers to an alliance increases. Although in theory the participation of more than two carriers should increase the potential for consumer benefits by expanding the scope of the network, the need for multiple carriers to reach a consensus greatly complicates the negotiation process. As the number of participants increases, so, too, does the difficulty in reaching a consensus. Thus, in the

---

<sup>10</sup> In addition to achieving broader agreement on the number of codeshare points, antitrust immunity allows the carriers to discuss and agree on common service enhancements, eliminating seams that would otherwise exist in pure codesharing relationships and improving the quality of the passenger's travel experience. One such jointly adopted service innovation that would not have been possible without antitrust immunity is the single NW/KL world business class product.

context of a six-carrier alliance, there is ironically both the prospect of greater consumer benefits and yet greater difficulty in achieving them.

With antitrust immunity, carriers can more readily overcome the obstacles that would otherwise prevent them from reaching agreements that provide maximum customer benefits. The use of pooling and/or profit-sharing arrangements allows alliance members to focus on the overall benefits that they can collectively offer to the marketplace, even if achieving them requires each of the carriers to take some actions or make some concessions that they would be unwilling to do in a conventional codesharing agreement. Furthermore, with antitrust immunity carriers can agree upon rates and promotions to stimulate travel on the alliance carriers. Thus, while it is theoretically possible for carriers to reach codesharing agreements even without antitrust immunity, they are much more likely to be able to reach broader codesharing agreements, especially in the context of a six-carrier alliance, with antitrust immunity.

(ii) In addition, there are other kinds of consumer benefits that are dependent upon the ability of carriers to work together to make scheduling and capacity decisions that maximize service offerings to the public. Here again, the challenge is to create an environment in which the alliance carriers act in the broad interest of the alliance as a whole, even if that means each carrier has to accept some decisions that it might not have made if it had been acting alone.

As described in the Joint Application, the Joint Applicants want to be able to agree explicitly upon matters relating to international routes, including schedules and capacity additions. Joint Application at 33. There will be instances, for example, in which two alliance carriers serve the same city pair with similarly-timed flights because each carrier has selected the time of day that the greatest number of passengers prefers. The carriers may recognize that it would be most desirable – for both the carriers and passengers -- to spread out the flights so that they could connect with two different banks of flights rather than one, because doing so would provide passengers with a greater array of travel timing options. Yet, neither of the carriers wants to move to the less desirable departure time, even though collectively they – and passengers – will be better off if one did so.

The same can hold true with respect to capacity additions. There are city pairs that have local traffic that is too thin to sustain nonstop service but that might be viable with feed traffic that a codesharing agreement could generate. Presumably, each of the alliance carriers would be interested in providing the nonstop service if the other alliance carriers would provide feed traffic, but none of them would want to provide the feed traffic if doing so would reduce the potential viability of providing their own nonstop service to the same geographic

area. If a stalemate results, consumers suffer because the additional nonstop service will not be provided.<sup>11</sup>

(iii) Thus, the best way to encourage alliance carriers to make decisions in the interests of the alliance as a whole, is to allow them to enter into an agreement to share the revenues and/or to divide the profits. Such agreements can make the alliance carriers indifferent as to who changes its schedule or who adds the nonstop flight. Instead, it encourages them to focus on total consumer benefits. Indeed, the ability of such agreements to increase traffic and service is demonstrated by success of the Northwest-KLM Joint Venture, where the "common bottom line" concept has allowed the carriers to focus on maximizing the international operations of the carriers as a group, rather than on individual carrier performance.

---

<sup>11</sup> Economists have long recognized this phenomenon, which was noted as early as 1929 in an article by Harold Hotelling. He describes two sellers of a commodity located along a hypothetical Main Street in a town. As long as the sellers are separately owned and operated, each seller will tend to position its store close to the center of the town in order to be closest to the greatest number of customers. Yet, there will be circumstances in which moving the stores apart and positioning them nearer to the ends of Main Street will increase total sales because they will be more accessible to more buyers. Since each seller thinks it will make itself worse off by moving, "the tendency is not to become distributed in the socially optimum manner but to cluster unduly." *See* H. Hotelling, "Stability in Competition," *The Economic Journal* 39, 53 (March 1929). Thus, the inability of the two sellers to negotiate and agree upon where they will place their respective stores and how they will share their combined revenues reduces total sales and reduces the benefits to buyers. Absent market power concerns – that is, assuming there are other sellers of the commodity – consumers suffer from the inability of the two sellers to negotiate and agree upon how to divide their revenues and profits so that they will place their stores in locations that will maximize their combined output.

Absent antitrust immunity, however, the Joint Applicants cannot be confident that such agreements would not be challenged under the antitrust laws. *See* Joint Application at 38-43. Certainly it could be argued that an agreement to share revenues or profits in the context of a carrier alliance should be reviewed under the rule of reason and upheld as a reasonable ancillary restraint to an otherwise legitimate joint venture. But the difficulty is that courts differ in their interpretation and application of the antitrust laws, and the consequences of misprediction can be financially staggering. Just recently, a court of appeals held that an agreement among joint venture partners to set a common price for two gasoline brands sold by the venture is subject to the *per se* standard, even though the Federal Trade Commission and several state Attorneys General had reviewed the formation of the joint venture and permitted it to proceed (subject to certain conditions) and the plaintiffs made no attempt to show that the defendants had market power. *Dagher v. Saudi Refining Inc.*, 369 F.3d 1108 (9<sup>th</sup> Cir. 2004).

It is for this reason that the six Joint Applicants have not yet even begun to negotiate, let alone enter into, revenue or profit-sharing agreements that would facilitate broad codesharing, schedule changes, and capacity additions, that they believe would provide maximum benefits to consumers. *See* Response to Clarification Question 12. With antitrust immunity, they would be free to do so.

19. Please explain (i) why failure to obtain antitrust immunity at this time puts the existing NW/KL and Sky Team Immunized alliances at risk, and (ii) whether that risk is mitigated by (a) the long-term domestic marketing alliance between DL and NW, (b) AF's commitment to managing KL as a separate airline and growing its Amsterdam hub

for five years, and (c) the likelihood that a carrier expelled from the alliance would join a competing alliance.

(i) Air France-KLM spans two separate antitrust immunized partnerships. The current gap in immunity resulting from the merger of Air France and KLM creates a need for antitrust immunity to bridge the two alliances, to preserve the benefits of the existing ATI alliances, and to obtain the benefits of greater coordination in an expanded alliance. While Air France and KLM will continue to operate as separate airlines, they also plan to continue the integration of their operations. With separate antitrust immunities, Air France and KLM today do not codeshare or otherwise coordinate their transatlantic operations, even though the efficiencies that could be achieved from such integration are evident.

The current gap in immunity impairs the ability the existing immunized alliances to function optimally. As Air France-KLM continue to integrate operations to achieve the merger-related efficiencies expected from the transaction, it will be essential for Delta and Northwest to be included in international route and marketing planning together with Air France-KLM. Without immunity, Delta will have to be kept in the dark about competitive initiatives Air France-KLM's KLM carrier plans with Northwest, and vice-versa. This is not viable as anything but an interim stop-gap measure.

Moreover, as discussed above, because one of the U.S. carriers could well find itself in a situation where it is unable to collaborate fully in alliance activities,

or would withdraw from its alliance, even the present level of coordination that occurs separately within each of the existing alliances could be threatened -- along with the concomitant substantial benefits to the U.S. carrier and the traveling public. Failure to approve the Joint Application therefore not only likely will prevent realization of the benefits of enhanced coordination in an expanded alliance, but could well cause the public and one of the U.S. carriers to lose benefits under its existing alliance.

(ii)(a) The risk discussed above is not mitigated by the Delta/Northwest/Continental alliance. The Delta/Northwest/Continental domestic marketing alliance has no bearing whatsoever on the need for antitrust immunity for Delta and Northwest to participate in an expanded alliance with Air France-KLM. As explained in response to Question 11, the domestic marketing alliance does not involve any activities requiring antitrust immunity. If the inability to effectively participate in an immunized international alliance required one U.S. carrier or the other to lose benefits under its international alliance relationship, those lost benefits would be entirely foregone and would not be made up by the domestic marketing arrangement. One has no bearing on the other.

(ii)(b) The commitment of Air France-KLM to manage KLM as a separate airline and to maintain the Amsterdam hub for a five year period does not mitigate the need for immunity in this proceeding.

Air France and KLM have merged, and they will continue to integrate to achieve the economic benefits of that combination. Although there will be two separate airline entities, those entities will have a common bottom line under Air France-KLM Holdings and they will be commonly-managed under the Strategic Management Committee structure provided for under the Framework Agreement to the extent the law permits. As the pace of integration intensifies, the difficulties of avoiding antitrust risk can only increase.

In the absence of antitrust immunity for the six carriers, Air France-KLM will have to forego certain collaborative activities either with Northwest or with Delta, in order to avoid third-party antitrust claims. The current gap in immunity thus needs to be addressed now by the Department through the grant of antitrust immunity to bridge the two alliances.

(ii)(c) The potential harm that would be inflicted on the applicant carriers and the traveling public by a denial of antitrust immunity is not mitigated to any significant degree by the possibility of one or the other U.S. carrier joining a different alliance. If immunity were denied, as Air France and KLM continue to integrate, the Department's decision could cause either Delta or Northwest to withdraw from its alliance. If that were to occur, the Department will have created a precedent here that will seriously reduce, if not eliminate, viable alternative alliance options for the withdrawing carrier.

First, every other significant global immunized alliance has a U.S. carrier as a principal member, *i.e.*, STAR, which has United as a lead member, and oneworld, with American. Thus, if the Department were to reject this application on the grounds that an international alliance cannot include more than one major U.S. carrier, then the "expelled" carrier could not join any of the major global immunized alliances that exist today. Such a policy would also make it difficult or impossible for other carriers, such as U.S. Airways, to participate in an antitrust immune major global alliance.

Second, both Delta and Northwest have invested heavily in their respective immunized alliances. It has taken years for the SkyTeam ATI carriers and Northwest/KLM to achieve the benefits that exist today. Requiring one carrier or the other to scrap its existing ties and start from scratch (even if it were possible) would be a huge loss, not only for the carrier, but also for consumers and for global competition. The severe impact of such financial losses would be particularly damaging in the current fragile economic environment.

**20. Please describe the sources of and estimate the value of any cost savings that You will be able to achieve only if You were granted ATI (i.e., that could not be achieved without ATI).**

The Joint Applicants do not believe, in the absence of ATI, that there are any significant cost savings potentially achievable through codesharing other than the sorts of limited cost savings that can be realized in competitor collaborations

within the constraints imposed by the antitrust laws.<sup>12</sup> Indeed, as discussed in response to Questions 11, and 19, the absence of antitrust immunity would threaten the continuing realization of cost savings currently being achieved within the two separately immunized alliances. The Joint Applicants believe that with antitrust immunity, but without joint revenue/profit sharing, it is possible to achieve certain cost savings such as through the negotiation of global maintenance agreements, "at cost" service provision for partner handling of flights outside of the expanded alliance, and leveraging of joint purchasing power.<sup>13</sup>

Short of complete revenue and profit sharing, certain cost savings can be realized such as through mini-JVs on specific gateway-to-gateway routes, allowing the carriers to optimize frequencies and aircraft gauge on such routes. Other, more extensive, merger-type cost savings will only be achievable as the carriers move toward and achieve full revenue and profit sharing. A major such cost saving, which has been achieved in the Northwest/KLM Joint Venture, flows from reciprocal representation of each partner by region. Northwest, for example, represents the Northwest/KLM Joint Venture in North America, while KLM represents the joint venture in Europe, the Middle East and Africa. This has allowed Northwest to completely withdraw (including its ticket stock) from

---

<sup>12</sup> Moreover, in addition to cost savings, there are substantial revenue benefits that can be achieved only with antitrust immunity. *See* Response to Question 16.

<sup>13</sup> While certain forms of joint purchasing may be theoretically available in the absence of ATI, the carriers are unlikely to enter into such collaborations absent the depth and continuity of relationships that form as a result of ATI.

Europe, while KLM is fully responsible for joint venture airport customer service, lounges, marketing, reservations, and frequent flyer programs.

Similarly, KLM has completely withdrawn from North America, and Northwest has assumed responsibility for all of the foregoing functions on behalf of the joint venture. The Northwest/KLM Joint Venture has also achieved cost savings and efficiencies in the elimination of unnecessary sales agents, in reducing distribution costs, through rental reduction through co-located offices, and through the sharing of knowledge and expertise in areas such as electronic services (E-ticketing and Internet), next generation revenue management, customer service, reservations and service recovery and dispatch.

Northwest and KLM do not maintain records that would allow them to quantify the cost savings that antitrust immunity and a common bottom line have permitted them to realize. The Joint Applicants have not discussed possible areas of cost savings and thus are not in a position to estimate the level of cost savings that could be achieved if antitrust immunity were granted and the carriers entered into revenue/profit sharing. Once antitrust immunity is granted and as the carriers move toward a common bottom line, they intend to explore areas of potential cost savings such as have been achieved in the NW/KLM Joint Venture.

21. **Please describe (i) how the NW/KLM Joint Venture has been impacted by the merger of AF and KL, and whether NW or KL have had to modify their procedures with respect to the NW/KLM Joint Venture in the post-AF/KL merger environment, (ii) how the AF/KL Strategic Management Committee has affected the operation of the NW/KLM Joint Venture, and (iii) whether the AF/KL Strategic Management Committee has made any changes to AF/KL procedures/operations to specifically accommodate the NW/KLM Joint Venture in the post-AF/KL merger environment.**

(i) The Northwest/KLM Joint Venture governance procedures remain in place. The Air France-KLM merger has, and is likely to continue to, give rise to operational and commercial issues that impact the joint venture and may deprive consumers of the full benefits they could enjoy from the Northwest/KLM Joint Venture (as well as from the SkyTeam ATI Alliance). Northwest and KLM will continue to seek to resolve these issues through established Joint Venture processes. Because of the gap in immunity coverage created by the Air France-KLM merger, KLM and Air France have implemented interim protocols to prevent the disclosure of competitively sensitive NW/KLM Joint Venture information to Delta.

(ii) The Air France/KLM Strategic Management Committee ("SMC"), as distinct from the AF-KLM merger itself (see response to subpart (i) above), has not affected the operation of the Northwest/KLM Joint Venture to date. The SMC is not involved in day-to-day operational matters.

(iii) The Air France-KLM SMC has implemented various protocols to address the circumstances presented by the immunity gap given the separate antitrust immunities held by the Northwest-KLM Joint Venture and the Air France's SkyTeam antitrust immunity with Delta. In effect, the carriers have been unable to work together to coordinate their transatlantic operations during this period. Air France-KLM therefore believe that the protocols significantly impair their ability to realize the potential efficiencies of their merger and also

prevent Air France-KLM from working together with their two alliance partners, Northwest and Delta, on operational and commercial issues in a way that maximizes the potential public benefits from the broader alliance that the Joint Applicants seek to achieve.

**22. Please describe (i) what markets You believe are relevant for the competitive analysis of Your Application for Antitrust Immunity and (ii) to what extent restrictions in the existing bilateral air services agreements between and among the United States and EU member states (a) would limit the benefits that would be derived from the Expanded SkyTeam ATI Alliance and (b) would affect competition, including the potential for new entry, in markets in which the Expanded SkyTeam ATI Alliance would compete.**

(i) The markets relevant for the competition analysis to be performed by the Department are the same as those the Department has regularly examined in past antitrust immunity cases. For the Expanded SkyTeam ATI Application, these would include: nonstop city pairs; the U.S.-country-pair markets; and the overall U.S. - transatlantic markets.

(ii)(a) With respect to EU states that have not signed Open Skies Agreements with the U.S. (such as the U.K., Ireland, Spain, and Greece), the ability of the Joint Applicants to codeshare may be restricted. Thus, for example, Northwest may not be able to codeshare on Air France beyond Paris to points in Spain (or Delta on KLM beyond Amsterdam to points in Spain). These limitations have equally affected all previous antitrust immunity applications and will not meaningfully constrain the public benefits from this Joint Application.

(ii)(b) There are Open Skies Agreements in effect between the U.S. and France, Netherlands, Italy and the Czech Republic - - the homelands of the four

SkyTeam carrier applicants in this immunity proceeding; thus, there are no bilateral restrictions on competition or new entry in the four U.S.- country markets involved in this Application.

There are also Open Skies Agreements in effect with the majority of EU Member States and the other European states served by the Expanded SkyTeam ATI carriers, such as Germany, the Scandinavian countries, Belgium, Switzerland, and Poland. As a result there should be no bilateral effects on competition and new entry in these markets.

For those U.S.-EU markets with restrictive bilaterals, principally the U.K., Spain, Ireland and Greece, the Expanded SkyTeam ATI Alliance would not significantly alter the competitive landscape. In each case, no nonstop overlap city-pairs exists among the Joint Applicants, as only one carrier at most provides nonstop service on any city-pair to and from the United States. As competitors offering predominantly connecting service in these markets against incumbents offering nonstop flights, the Joint Applicants can only become more effective competitors offering expanded one-stop services over multiple EU gateways if the immunity application is granted by the Department. Bilaterals between the U.S. and even the restricted countries contain rights for new entry which are available today, and will not be affected by the instant application.

23. **Please provide a detailed description of the Parties' mutually agreed inventory management procedures for codeshare flights, including, but not limited to, procedures and criteria for establishing inventory allocations in the automated environment. Include the maps of CRS fare classes between AF, AZ, DL, KL, NW, and OK as well as the maps between the revenue management buckets of AF, AZ, DL, KL, NW, and OK.**

**These maps should include the revenue dollar amount and all restrictions associated with each fare class and revenue management bucket. (We understand that such maps may be preliminary and in draft form at this stage.)**

Northwest:

Northwest is not a party to “mutually agreed to” inventory management procedures for codeshare flights with the other Joint Applicants. Requests for Northwest operated inventory (including code-share requests) are assessed based on network value and are granted inventory access accordingly. Outlined below is a description of how the inventory valuation process works in a codeshare environment (except with KLM, which is discussed immediately following), in a two segment trip in which one segment is operated by Northwest and the second segment is operated by a SkyTeam partner.

*Where Northwest is the marketing carrier:* Northwest first determines the revenue value of the Northwest operated portion of the itinerary (based on a previously agreed prorate of the O&D fare) to determine whether access will be granted for the Northwest operated portion of the trip. If inventory is available based on the value to Northwest's network, inventory access is granted. The partner's inventory availability is displayed based on an agreed class mapping table (the NW fare class is mapped to the partner's fare class table). If the partner indicates that inventory is available for the corresponding fare class, it will be shown as available for the partner's operated portion of the itinerary. If the partner's inventory has been closed out for that fare class, no seats will be displayed as available at that fare level.

*Where Northwest's partner is the marketing carrier:* In this situation, the process is reversed. The partner (marketing carrier) first determines whether to make inventory available on its operated leg based on its own internal inventory valuation process. Northwest provides information on its seat availability. A class mapping table provided by Northwest is used by the partner to translate the quoted fare into the appropriate Northwest fare class. If inventory is available for that Northwest fare class (based on the approximate value to the network), inventory will be displayed as available to the marketing carrier.

Northwest provides only *fare class* mappings to its partners for Northwest inventory availability access. There are no "maps between the revenue management buckets" provided to/from Northwest and any of its partners.

Northwest is producing herewith the currently agreed fare class mappings between Northwest and its SkyTeam partners. See Bates No's. NW-ST-ITA 02603 (AZ); NW-ST-ITA 02769-70 (AF); NW-ST-ITA 02950 (CSA); NW-ST-ITA 03171 (DL).

For flights marketed and operated with Northwest's joint venture partner, KLM, yield management decisions reflect the alignment of incentives created by the revenue sharing agreement between Northwest and KLM. While Northwest and KLM have separate yield management systems, the joint venture flights are managed by one fully integrated department with staff from both carriers.

The primary difference between the yield management process described above and the process employed within the Northwest/KLM Joint Venture is that Northwest and KLM, in effect, each treat the other's network as an extension of its own. Northwest and KLM make separate inventory evaluations for their own operated flights but they each use fare estimates and displacement costs for the combined Northwest and KLM network that each provides to the other.

Conceptually, the process works as follows:

Each carrier separately estimates a revenue amount that NW + KL will receive from the customer.

In addition, each carrier sends to the other a displacement cost for each segment in its network.

Access on the operating carrier is then determined by taking the NW + KL network revenue amount, subtracting the displacement costs from the legs operated by the partner carrier, and using the resulting revenue amount to determine inventory access.<sup>14</sup>

Delta Response:

Delta does not have a multilateral mutually agreed inventory management policy. Each carrier is responsible for managing its own inventory and the access of other carriers to an operating carrier's inventory is governed by the mapping

---

<sup>14</sup> This process is currently in place for both Northwest and KLM operated flights of Northwest marketed itineraries and for KLM operated flights of KLM marketed itineraries. System development efforts currently underway will extend this process to Northwest operated, KLM marketed flights.

arrangement entered into with each codeshare carrier. Delta revenue manages the inventory on its flights independently of what other carriers may do.

The difference in Delta inventory management between an antitrust immunity and a non- antitrust immunity codeshare relationship is that with antitrust immunity, Delta and its codeshare partner are free to discuss inventory management and pricing issues that would not be permitted absent such immunity. Thus, in establishing their fare mapping agreements, the carriers may have detailed discussions concerning the relative revenues generated by various ticket sales, actual fares, pricing logic and policies, etc. and based on these discussions can more efficiently establish fare mapping arrangements.

Delta does not map to other carriers' "revenue buckets" as this question assumes. Different carriers value their revenues differently, and this is not a meaningful or efficient means of accomplishing fare mapping. Instead, Delta enters into agreements that map Delta fare classes to the fare classes of the codeshare partner. Each carrier decides separately on the revenue criteria that it will assign to those fare classes. This inventory class-mapping is done on a bilateral basis, not through any overarching global SkyTeam agreement. Delta is producing documents Bates No. DL002722-02726 reflecting its fare class mapping with the other Joint Applicants as requested.

Air France:

Air France is engaged in two types of codesharing services, namely block space and free flow.

In the case of block space services, the operating and marketing carriers typically agree on the size of the seats allotments and on a price per seat. The marketing carrier then offers the seats for sale to the public. No inventory requests or class mapping operations are necessary.

In the case of free flow codesharing, inventory requests between code share partners are assessed based on network value and are processed as described below.

1. *Air France is the marketing carrier.* AF determines the revenue value of the Air France operated portion of the itinerary to determine availability granted for the Air France operated portion of the trip. A class mapping table, negotiated between Air France and his partner, is used to determine the partner's fare classes (the Air France fare class is mapped to the partner's fare class table and inventory is displayed accordingly).

2. *Air France's partner is the marketing carrier.* The partner determines how much inventory to display on its operated leg(s) based on its inventory procedures. A class mapping table, negotiated between Air France and its partner, is used to determine Air France's fare classes to request inventory to display for Air France's operated leg(s). Air France determines the approximate

network value by Air France class for the Air France portion of the trip and responds with the appropriate availability.

Air France only provides fare class mappings to its partners for Air France availability access.

KLM:

Northwest's response to this question, both with respect to its procedures with KLM and with respect to other carriers, accurately describes KLM's procedures.

Alitalia:

Alitalia has codeshare arrangements with Delta and Air France. Their responses to this question describe the inventory management procedures in place for these arrangements.

CSA:

CSA has a codeshare arrangement with Delta. Delta's response accurately describes the procedures relevant to that arrangement.

24. Please discuss (i) whether Your interline traffic with airlines that are not part of the Expanded SkyTeam ATI alliance has declined over the past three years, and, if so, the extent to which such declines are attributable to less favorable prorate terms for airlines that are not part of the Expanded SkyTeam ATI alliance, (ii) how the terms of Your interline agreements with airlines that are not members of the Expanded SkyTeam ATI Alliance have changed over the past three years when compared with Your interline agreements with airlines that are members of the Expanded SkyTeam ATI Alliance, (iii) whether You plan to reduce the number of airlines that are not part of the Expanded SkyTeam ATI Alliance with which You maintain interline agreements or otherwise reduce (either contractually or through inventory availability) the numbers of passengers You carry on an interline basis with airlines that are not part of the Expanded SkyTeam ATI Alliance, and (iv) whether any changes to Your interline practices and policies vis-à-vis carriers that are not part of the Expanded SkyTeam ATI Alliance are contemplated.

Northwest:

(i) Interline traffic with non-Expanded SkyTeam ATI Alliance carriers has increased over the past three years. Northwest maintains interline agreements with approximately 190 airlines. The terms of these Interline Ticket and Baggage Agreements stipulate that in the absence of a negotiated bilateral prorate agreement, standard industry settlement rules shall apply, either IATA or ACH, as applicable. Neither IATA nor ACH have not changed terms of settlement in the past three years.

(ii) Solely as a function of SkyTeam status, the terms of Northwest's interline agreements with carriers that are not part of the Expanded SkyTeam ATI Alliance have not changed during the past three years vis-à-vis the terms of interline agreements with carriers that are part of the Expanded SkyTeam ATI Alliance. Rather, Northwest's interline agreements that have undergone change have done so as a result of other factors, including (a) that individual agreements' continuing value to the Northwest network, (b) the complexity of interline accounting processes with that specific interline partner (including but not limited to revenue accounting data exchange and ability to handle non-standard settlement methods), and (c) the distribution compatibility with that specific interline partner (e.g. interline e-ticket processing).

(iii) Northwest does not plan to reduce the number of interline relationships or reduce the interline activity with carriers that are not part of the

Expanded SkyTeam ATI Alliance. Northwest's interline carrier portfolio is comprised of airlines providing economic value to the Northwest network and Northwest will continue to manage its interline relationships in this manner.

(iv) Northwest does not plan to change interline practices or policies vis-à-vis carriers that are not part of the Expanded SkyTeam ATI Alliance. However, changes could be made based on other factors, such as ability to support interline e-ticket processing.

Delta:

(i) Delta's interline traffic with all carriers other than the five other ATI applicants has not declined. It has remained essentially flat during the past three years.

(ii) The terms of the Interline Ticket Baggage Agreement and the standard IATA prorate terms that apply in the absence of a special prorate agreement have not changed in the last three years. This governs Delta's relationship with most interline carriers. With respect to those carriers with whom Delta has negotiated special prorate agreements, Delta generally has not changed its special prorate strategy in any way that would discourage interline service on non-SkyTeam carriers. There are individual cases in which an interline carrier initiated a less favorable prorate arrangement, or substantially revised its fare structure in a way that would have resulted in very low pro rate payments under the former agreement. In those cases, Delta agreed to less

favorable special pro rate terms in the last three years. In general, however, Delta has no separate special prorated strategy applicable to alliance carriers and non-alliance carriers. Each case is negotiated based on the specific circumstances of the bilateral relationship.

(iii) Delta does plan to reduce the number of carriers with whom it maintains special pro rate relationships. However, this is due to the cost of administering the special pro rate relationship, rather than any alliance considerations. The decision to simplify Delta's interline relationships is driven primarily by a comparison of the revenue generated by the relationships versus the cost of maintaining a special pro rate agreement with individual carriers. However, any carrier with whom Delta chooses not to maintain a special pro rate agreement with will simply default to the IATA standard Interline Ticket Baggage agreement. Delta has no plans to cancel the standard IATA ITB agreement with any carrier at this time; in fact Delta signed 17 new ITB agreements during the past year. Delta has a goal of 100% e-ticket interline transactions by the end of 2007 (an IATA-imposed deadline) and will cancel interline relationships with carriers that cannot comply with e-ticket requirements at that time (unless there are significant contrary revenue considerations).

(iv) Other than as set forth in the responses above, Delta does not plan to change interline practices or policies with respect to carriers that are not part of the Expanded SkyTeam ATI Alliance.

Air France:

(i) Over the Air France survey period (April 2003-September 2004) the global interline volume has been consistent with the industry trend: growing during periods with high demand in the marketplace, decreasing during low demand periods. The year-over-year figures make this change clearly apparent. During this period Air France has neither terminated any interline prorate agreements, nor changed the prorate amounts to make them less favorable to non-SkyTeam airlines. Airlines with whom billing was made under the IATA multilateral prorate regulation were kept as interline partners with no change as to billing aspects.

(ii) The terms of Air France interline prorate agreements with airlines that are not members of the Expanded SkyTeam ATI Alliance have not changed over the past three years (besides the natural change of prorate amounts in order to remain consistent with Air France expected revenue on its own sectors, that is impacting all prorate agreements). What has changed is the flexibility offered to the Expanded SkyTeam ATI Alliance members essentially in terms of billing methodology (based on actual fares, rather than on average billing amounts) and in some instances improved access to seat inventory.

(iii) Air France's approach to an interline strategy is rather opportunistic: Air France intends to maintain and develop any agreements that would allow its network to expand. The two conditions for an interline

agreement between Air France and a third carrier to be maintained or developed are:

1. that it is a balanced agreement between Air France and the third carrier in terms of what sales opportunity the network of each airline brings to the other, and

2. that the prorate amounts respect the yield requirement for sales of the third carrier over Air France sectors, and that Air France is not over-charged for its tickets uplifted on the services of the third carrier.

Inventory is decided based on the revenue paid by the third carrier, or the internal inventory management system constraints.

(iv) No changes to Air France Bilateral Prorate Agreements have been studied and planned. Air France is currently contemplating seeking a change in the IATA Multilateral Prorate regulation in order to have this billing methodology remain consistent with its own expected revenue per booking class. In order to achieve our goal in this area, Air France is working with other airlines within competent IATA structures to have the Multilateral billing methodology amended.

KLM:

(i) KLM's over all interline traffic has declined over the past three years, including for carriers that are, and are not, part of the Expanded SkyTeam ATI Alliance. KLM does not believe that those declines are attributable to less favorable prorate terms for airlines that are not part of the Expanded SkyTeam

ATI Alliance. The changes in interline traffic vary by carrier. Thus, during that period, interline traffic between KLM and certain airlines that are part of the Expanded SkyTeam ATI Alliance has increased, while interline traffic between KLM and other carriers that are part of the Expanded SkyTeam ATI Alliance has decreased. The same is true with respect to KLM's interline traffic with airlines that are not part of the Expanded SkyTeam ATI Alliance.

(ii) The terms of KLM's interline agreements with airlines that are not members of the Expanded SkyTeam ATI Alliance have not changed over the past three years when compared with KLM's interline agreements with airlines that are members of the Expanded SkyTeam ATI Alliance. Such agreements are negotiated individually and reflect both carriers' perceptions of the benefits they can obtain by working together.

(iii) KLM does not have plans to reduce the number of airlines -- whether or not those airlines are members of the Expanded SkyTeam ATI Alliance -- with which it has interline agreements. In fact, KLM anticipates that it will increase the number of airlines with which it has interline agreements by entering into agreements with carriers that presently have such agreements with AF but not with KLM. KLM does not have plans to reduce the number of passengers it carries on an interline basis with airlines that are not part of the Expanded SkyTeam ATI Alliance. The number of passengers carried by KLM on

an interline basis with any particular carrier will be based on the benefits that KLM and that carrier believe can be achieved by working together.

(iv) KLM is not contemplating changes to its interline practices and policies vis-à-vis carriers that are not part of the Expanded SkyTeam ATI Alliance.

Alitalia:

Alitalia's interline traffic on US services with carriers that are not part of the Expanded SkyTeam ATI Alliance has declined over the past three years. However, this change is due to several factors, including changes in capacity and service by Alitalia and the other carriers, changes in overall market demand, and changes in competitive services. It is not possible to measure the extent to which it might be attributable in part to the terms of prorate agreements. Most Alitalia interline agreements use the standard IATA prorate terms which have not changed over the past three years. Alitalia has no plans to reduce the number of non-SkyTeam carriers with which it interlines or the number of passengers exchanged with them. Nor does Alitalia have plans to change its interline practices and policies towards non-SkyTeam carriers.

CSA:

(i) CSA's interline traffic on U.S. services with carriers that are not part of the Expanded SkyTeam ATI Alliance has remained level over the past three years.

(ii) Most CSA interline agreements use the standard IATA prorate terms which have not changed over the past three years.

(iii) CSA has no plans to reduce the number of non-SkyTeam carriers with which it interlines or the number of passengers exchanged with them.

(iv) CSA also does not have plans to change its interline practices and policies towards non-SkyTeam carriers.

**Conclusion**

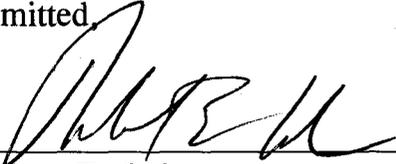
The foregoing responses, together with the accompanying production of documents and data, constitute a full and complete response to the Department's Order Requesting Additional Information. Accordingly, the Joint Applicants urge the Department to immediately issue a Scheduling Order establishing the due date for answers, and to proceed with prompt approval of the Joint Application.

Respectfully Submitted,

/s/ Michael F. Goldman  
Silverberg, Goldman & Bikoff, LLP  
1101 30<sup>TH</sup> Street, N.W.  
Washington, DC 20007  
Counsel for SOCIÉTÉ AIR FRANCE

/s/ Paul V. Mifsud, Vice President -  
Government and Legal Affairs, USA  
KLM ROYAL DUTCH AIRLINES  
2501 M Street, NW  
Washington, DC 20037

/s/ Allan I. Mendelsohn  
Sher & Blackwell  
1850 M Street, NW  
Suite 900  
Washington, DC 20036  
Counsel for CZECH AIRLINES

  
Robert E. Cohn  
Alexander Van der Bellen  
Shaw Pittman LLP  
2300 N Street, N.W.  
Washington, D.C. 20037  
Counsel for DELTA AIR LINES, INC.

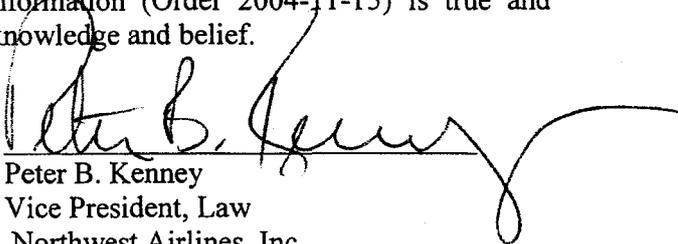
/s/ Megan Rae Rosia  
Managing Director  
Government Affairs and  
Associate General Counsel  
NORTHWEST AIRLINES, INC.  
901 15<sup>th</sup> Street, NW, Suite 310  
Washington, DC 20005

/s/ Richard D. Mathias  
Zuckert, Scoutt & Rasenberger, L.L.P.  
888 Seventeenth Street, N.W.  
Washington, DC 20006  
Counsel for ALITALIA-LINEE AEREE  
ITALIANE-S.P.A.

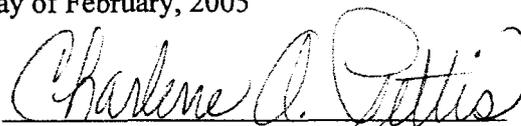
**VERIFICATION**

I, Peter B. Kenney, being first duly sworn, deposes and says:

1. I am Vice President, Law for Northwest Airlines, Inc.
2. I hereby verify that the information submitted by Northwest Airlines, Inc. in response to the Department of Transportation's Order Requesting Additional Information (Order 2004-11-15) is true and correct to the best of my knowledge and belief.

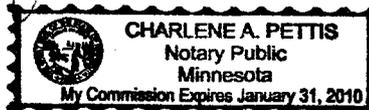
  
Peter B. Kenney  
Vice President, Law  
Northwest Airlines, Inc.

Subscribed and sworn to before me this 4<sup>th</sup> day of February, 2005

  
Notary Public

My commission expires:

Jan. 31, 2010



**VERIFICATION**

I, Jean-Michel Barthélémy, being first duly sworn, deposes and says:

1. I am Vice President, European and International Affairs of Société Air France.
2. I hereby verify that the information submitted by Société Air France in response to the Department of Transportation's Order Requesting Additional Information (Order 2004-11-15) is true and correct to the best of my knowledge and belief.



Jean-Michel Barthélémy  
Vice President, European and  
International Affairs  
Société Air France

Subscribed and sworn to before me this \_\_\_ day of February, 2005

\_\_\_\_\_  
Notary Public

My commission expires:

\_\_\_\_\_  
Le soussigné M<sup>me</sup> Muriel LEVI  
notaire à Paris certifie la signa-  
ture de M. Jean-Michel BARTHELEMY  
apposée ci-contre  
A Paris, le 7 Février 2005



**CERTIFICATION**

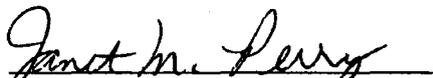
I, Jan-Ernst de Groot, being duly sworn, deposes and says:

1. I am General Counsel and Company Secretary of KLM Royal Dutch Airlines ("KLM").
2. I hereby certify that the information submitted by and on behalf of KLM in response to the Order Requesting Additional Information issued by the Department in this proceeding is true and correct to the best of my knowledge and belief.



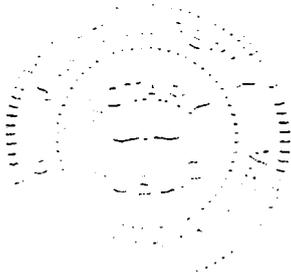
\_\_\_\_\_  
Jan-Ernst De Groot

Subscribed and sworn to before me this 3 day of February, 2005

  
\_\_\_\_\_  
Notary Public

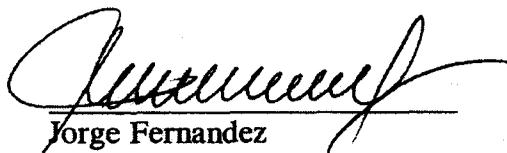
My commission expires: 3/14/09

\_\_\_\_\_  
**JANET M. PERRY**  
NOTARY PUBLIC - DISTRICT OF COLUMBIA  
MY COMMISSION EXPIRES 3/14/09



**CERTIFICATION**

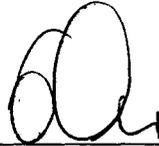
Pursuant to title 18 United States Code section 1001, I, Jorge Fernandez, in my individual capacity and as an authorized representative of the pleader, have not in any manner knowingly and willfully falsified, concealed or failed to disclose any material fact or made any false, fictitious or fraudulent statement or knowingly used any documents which contain such statements in connection with the preparation, filing or prosecution of the pleading. I understand that an individual who is found to have violated the provisions of 18 U.S.C. section 1001 shall be fined or imprisoned for not more than five years, or both.

A handwritten signature in black ink, appearing to read 'Jorge Fernandez', written over a horizontal line.

Jorge Fernandez  
Vice President - International & Alliances  
Delta Air Lines, Inc.

**CERTIFICATION**

Pursuant to title 18 United States Code section 1001, I, Orlando D'Oro, in my individual capacity and as an authorized representative of the pleader, have not in any manner knowingly and willfully falsified, concealed or failed to disclose any material fact or made any false, fictitious or fraudulent statement or knowingly used any documents which contain such statements in connection with the preparation, filing or prosecution of the pleading. I understand that an individual who is found to have violated the provisions of 18 U.S.C. section 1001 shall be fined or imprisoned for not more than five years, or both.



---

Orlando D'Oro  
V.P. Regulatory Affairs  
North America & Mexico  
Alitalia Group

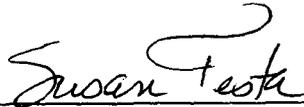
## CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Joint Applicants' Supplemental Information Response has been served this 8<sup>th</sup> day of February, 2005, upon each of the following addressees:

James J. Ballough	jim.ballough@faa.gov
U.S. TRANSCOM/TCJ5-AA	tcbentdw@hq.transcom.mil
Roger Fones	roger.fones@usdoj.gov
Marshall S. Sinick	msinick@ssd.com
Carl B. Nelson, Jr.	carl.nelson@aa.com
Howard Kass	howard_kass@usairways.com
Jeffrey A. Manley	Jeffrey.Manley@wilmerhale.com
R. Bruce Keiner, Jr.	rbkeiner@crowell.com
Joanne Young	jyoung@bakerlaw.com
David Kirstein	dkirstein@bakerlaw.com
Jonathan B. Hill	jhill@dlalaw.com
Stephen H. Lachter	lachter@starpower.net
Thomas V. Lydon	tom.lydon@evergreenaviation.com
David Short	dshort@fedex.com
Russell E. Pommer	rpommer@atlasair.com
Mark McMillin	mcmillin@woa.com
Moffett Roller	mroller@rollerbauer.com
John L. Richardson	jrichardson@johnlrichardson.com
David L. Vaughan	dvaughan@kelleydrye.com
Pierre Murphy	pmurphy@lopmurphy.com
Lawrence D. Wasko	ldwasko@erols.com
Mark W. Atwood	matwood@sherblackwell.com
James R. Weiss	jimwe@prestongates.com

Responsive pleadings should also be served upon:

Megan Rae Rosia	megan.rosia@nwa.com
Michael F. Goldman	mgoldman@sbgdc.com
Allan I. Mendelsohn	amendelsohn@sherblackwell.com
Richard D. Mathias	rdmathias@zsrllaw.com
Paul V. Mifsud	pmifsudklm@earthlink.net



---

Susan Testa