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Re: Competition in Air Transportation

Dear Ms. Lubell and Ms. Petsonk,

The Open Markets Institute applauds the U.S. Department of Justice (DOJ) and the U.S. Department of Transportation (DOT) for launching this broad inquiry into the state of competition in air travel. The Open Markets Institute is a non-profit organization whose mission is to safeguard our political economy from concentrations of private power that undermine fair competition and threaten liberty, democracy, and prosperity.

The U.S. air travel system is facing significant challenges. Americans are deeply unsatisfied with air service because they have increasingly suffered routine indignities such as frequent delays,[1] denied boardings,[2] mishandled baggage,[3] and escalating ancillary fees.[4] Small and mid-sized cities have seen their air service significantly reduced or eliminated. Workers have seen their wages and benefits slashed. Meanwhile, the airlines themselves face routine bankruptcies, necessitating public bailouts. The root cause is a vicious combination of deregulation and

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[1] The percentage of severely delayed flights (those delayed by at least 90 minutes) reached an all-time high in 2024. Ben Blatt, *Airlines Are Padding Flight Times. It's Not Your Imagination.*, THE NEW YORK TIMES, Nov. 27, 2024, https://www.nytimes.com/2024/11/27/upshot/airlines-flight-times-padding.html.

[2] The percent of passengers who have been involuntarily denied boarding more than doubled between 2018 and 2023. Bureau of Transportation Statistics, *Passengers Boarded and Denied Boarding by the Largest U.S. Air Carriers*, UNITED STATES DEPARTMENT OF TRANSPORTATION (2023), https://tinyurl.com/rosapntlbtsNTS.

[3] The number of bags mishandled per 1,000 bags enplaned increased by over 40 percent between 2020 and 2023. Bureau of Transportation Statistics, *Baggage Mishandled by Marketing U.S. Air Carriers*, UNITED STATES DEPARTMENT OF TRANSPORTATION (2019), https://tinyurl.com/rosapntlbtsNTS.

[4] *See* RICHARD BLUMENTHAL, *The Sky's the Limit: The Rise of Junk Fees in American Travel*, 55 (2024), https://www.hsgac.senate.gov/wp-content/uploads/2024.11.25-Majority-Staff-Report-The-Skys-the-Limit-The-Rise-of-Junk-Fees-in-American-Travel-1.pdf.

increasing monopoly power, resulting in an airline industry marked by declining quality and shrinking service levels.

The Biden administration is the first administration in decades to take significant steps toward addressing the various crises in the airline industry. The administration has proposed and finalized rules to improve the passenger experience, publicly pressured airlines to improve service commitments and reliability, and successfully blocked anticompetitive proposed mergers. However, there is much more that must be done.

While Congressional action is necessary to restore traditional common carriage requirements that require transparent, equitable pricing and terms of service, there still is much that DOJ and DOT can do under current law to ameliorate the continuing deterioration of this essential sector of the economy.

20th Century Regulatory Successes

In the early 20th century, policymakers recognized that the nascent airline industry, like other networked transportation industries, was inherently prone to destructive competition, as rate wars would lead competitors to drive each other into insolvency and bankruptcy. This tendency was caused by the economic characteristics of the airline industry.[5] The high fixed costs and low short-term marginal costs of commercial aviation, coupled with comparatively low barriers to entry, led to vicious competition that ultimately scared away investment in the industry and damaged the public interest.[6]

Lawmakers had previously seen the harsh results of an unregulated transportation system in the 19th-century railroad industry. While they remained unregulated, railroads typically engaged in self-destructive rate wars in large metropolises where they faced competition, while they did the opposite — price-gouging — in small towns and rural areas where they held a monopoly. Lack of regulation contributed to the bankruptcy of nearly one-third of the industry by the 1870s, while also leaving millions of farmers and other shippers exposed to predatory and monopolistic pricing.[7] Lawmakers hoped to avoid the same fate in the airline industry.

To this end, lawmakers created the Civil Aeronautics Board (CAB) in 1938 to regulate the industry. The CAB was tasked with employing utility-style regulation, similar to regulations long-before applied to railroads by the Interstate Commerce Act of 1887. Specifically, Congress instructed the CAB to write market rules focused on three primary areas: market entry and exit, rates, and antitrust.[8] All three legs of the airline regulation "stool" were required to prevent destructive competition and ensure regional parity while also guarding against the emergence of local and regional monopolies.

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[5] *See* Paul Stephen Dempsey, *The Rise and Fall of the Civil Aeronautics Board - Opening Wide the Floodgates of Entry*, 11 TRANSP. LAW J. (1979), https://papers.ssrn.com/abstract=2233081.
[6] Paul S. Dempsey, *Airlines, Airports and Antitrust: A Proposed Strategy for Enhanced Competition*, 58 J. AIR LAW COMMER., 461–465 (1993), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1942926.
[7] Phillip Longman, *The Spirit Airlines Paradox*, THE ATLANTIC (2024), https://www.theatlantic.com/ideas/archive/2024/01/jetblue-spirit-airlines-antitrust/677192/.
[8] Dempsey, *supra* note 1 at 93.

The CAB's regulatory regime certainly was not perfect. CAB regulators were reluctant to issue operating authority, which at times retarded competition below optimal levels. Additionally, the CAB's utility-style ratemaking encouraged airlines to compete more vigorously on service quality instead of price, making it difficult for airlines to lower prices to stimulate demand.[9]

On balance, however, the regulatory system worked. The CAB's system of regulation led to stability in the industry, falling fares, and increased access to air travel. In 1962, only 33 percent of American adults had flown on an airplane. By 1977 that number increased to 63 percent thanks to lower fares.[10] Regulation also allowed for great technological progress. Investors, assured of the industry's stability, financed innovations that would lead to the introduction of the "Jet Age" in the 1960s. Additionally, because airlines were required to charge roughly equal fares for equal distances, the CAB's regulation also promoted regional equality and the growth of America's heartland.[11]

Rationale for Deregulation

In 1975, liberal Democrats including Ted Kennedy joined with Republicans in calling for the deregulation of the airline industry through the elimination of the CAB. High inflation was a major concern, and policymakers hoped that deregulation would lead to lower airfares. Even consumer activists such as Ralph Nader argued that the CAB had been "captured" by the airline industry, claiming that "both airline management and unions had become overpaid and sclerotic at the expense of 'the consumer.'"[12] Proponents of deregulation posited that the airline industry would evolve into a model of near-perfect competition, and that concentration was unlikely because of free entry and exit.[13] As a result of these efforts, Congress passed and President Carter signed the Airline Deregulation Act of 1978.

The Deleterious Effects of Deregulation

After deregulation, airlines were permitted to unilaterally set prices, terms of service, and enter and exit markets. Airfares did initially fall on high volume routes, but soon, a flood of new entrants destabilized the industry. The new entrants used rock-bottom pricing for airlines tickets, barely recovering their variable costs. The incumbent airlines were forced to do the same to remain competitive. However, this price war rendered airlines unable to recoup their high fixed

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[9] Dempsey, *supra* note 5 at 114–118.
[10] The CAB's regulatory regime was generally successful. It permitted airline fares to fall so significantly that energy-adjusted fares more rapidly in the decade before airline deregulation than in the decade after deregulation. PAUL STEPHEN DEMPSEY, FLYING BLIND: THE FAILURE OF AIRLINE DEREGULATION (1990); Phillip Longman & Lina Khan, *Terminal Sickness*, WASHINGTON MONTHLY, Mar. 2012, http://washingtonmonthly.com/2012/03/01/terminal-sickness/.
[11] *See* PHILLIP LONGMAN & LINA KHAN, *Hard Landing: The Breakdown of America's Air Transport System and the Role of Deregulation*, (2012), https://static.newamerica.org/attachments/4332-hard-landing/Hard%20Landing,%20July%202012.742497c91ebe4f72a6449d60221eea07.pdf.
[12] Longman and Khan, *supra* note 10.
[13] Dempsey, *supra* note 6.

costs.[14] Unable to recover fixed costs, airlines were forced to take on excessive debt, leading to bankruptcy.[15] A full 97 percent of airlines launched after deregulation declared bankruptcy within 10 years of operation.[16]

In addition to instability within the airline industry, deregulation also led to airlines immediately cutting service to small and mid-sized cities, including state capitals like Salem, OR and Trenton, NJ. Senator Robert Byrd of West Virginia voiced his regret in 1986 for casting his vote for deregulation after airlines cut almost all service to his state:

> *This is one Senator who regrets that he voted for airline deregulation. It has penalized States like West Virginia, where many of the airlines pulled out quickly following deregulation and the prices zoomed into the stratosphere—doubled, tripled and, in some instances, quadrupled. So we have poorer air service and much more costly air service than we in West Virginia had prior to deregulation. I admit my error; I confess my unwisdom, and I am truly sorry for having voted for deregulation.*[17]

A recent DOT OIG report documented the extent to which middle America has been hurt by deregulation. In the report, DOT showed that five mid-sized communities — Pittsburgh, PA; Greensboro, NC; Cleveland, OH; Milwaukee, WI; and Cincinnati, OH — all lost over half their departures since 2005.[18] Cincinnati (CVG) has lost over 80 percent of its departures.[19]

Despite paring unprofitable or low-profit routes, carriers still struggled under deregulation to even earn their cost of capital as they continued to face vicious competition. One result was a series of federal bailouts that required taxpayers to absorb billions of dollars in pension debts after such major carriers as United and US Airways declared bankruptcy.[20]

Another consequence was that many airlines defensively merged into other airlines. A total of 46 mergers have been completed since the passage of the Airline Deregulation Act.[21] After a round

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[14] Airlines face relatively high fixed costs. One analysis calculated that fixed costs for airlines represent nearly 80 percent of all fully allocated costs. Paul Stephen Dempsey, *The Financial Performance of the Airline Industry Post-Deregulation*, 456 (2008). Large fixed costs for airlines include aircraft purchasing or leasing, labor (in the short term), and fuel (in the short term).

[15] U.S. Airline Bankruptcies, AIRLINES FOR AMERICA (2024), https://www.airlines.org/dataset/u-s-bankruptcies-and-services-cessations/.

[16] Dempsey, *supra* note 14 at 445.

[17] Phillip Longman, *It's the Monopoly, Stupid*, WASHINGTON MONTHLY (Jun. 21, 2022), http://washingtonmonthly.com/2022/06/20/its-the-monopoly-stupid/ (last visited Dec 23, 2024).

[18] OFFICE OF THE SECRETARY, *Changes in Airline Service Differ Significantly for Smaller Communities, but Limited Data on Ancillary Fees Hinders Further Analysis*, (2020), https://www.oig.dot.gov/sites/default/files/Airline%20Service%20to%20Small%20Communities%20Final%20Report_0.pdf.

[19] Bureau of Transportation Statistics, *Transtats Airports*, UNITED STATES DEPARTMENT OF TRANSPORTATION (2024), https://www.transtats.bts.gov/airports.asp?20=E.

[20] GAO, *Commercial Aviation: Bankruptcy and Pension Problems Are Symptoms of Underlying Structural Issues*, (2005), https://www.gao.gov/assets/gao-05-945.pdf.

[21] U.S. Airline Mergers and Acquisitions, AIRLINES FOR AMERICA (2024), https://www.airlines.org/dataset/u-s-airline-mergers-and-acquisitions/.

of mergers in the 2010s, that included the merger between American Airlines and US Airways, Delta Air Lines and Northwest, United Airlines and Continental, and Southwest Airlines and AirTran Airways, the "Big Four" airlines now control 80 percent of the domestic market. By now, meaningful price competition between legacy carriers has given way to the effects of excessive corporate concentration of ownership. Large institutional investors, such as Blackrock, Vanguard, and State Street now own significant shares in multiple legacy airlines. This "common ownership" by institutional investors has led to increased prices and reduced seat capacity.[22]

In addition to the creation of a national monopoly, deregulation and lax antitrust enforcement have allowed airlines to monopolize airport hubs. The at-will market entry and exit afforded to airlines through deregulation prompted airlines to reorganize their networks from the "point-to-point" model to the "hub-and-spoke" model. This model was pursued, in part, because the creation of hubs gave airlines monopoly and duopoly power at hub airports.

Before deregulation, no airline controlled more than half of any major airport. A 2016 analysis found that at 40 of the 100 largest U.S. airports, one airline controls the majority of the market.[23] Take, for example, three of the busiest airports in the United States by total passenger boardings. Delta carries nearly three-quarters of passengers in Atlanta; American carries over two-thirds of passengers in Dallas/Fort Worth; United and Southwest together carry nearly three-quarters of passengers in Denver.[24]

While some analyses point to a decrease in the number of monopoly city-pair combinations as a sign of robust competition, this is illusory. Prior to deregulation, airlines did not engage in predatory or extractive pricing because prices were fairly set by the CAB instead of driven by monopoly power. Now, on any routes that are not robustly served by ultra low-cost carriers, legacy airlines are freely able to extract monopoly prices through pricing that reflects market power. Additionally, on routes served by low-cost and ultra low-cost carriers, legacy carriers use predatory pricing to drive out competition and subsequently raise prices.[25]

National and route-level consolidation resulting from deregulation and lax merger enforcement has resulted in harms to consumers, labor, and the public more broadly through:

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[22] Martin Schmalz, *Warren Buffett Is Betting the Airline Oligopoly Is Here to Stay*, HARVARD BUSINESS REVIEW (2016), https://hbr.org/2016/11/warren-buffett-is-betting-the-airline-oligopoly-is-here-to-stay.

[23] The Associated Press, *Airline Consolidation Has Created Airport Monopolies, Increased Fares – The Denver Post*, THE DENVER POST (2016), https://www.denverpost.com/2015/07/17/airline-consolidation-has-created-airport-monopolies-increased-fares/.

[24] Bureau of Transportation Statistics, *supra* note 19.

[25] WILLIAM J MCGEE & HELAINE OLEN, *Predatory Pricing In Airlines: How Southwest Lowered Prices to Squeeze Out Competition in Hawaii*, (2024), https://www.economicliberties.us/wp-content/uploads/2024/12/20241209-AELP-predatory-pricing-airlines-v3.pdf; Paul Stephen Dempsey, *Predation, Competition & Antitrust Law: Turbulence in the Airline Industry*, (2002), https://papers.ssrn.com/abstract=1814304.

- Elimination of routes, particularly to small and mid-sized cities,[26]
- Increased delays, mishandled baggage, denied boardings, and escalating ancillary fees,[27]
- High prices at monopolized hub airports,
- High prices in markets not served by low-cost carriers,
- The establishment of two-tier labor systems,
- The slashing of jobs and benefits.[28]

Although unbundling has nominally lowered face-value airline ticket prices, the overall degradation of the flying experience must be considered when reckoning with the true cost of flying. For example, airlines have shrunk seat pitch from an average of 35 inches to 31 inches and width from 18.5 inches to 17 inches. Airlines are also increasingly nickel and diming passengers for every basic amenity, from baggage fees to cancellation and change fees to seat selection.[29] These fees add up. A 2017 Government Accountability Office report noted that for passengers flying with bags, the average cost of airfare *increased* after "unbundling" was introduced.[30] In fact, other than a brief period after 9/11, airfares fell slower after deregulation than before deregulation.[31] In the airline industry, the United States has traded stability through public-focused regulation for stability through extractive oligopoly.

The DOJ and DOT's Role

The DOJ and DOT have an important role to play in protecting the public, including consumers and workers, from abuses of power by today's airline monopolists. These roles fall into three broad categories:

1. Prevent further consolidation of the airline industry,
2. Proscribe anticompetitive actions of dominant airlines,
3. Improve the airline experience for passengers.

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[26] Office of the Secretary, "Changes in Airline Service Differ Significantly for Smaller Communities, but Limited Data on Ancillary Fees Hinders Further Analysis" (Washington, D.C.: United States Department of Transportation, May 27, 2020), https://www.oig.dot.gov/sites/default/files/Airline%20Service%20to%20Small%20Communities%20Final%20Report_0.pdf; *See generally* Longman and Khan, "Terminal Sickness" (detailing the deleterious economic impacts of airline deregulation on the ability to conduct business in middle America).

[27] GANESH SITARAMAN, WHY FLYING IS MISERABLE AND HOW TO FIX IT (2023).

[28] *See* Myongjin Kim, Qi Ge & Donggeun Kim, *Mergers and Labor Market Outcomes in the US Airline Industry*, (2020), https://papers.ssrn.com/abstract=3615410 ("Our findings point to a consistently negative labor market impact of airline mergers with a significant reduction in merging airlines' short-term employment level and long-term per capita salaries and fringe benefits following the mergers").

[29] WILLIAM J MCGEE & GANESH SITARAMAN, *How to Fix Flying: A New Approach to Regulating the Airline Industry*, (2024), https://cdn.vanderbilt.edu/vu-sub/wp-content/uploads/sites/281/2024/01/26143159/20240124-AELP-airlines-final.pdf.

[30] COMMERCIAL AVIATION: INFORMATION ON AIRLINE FEES FOR OPTIONAL SERVICES, 21 (2017), https://www.gao.gov/assets/gao-17-756.pdf.

[31] David B. Richards, *Did Passenger Fare Savings Occur After Airline Deregulation?*, 46 J. TRANSP. RES. FORUM (2007), https://journals.oregondigital.org/trforum/article/view/4461.

Prevent Further Consolidation of the Airline Industry

An increase in oligopolistic market power for the "Big Four" airlines, fueled by deregulation and lax antitrust enforcement, is a prime factor behind the failure of the airline industry to meet its public purposes.

To prevent further consolidation, the DOJ must use its robust authority to challenge any mergers that may cause further anticompetitive effects or that may tend to create a monopoly on the national level, on the airport level, or on the city-pair level. The DOJ's successful lawsuit blocking the proposed merger between JetBlue and Spirit Airlines is an important first step that must be replicated for future proposed mergers.

However, it must be noted that antitrust enforcement is merely one part of the "three-legged stool" of airline regulation. Antitrust enforcement alone will not produce a healthy airline industry. It must be paired with entry/exit and rate regulation.

DOT must also aim to reduce concentration at major airport hubs, which will reduce prices at hubs and improve service. This could be achieved through placing a cap on the percentage of flights a single airline can have at an airport.

Proscribe Anticompetitive Actions of Dominant Airlines

In markets where legacy airlines face competition from low-cost and ultra low-cost carriers, the legacy airlines use several methods to entrench their market power and preclude competition. These include excessive, targeted expansion of capacity, predatory pricing enabled by cross-subsidization from credit card renumerations, and refusals to share essential facilities.[32]

One example of a refusal to share essential facilities is airlines use of majority-in-interest clauses, which allow dominant airlines to stifle competition by effectively disallowing airport expansion. When airports look to expand their facilities, they enter long-term lease agreements with airlines to underwrite the bonds that fund construction. In return, airlines demand majority-in-interest clauses in their leases.[33]

Unlike foreign airports, U.S. airports do not have widespread usage of "common gates." The provisioning of preferential gate leases to monopoly airlines precludes competition from low-cost and ultra low-cost competitors, thereby allowing legacy airlines to keep fares high while also suppressing wages at hub airports.[34] Additionally, at several "capacity-constrained" airports, legacy airlines control takeoff and landing slots.

Although current FAA rules allow the agency to claw back unused slots, airlines can also choose to sublease slots. This allows legacy airlines to extract monopoly rents while maintaining monopoly control over airport infrastructure, effectively giving them controlling of operating certificates at several of the nation's largest airports. The FAA should amend its rules to allow

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[32] Dempsey, *supra* note 25.
[33] McGee and Sitaraman, *supra* note 33.
[34] *Id.*

competitive access to airport infrastructure including takeoff and landing slots, gates, and other facilities. Additionally, DOT should also look to proscribe abuses of majority-in-interest clauses, which allow airlines to stifle growth at airports.[35] Again, it is important that tools used to increase competition are not used in isolation. They must be paired with tools that establish entry and exit regulation and rate regulation.

The DOJ and DOT should also closely examine whether the oligopolistic carriers use predatory pricing to drive out competitors. The financial struggles of airlines such as Spirit Airlines and Hawaiian Airlines can likely be attributed, in part, to predatory pricing by incumbent airlines. This predatory pricing is facilitated by the legacy airlines use of their credit card programs to cross subsidize operational losses for the core business of providing air transportation. By using credit-card cross subsidies, airlines can lower fares and choke low-cost and ultra low-cost competitors out of their dominant hubs. Delta Air Lines, for example, stated in its November 2024 Investor Day presentation that its renumerations from credit card “swipe fees” totaled over $7 billion, while the airline only generated $5.6 billion in operating income.[36] The DOJ and DOT should aggressively enforce any predatory pricing law violations, and the DOT should issue a policy statement on predatory pricing.

The DOJ and DOT should pay particular attention to any attempts by legacy carriers to undercut small airlines that have found a niche of serving smaller airports. Small airlines such as Avelo and Breeze have found success serving airports that legacy carriers have pulled back from,[37] but without adequate investigation and prosecution of predatory pricing violations, nothing stops legacy airlines from replicating their services, underselling them, bankrupting them, and then reverting to status quo ante.

Improve the Airline Experience for Passengers

To improve the passenger experience, DOT should finalize its “Family Seating in Air Transportation” proposed rule and its “Ensuring Safe Accommodations for Air Travelers With Disabilities Using Wheelchairs” proposed rule. DOT should also consider requiring airline interlining, which would require airlines to rebook passengers on different carriers if flights are canceled or significantly delayed. Finally, DOT should use its authority to investigate and address unfair and deceptive practices and methods of competition to investigate airlines abuses of points systems, including instances of point devaluations, excessive fees, and overbearing restrictions on reward points usage.

Conclusion

Deregulation of the airline industry, paired with lax antitrust enforcement, has created the current crisis in the airline industry. The elimination of price and entry and exit regulation unleashed

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[35] Dempsey, *supra* note 6.
[36] Delta Air Lines, *Delta 2024 Investor Day*, (2024), https://s2.q4cdn.com/181345880/files/doc_presentations/2024/Nov/20/2024-Delta-Investor-Day-vF-Website.pdf.
[37] Niraj Chokshi, *Coming to a Tiny Airport Near You: New Airlines*, THE NEW YORK TIMES, Dec. 25, 2024, https://www.nytimes.com/2024/12/25/business/avelo-breeze-small-airports.html (last visited Jan 6, 2025).

destructive competition in the airline industry, which severely destabilized the industry, degraded the experience of flying, cut access to air travel in middle America, and created worse conditions for the airline workforce. Subsequent lax antitrust enforcement has created the worst of all worlds: a highly monopolized industry that uses it market power to enrich CEOs and financiers at the expense of the public interest.

While recent DOJ and DOT efforts to address lax antitrust enforcement and the degraded passenger experience are welcome, no permanent solution to the ills of the airline industry is likely that does not involve at least some re-regulation. This includes reinstatement of the common carriage principles that traditionally applied to all forms of transportation to prevent discriminatory pricing and terms of service. Finally, to insure the long-term financial viability of an airline industry committed to equitably serving a broad range of public purposes, regulation is needed to ensure that well-run airlines providing reliable and efficient service are able to earn their cost of capital and deliver a fair return to their investors.