

**BEFORE THE
SENATE COMMITTEE ON COMMERCE,
SCIENCE AND TRANSPORTATION**

**FULL COMMITTEE HEARING ON
“S. 415: THE AIRLINE
COMPETITION RESTORATION ACT”
MARCH 13, 2001**

**TESTIMONY OF MARK KAHAN,
VICE CHAIRMAN, SPIRIT AIR LINES**

Chairman McCain, Senator Hollings, and Members of the Committee:

It has been almost five years since my first appearance on behalf of Spirit Airlines before this Committee to discuss competition in the airline industry, and the nation's successes and failures as the deregulation process has unfolded. I am honored to be here again today in support of the Aviation Competition Restoration Act, because it addresses many of the dangerous trends we have observed over those years. As Professor Michael Levine testified before you on Feb 1, 2001, the deregulation process is at a critical point.

First, Spirit Airlines would like to recognize the Committee's efforts over these last five years in promoting airline competition. In 1997, when I first testified here, no branch of government had a good understanding of the potential for predatory behavior in this industry, its tendencies toward concentration, or the intractability of its barriers to new entry. In 1997, Spirit had just finished a very difficult year. In 1996, Spirit was driven by its major hub competitor from the Detroit-Boston and Detroit-Philadelphia markets. We had no gates in Detroit and little prospect for obtaining them. Spirit had no access whatsoever to the High Density airports.

There has been progress in a number of areas. Last year, we carried almost 3 million passengers and our 1950 dedicated employees saved passengers in excess of \$300 million. Our two gates in Detroit became fully operational last year and serviced almost 500,000 of those passengers. In 2000 as well, as a direct result of this Committee's efforts, Spirit began service to Chicago's O'Hare airport. That service has been well received and, in just two days, will be expanded to

include Myrtle Beach, South Carolina. We began a very limited service from Reagan National Airport, which would have been completely impossible without the Chairman's efforts. And in New York City, a subleased gate became available at Newark and Air 21 slots became available at LaGuardia, permitting service throughout the day from both airports.

Spirit's progress has not always been smooth and we have encountered bumpy air from time to time. Our operations remain intensely constrained by a scarcity of facilities and slots at key airports. There are many examples, which I would be pleased to share with you and your staff. But much of Spirit's growth would have been impossible without this Committee's efforts and your continuous oversight has helped the public understand that airline deregulation cannot succeed unless barriers to entry are addressed by an intelligent public policy.

Of course, if all were rosy, we would not be sitting here today. One theme has been constant in every hearing over these past years-- the airline industry is concentrating to alarming levels. Far more carriers continue to exit the market than enter it, even without mergers. Although I believe that S. 415 can be improved in some ways as it goes through the legislative process, its fundamental premises are correct. S. 415 recognizes that barriers to entry and exclusionary conduct remain constant concerns and that concentration of the industry's real estate (gates) and its airspace (slots) in a few dominant carriers precludes truly competitive outcomes. With the proposed mergers of American and TWA, and United and US Airways (with American's participation), the long predicted concentration of the country's major airlines, covering 80% or

more of the entire national marketplace, toward three principal entities, has moved from a reasonable prediction to a substantial probability.

A second and related theme at each hearing is that we must seriously address congestion in the infrastructure supporting the airline industry if deregulation is to succeed. In 2000, congestion issues came to a head as DOT, despite good intentions, implemented Air 21 without sufficient regard for practicality. This led to total gridlock at LaGuardia airport, creating enormous problems for us and the travelling public.

Before addressing what needs to be done, however, a caution is in order about what we should not do. The goal of competition policy, whether expressed through legislation or the executive branch, should always be to promote and protect competition, not competitors. We say this often, but cannot overemphasize it. If a company has been through two bankruptcies and has been unable to earn a profit for a decade or longer, public policy should not prevent it from exiting the market. In fact, the marketplace is distorted when well-intentioned policy makers take actions designed solely to prop up such a carrier-- such as conferring two free slots from DCA to Los Angeles when that same carrier is already selling or leasing to other carriers the vast majority of slots it long ago received for free. Likewise, it is not totally unreasonable for the management of an extremely high cost carrier, which is steadily losing market share to others, to look for a way out in the interests of its shareholders and employees.

What is unreasonable is for the management of a high cost carrier to expect a merger solution that will result in a 100% stock premium primarily because the purchaser will gain control of congested airports through public assets that the acquired carrier previously obtained without charge. To the extent that the impetus for either of these mergers flows from monopoly power arising from conglomeration of public assets, government intervention such as that envisioned under S. 415 is certainly appropriate. Anti-trust analysis and remedies are important but not sufficient.

This legislation shines the spotlight on several problems that must be addressed. First, 15 years after it was issued, it is time to recognize that the "Buy-Sell" slot rule (14 CFR 93.221) has retarded rather than promoted competition. It is a major facilitator of both current mergers and a problem all by itself; even if the carriers left the market in the traditional manner, i.e., through bankruptcy and liquidation, the competitive outcome would be much the same because the resulting auction would see the airport assets likely going to the same incumbents.

The value of slots to carriers who are seeking to protect existing operations or thwart new entry will always be greater than their intrinsic value to a new entrant who must offer lower, competitive fares to penetrate the market. Since incumbent carriers also have the biggest checkbooks, there is no contest as to who gets access in these situations and, not surprisingly, concentration at slot controlled airports has steadily increased. Along with passage of S. 415, Congress should require DOT and FAA to take a hard look at this regulation and sunset it. And, for much the same reasons, I believe the Committee will be highly disappointed if an auction turns out to be the principal tool of slot allocation.

Second, there is a gap in federal law relating to gates at congested or hub airports. Control over gates has always been viewed as appropriately local. Neither Anti-discrimination provisions in the FAA's authorizing statutes, nor competitive impact requirements in PFC (passenger facility charge) administration, have provided effective tools to avoid concentration of scarce airport gates in the hands of a few dominant carriers. There is also considerable doubt that DOT's jurisdiction over unfair and competitive practices reaches these kinds of situations. DOT should have effective tools to deal with airport concentration issues on a regular basis and not only in the crisis of a proposed mega-merger or where there is extreme hub dominance. 49 U.S.C. 41712 could be amended to bring all gate transactions that increase concentration within DOT's discretionary authority. Refusals to deal by "have" carriers should be presumptively labeled as unfair and exclusionary practices.

Public policy that increases the availability of resources and the efficiency with which they are used is far superior to prescriptive regulation that merely deals with the negative effects of scarcity. We need to address the underlying problems of airport and airway congestion, which not only lead to these competitive distortions but also, as we are all aware, have seriously degraded service to the flying public in recent years. Before we can think in terms of congestion pricing, which, in principle, I wholeheartedly support, we must recognize that the current bias in airport pricing effectively subsidizes small airplanes. Current airport pricing practices, some of which are embedded in legislation, actively promote congestion. This is not, as popularly thought, a simple political struggle between the airlines and general aviation. This bias infects airline scheduling in a major way.

I recall sitting in the jump seat of one of Spirit's 164 seat MD-80s while we sat immobile on a LaGuardia taxiway waiting to cross some other taxiways and enter the alley where our gate is located. This was in November, at the height of the chaos. Before we could make a move, a parade of 10 turbo props and regional jets had to taxi by and clear the area. Recognizing that current "user charges" for airport facilities are basically the excise tax/segment fee and a weight-based landing charge, I did some basic arithmetic during the 45 minutes our 164 passengers waited to move the 150 yards to the gate. I concluded that our MD-80 passengers were contributing a minimum of \$2100 to infrastructure costs while the commuter passengers were paying, at most, about \$600. Consider, however, that there is little or no difference in infrastructure costs imposed by varying sizes of aircraft; the primary resource to be allocated is runway space and time and, if anything, smaller and slower planes impose more costs than larger aircraft. It follows that, at least at congested airports, a rational pricing system would assess infrastructure fees on a per plane basis. The only quick way to increase airport capacity is to encourage the use of larger aircraft and the discouraging truth is that we currently do the opposite.

In closing, I'd like to comment on DOT's role. S. 415 is to some degree self-executing and to some degree requires considerable administrative discretion by the Department. The previous Administration asked many of the right questions with respect to the state of aviation competition, increased the understanding of predatory pricing, and sought to move in the right direction. At the same time, DOT was hampered by a lack of resources and expertise. It dropped the ball entirely on some issues, such as CRS and the use of new entrant proprietary data by mega-carrier marketing departments. We at Spirit are heartened by the President's decision to name an

experienced and effective aviation legislator as Secretary. My mentor, Alfred Kahn, taught me one fundamental rule: regulate only if necessary, but if you must regulate, regulate well. Secretary Mineta has his work cut out for him. His declared intention to bring more rigor into the DOT's competitive analysis and recommendations to the Department of Justice are welcome. S. 415, the Aviation Competition Restoration Act, will not work well unless the Executive Branch is capable of doing its share. It is my hope that this Committee, along with the relevant Appropriations Committees, will take the steps necessary to ensure that the Secretary's intention becomes a reality.

Mr. Chairman, I will be pleased to answer any questions from the Committee or to provide any additional information that may be helpful.