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MESSAGE FROM THE CHAIR

On behalf of the Transportation Committee of the Section of Antitrust Law of the American Bar Association, I would like to welcome committee members and non-committee members to the re-designed version of our newsletter—The Transportation Antitrust Update. The Transportation Antitrust Update is a publication designed for all those interested in the antitrust developments and issues that arise in or are relevant to the airline, rail, shipping, and trucking industries.

This edition of The Transportation Update is highlighted by three articles dealing with timely subjects: (1) a recent Department of Transportation action dealing with terminal rents at LAX airport (by Roy Goldberg), the ongoing international cargo and fare investigations undertaken by the US Department of Justice and other national regulators (by Richard Snyder), and recent airline actions and initiatives at the Department of Transportation (by Andrew Steinberg and Naveen Rao). In addition to the articles, the newsletter provides updates on recent developments in the airline, rail, shipping, and trucking industries.

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DOT FINDS UNJUST DISCRIMINATION IN TERMINAL RENTS AT LAX

Roy Goldberg¹

In an unprecedented decision handed down on June 15, 2007, the U.S. Department of Transportation (DOT) sought to level the competitive playing field at Los Angeles International Airport (LAX) by vacating millions of dollars in new rental charges that unjustly discriminated against the mostly low-cost airlines at terminals 1 and 3.² The *LAX III* decision (*LAX I* and *II* were decided in the 1990's) was issued following a four-week trial before an administrative law judge in Los Angeles pursuant to a 13-year old statute³ that provides for an expedited trial of airline claims that airport fees are unjustly discriminatory or otherwise unreasonable. However, this was the first case under that statute in which the DOT ruled that the airport discriminated in fees charged to commercial airlines.

The case started when airlines at LAX terminals 1 (Southwest Airlines, US Airways and America West) and 3 (Alaska Airlines, AirTran, ATA, Frontier, and Midwest) filed a complaint with DOT on February 16, 2007, claiming that millions of dollars in new terminal rents grossly exceeded the rents charged competing airlines at terminals 2, 4-8 (including American Airlines, Continental Airlines, Delta Airlines, Northwest Airlines and United Airlines). In the first five years alone the rate differential—largely attributable to a new fee-setting methodology known as “rentable space” that solely burdened the terminal 1 and 3 carriers with the costs of common-use space in the terminals—would exceed \$220 million. LAX's operator—Los Angeles World Airports (LAWA)—defended the discrimination by pointing to the fact that the terminal 1/3 airlines' leases had

expired, while the terminal 2/4-8 airlines had long-term leases that remained in effect as long as December 2025.

Public Airports Not Normal Commercial Landlords

In ruling that the terminal rents were unjustly discriminatory, the DOT rejected LAWA's argument that the airport was a normal commercial landlord that could increase the rent charged an airline tenant whose lease has expired without consideration of the amounts paid by other airline tenants with unexpired leases. LAWA's effort to cast itself as a typical commercial landlord could not be squared with the “assurances” it gave to the Federal Aviation Administration (FAA) when it accepted federal funds for LAX projects. These “assurances” included the commitment to make LAX “available for public use . . . without unjust discrimination,” and to ensure that “air carriers making similar use of the airport . . . be subject to substantially comparable charges . . . for facilities directly and substantially related to providing air transportation.”⁴

LAWA did not even *attempt to argue* that the airport incurred higher costs to serve the terminal 1/3 airlines than the terminal 2/4-8 carriers. Furthermore, although LAWA claimed that the “circumstances” were different when the terminal 2/4-8 carriers entered into their long-term leases in the 1980's, it admitted that the airport made no attempt to link the increase in charges at terminals 1/3 to the debt obligations incurred by the airlines at terminals 2/4-8 for capital improvements to their terminals. Indeed, LAWA never sought to justify the amount of new



terminal charges by reference to the amount of investment that carriers in other terminals may have made in their terminals.

The complete absence of any linkage between the higher charges imposed on the terminal 1/3 airlines and the other terminals, and the actual costs at the respective terminals, was fatal to LAWA's defense of the disputed fees. As the applicable statute makes clear, "air carriers making similar use of the airport" must be "subject to substantially comparable charges" *unless* the difference in charges is "*based on* reasonable classifications . . ." ⁵ Thus, there must be a "classification" that is "reasonable," *and* the difference in airport charges must be "*based on*" that classification. As the DOT explained:

The grant assurance requires that differences in air carrier fees, terms, or conditions be reasonably related to the reasonable classifications undertaken by the airport proprietor. LAWA asserts that it may reasonably impose the rentable space methodology on carriers operating pursuant to a Tariff or a short-term lease since they are classified differently than carriers still serving the airport under long-term leases signed 20 years ago. LAWA, however, has not shown that the rentable space methodology is reasonably related to the carriers operating under a Tariff or short-term lease and therefore has not shown how it is justified in treating the T1/T3 Carriers differently than those in T2/T4-8. ⁶

The DOT further reasoned that LAWA had failed to show "any obligations undertaken by the airport, for example, that merit the additional fee imposition on the T1/T3 Carriers or, on the other hand, commensurate obligations undertaken by the T2/T4-8 Carriers that warrant their exclusion from the rentable space methodology." ⁷ "Rather,

LAWA simply justified the new methodology on the T1/T3 Carriers by explaining that its contractual commitments with the T2/T4-8 Carriers do not permit the rentable space methodology. That reason alone is not sufficient to impose a new fee methodology on one group of carriers and not another when they both make similar use of similar 'common space.'" ⁸

To defend its disparate treatment of the low cost carriers, LAWA cited to public utility case law for the proposition that the mere fact of a rate disparity between similarly situated parties does not establish unlawful rate discrimination where the rate disparity results from arms-length private contractual arrangements. In rejecting this argument, DOT stated that such cases were not directly on point. "For one, the airport grant assurance statute contains protections to airline users in addition to the 'unjust discrimination' safeguards that may not be afforded by the power and gas statutes." ⁹ "Second, unlike natural gas companies (which had needed stable supply arrangements for the health of the industry), airports rely not only on revenue generated by their long-term tenants but also on passenger facility charges, FAA grants, and concession revenues. Airports therefore are not as dependent upon a long-term customer as are natural gas companies." ¹⁰

LAWA also relied on several fixed base operator (FBO) cases which held that an airport had not engaged in unjust discrimination by offering more expensive lease terms to newer tenants. DOT found one such case inapposite because it "did not involve comparable leased premises, addressed minimal disparities in lease rates (2.5%)," and was brought by a tenant that "had agreed to the fees charged" under its lease. ¹¹ Another case "also involved a situation of distinctly different leased premises and obligations undertaken by the long-term lessee." ¹²



Not Every Rate Differential is Unjust

In *LAX III*, the DOT made it clear that “an airport proprietor does not engage in unjust discrimination *per se* by imposing different lease terms on carriers whose leases have expired”¹³:

Not every difference is unjust discrimination. For example, by retaining a long-term lease with one airline tenant and negotiating shorter term leases that may reflect increased costs with new entrants is allowable. An airport may lawfully impose reasonable classifications on air carriers and negotiate different terms of use and charges for such use with them. Indeed, an airport that finances its gates with passenger facility charges is in fact obligated to negotiate short term arrangements with the tenants of those gates. Furthermore, the FAA has found that an airport may reasonably assess fees on certain resident aircraft while not assessing fees on transient aircraft without engaging in unjust discrimination.¹⁴

However, “an airport proprietor may not impose a more burdensome fee structure on a new classification of airline user without demonstrating at least a reasonable correlation between the new fees and the airline classification.”¹⁵

Reaffirmation of the Prohibition Against Unjust Discrimination

For LAX and other public use airports that receive federal funds, the ruling in *LAX III* makes it clear that airline tenants cannot be charged significantly higher rents or fees merely because of different lease expiration dates. Rather, a material difference in airport rents must be tied to the actual differences in costs borne by the airport.

The decision reaffirms the prohibition against airports discriminating in the fees imposed on air carriers making similar use of the airport. Had the DOT accepted LAWAA’s argument that the circumstances and norms which exist in commercial leasing situations should apply in a public-use airport environment, it would have effectively removed the prohibition against unjust discrimination by airports. Unlike most commercial landlords, LAX and similar public use airports wield substantial market power over their airline users. Allowing an airport to dictate rates and terms based on a unilateral determination of what it claims is commercially acceptable would permit the airport to discriminate against airlines whose leases had expired. It would also render it difficult if not impossible for new entrant carriers to compete against entrenched airlines at the airport. The ultimate victims would be the traveling public, who would suffer from higher airfares, reduced air service, and the resulting loss of airline competition that inevitably follows from the discriminatory imposition of significantly higher airline costs.

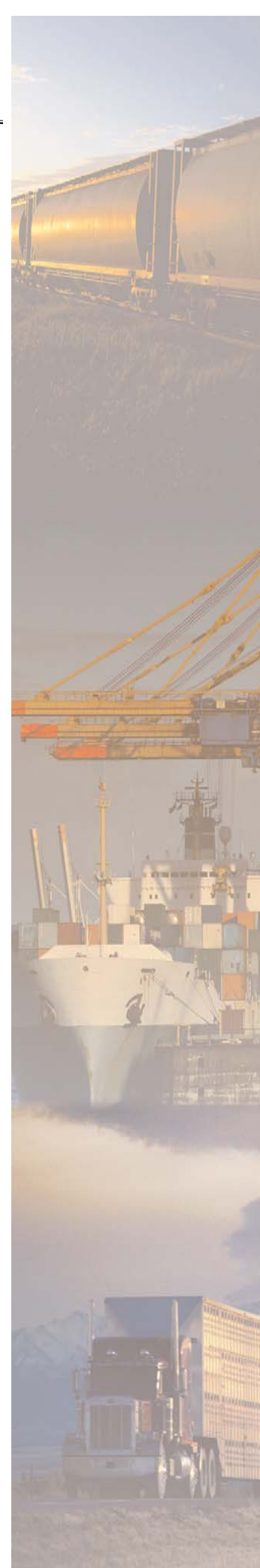
The City of Los Angeles has appealed the DOT’s ruling to the U.S. Court of Appeals for the D.C. Circuit.¹⁶

1 Roy Goldberg is a partner in the Washington, D.C. office of Sheppard Mullin Richter & Hampton LLP. Sheppard worked closely with in-house counsel for the terminal 1 and 3 airlines in representing those carriers in the “*LAX III*” litigation discussed in this article.

2 *Alaska Airlines v. L.A. World Airports*, Docket No. OST-2007-27331, 2007 DOT Av. LEXIS 437 (DOT June 15, 2007) (*LAX III*).

3 49 U.S.C. § 47129.

4 49 U.S.C. § 47107(a)(1), (2).



5 49 U.S.C. § 47107(a)(2)(B) (emphasis added).

6 *LAX III*, 2007 DOT Av. LEXIS 437, at *178-79.

7 *Id.* at *180.

8 *Id.*

9 *Id.* at *181.

10 *Id.*

11 *LAX III*, 2007 DOT Av. LEXIS 437, at*180.

12 *Id.* at *181.

13 *Id.* at *183.

14 *Id.*

15 *Id.* at *183-84.

16 The terminal 1 and 3 carriers have themselves appealed another aspect of the DOT decision which would permit airports, under certain circumstances, to use the purported “fair market value” of airport terminal space to set terminal rents for airlines.

