

2008

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Recommended Citation

Erin Shea, *Analysis of the Proposed Hub Carrier Slot Preference at Chicago O'Hare*, 73 J. AIR L. & COM. 611 (2008)

<https://scholar.smu.edu/jalc/vol73/iss3/6>

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ANALYSIS OF THE PROPOSED HUB CARRIER “SLOT” PREFERENCE AT CHICAGO O’HARE

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THE RIGHT TO USE a runway, or to take-off and land at an airport, is called a slot.¹ “*Slot* means the operational authority to conduct one IFR landing or take-off operation each day during a specific hour or 30 minute period at one of the High Density Traffic Airports.”² At certain airports with a capped number of slots, they are not only essential but also extremely valuable to airlines. Where slots are capped, “owning” a slot means that you can use the runway and your competitor cannot. At O’Hare International Airport, an airport with limited or capped slots, the airline industry is fighting over slot allocation. The current fight at O’Hare airport has important implications for the aviation industry, large hub carriers, small carriers (or limited incumbents and new entrants), and consumers. If hub carriers get a preference in slots at O’Hare, it could compel those carriers to continue to contribute to the airport’s multi-billion dollar expansion and may have implications for other airports looking to expand. If hub carriers do not get a preference, it may give new entrants a chance to compete (and smaller carriers a chance to expand) at one of the biggest airports in the country. And if this drives down prices, consumers will certainly take notice.

There could be even larger implications, too. If hub carriers lose the battle at O’Hare, their investment (billions of dollars) in the O’Hare expansion might be viewed as fruitless, and those airlines could withdraw support and put the expansion in jeopardy.

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¹ 14 C.F.R. § 93.213(a)(2) (2008).

² *Id.*

I. HISTORY AND USE OF LANDING SLOTS IN THE UNITED STATES

A. SLOTS GENERALLY NOT RESTRICTIONS

Most airports in the United States have operated and continue to operate without slot restrictions.³ In fact, save for a few highly congested airports, “first come-first serve” has been and is currently the U.S. system for allocating slots.⁴ Gate availability, terminal space, and air traffic management requirements limit the number of aircraft with rights to land at an airport.⁵ “The aircraft of airlines who have the rights to gates simply queue up on the taxi-ways and await their turn to take-off. Incoming aircraft are either stacked up overhead or delayed at their origination points.”⁶

Hence, slots traditionally had no value because limitations on a carrier’s ability to take-off and land came from other sources (air traffic management requirements and technical restrictions such as the availability of terminal gates).⁷ But the “first come-first serve” system became unworkable at highly congested airports. The Federal Aviation Administration (“FAA”) began instituting flight caps at these airports by managing and restricting slots.⁸ The FAA’s slot controls came in the form of the “high-density rule.”⁹

B. THE HIGH-DENSITY RULE: SLOT RESTRICTIONS

In 1968, congestion at several U.S. airports emerged as a problem demanding attention and intervention.¹⁰ The most congested areas were Chicago, New York, and Washington, spe-

³ Loan Le, George Donohue & Chun-Hung Chen, *Using Auction-Based Slot Allocation for Traffic Demand Management at Hartsfield Atlanta International Airport: A Case Study*, 2005, at 3, <http://catsr.ite.gmu.edu/pubs/AuctionPaperTRB2005.pdf>.

⁴ See Robert Hardaway, *Economics of Airport Regulation*, 20 TRANSP. L.J. 47, 60 (1991). But see Policy Regarding Airport Rates and Charges, 73 Fed. Reg. 3310 (Jan. 17, 2008) (proposing fee pricing which would use variable landing fees to encourage carriers to use runways at less congested times).

⁵ See Hardaway, *supra* note 4, at 60; Le, Donohue & Chen, *supra* note 3, at 3.

⁶ Hardaway, *supra* note 4, at 60.

⁷ See Le, Donohue & Chen, *supra* note 3, at 3.

⁸ John Sabel, *Airline-Airport Facilities Agreements: An Overview*, 69 J. AIR L. & COM. 769, 779 (2004).

⁹ *Id.*

¹⁰ See Dario Maffeo, *Slot Trading in the Reform of the Council Regulation (EEC) No. 95/93: A Comparative Analysis with the United States*, 66 J. AIR L. & COM. 1569, 1572 (2001).

cifically John F. Kennedy International Airport, LaGuardia Airport, Newark International Airport, Chicago O'Hare International Airport, and Washington National Airport.¹¹ To address the congestion at these airports and the corresponding discontent on the part of the carriers, passengers, and the federal government, the FAA proposed special rules that would apply to airports it designated as "high-density" airports.¹²

These rules proposed to limit the number of Instrument Flight Rule (IFR) operations (takeoff and landings) permitted per hour and to require that each operation be supported by a "slot." The FAA proposed to allocate the hourly IFR reservations or "slots" among three classes of users – scheduled air carriers (except air taxis), scheduled air taxis, and all other aircraft operators.¹³

In December 1968, the FAA adopted these restrictions, calling it the "high-density rule."¹⁴ The rule applied only to the high-density airports (John F. Kennedy, LaGuardia, Newark, Chicago O'Hare, and Washington National), but the FAA maintained that it would add overly congested airports to the high-density list if necessary.¹⁵

"In the preamble to the rule, the FAA advised that the rule should not be viewed as the permanent solution to the air congestion problem and that it would be kept under continuing review and modified as circumstances required or permitted."¹⁶ While the FAA amended the rule in February of 1969 and set an expiration date of December 31, 1969, the FAA was forced to extend it because congestion and delay persisted.¹⁷ While the rule was not extended to other airports, the FAA did remove Newark International Airport from high-density status in 1970.¹⁸ The rest of the high-density airports remained subject to restrictions.¹⁹ In 1973, the FAA finally announced that the slot restrictions at O'Hare, John F. Kennedy, LaGuardia, and Washington National would remain for an indefinite period.²⁰

¹¹ Eileen M. Gleimer, *Slot Regulation at High-Density Airports: How Did We Get Here And Where Are We Going?*, 61 J. AIR L. & COM. 877, 878 (1996).

¹² See *id.*; Maffeo, *supra* note 10, at 1572.

¹³ Gleimer, *supra* note 11, at 879.

¹⁴ High Density Traffic Airports, 33 Fed. Reg. 12,580 (Sept. 5, 1968).

¹⁵ Gleimer, *supra* note 11, at 878–79.

¹⁶ *Id.* at 880.

¹⁷ Maffeo, *supra* note 10, at 1573.

¹⁸ Gleimer, *supra* note 11, at 880.

¹⁹ See Maffeo, *supra* note 10, at 1573.

²⁰ Gleimer, *supra* note 11, at 880.

The high-density rule did not contain the specifics, and the FAA did not provide rules as to how the limited slots would be allocated beyond designating a set number for each of the three categories (scheduled air carriers, scheduled air taxis, and other aircraft operators).²¹ "In fact, the FAA expressly contemplated that the airlines would voluntarily reach decisions to reduce their schedules to the level required by the high-density rule and noted that the airlines were already discussing schedule changes pursuant to authority granted by the Federal Government."²² The carriers used Scheduling Committees to allocate slots among themselves and carriers desiring to operate at high-density airports.²³ Agreements reached by such committees were submitted for approval to the Civil Aeronautics Board ("CAB"),²⁴ which at the time had jurisdiction over the licensing of U.S. and foreign air carriers engaging in air transportation and related economic matters.²⁵ An approval by the CAB translated into antitrust immunity for carriers, and thus Scheduling Committees could negotiate without fear of liability.²⁶

The success of the Scheduling Committees dwindled with the Airline Deregulation Act of 1978.²⁷ "Because of the requirement that schedule changes be voluntary, the schedule changes could not be made unless there was unanimity among the affected carriers."²⁸ Clearly, unanimity was challenging when those on the Scheduling Committee were asked to grant a slot request to a competitor who would fly the same route at a discounted price.²⁹ Not only did the Scheduling Committees (purposely) act as a barrier to new entrants,³⁰ but the committee structure was not conducive to quick and efficient reaction to the market changes stemming from deregulation.³¹

²¹ Maffeo, *supra* note 10, at 1573.

²² *Id.* at 1574.

²³ Gleimer, *supra* note 11, at 881.

²⁴ *Id.*

²⁵ See 49 U.S.C. § 1382 (1988) (repealed and recodified at 49 U.S.C. § 41309 (2000)).

²⁶ Gleimer, *supra* note 11, at 881–82.

²⁷ Maffeo, *supra* note 10, at 1574.

²⁸ Gleimer, *supra* note 11, at 882–83.

²⁹ See *id.* at 882.

³⁰ See Sabel, *supra* note 8, at 780.

³¹ See Andrew B. Steinberg & James W. Tegtmeier, *Dealing with Airport Congestion: The Regulatory Challenge of Demand Management*, 19 AIR & SPACE LAW. 14, 15 (2005).

A fight over landing slots at Washington National Airport highlighted the problems associated with the Scheduling Committees.³² In 1980, New York Air planned to expand service by adding flights between Washington and New York.³³ The airline therefore requested twenty slots (spread out over peak hours) at Washington National and LaGuardia.³⁴ Not surprisingly, the Scheduling Committees were reluctant to hand over their slots to a competitor, and FAA intervention became necessary.³⁵ The FAA handed over eighteen of the twenty requested slots to New York Air by taking slots from other carriers.³⁶ Some of the carriers forced to give up their slots filed suit against the FAA.³⁷ But the court in *Northwest Airlines, Inc. v. Goldschmidt* upheld the FAA's action and stated that the slot reallocation was legitimate, procedurally sound, and with a rational basis.³⁸

Following the FAA intervention in Washington, the legitimacy and authority of Scheduling Committees came in to question.³⁹ As the FAA began making plans to address the confusion, the air traffic controllers' strike of 1981 demanded a shift in focus.⁴⁰

In order to face the air traffic paralysis caused by this strike, the FAA substituted the high-density rules with the National Air Traffic Control Contingency Plan. This later became known as the Interim Operation Plan, and through this, it was possible to enforce restrictions at twenty-two of the busiest airports, thus reducing the carriers' scheduled operations by twenty percent.⁴¹

During this time, the FAA tested a system whereby slots could be traded between carriers with FAA approval.⁴² After the forty-two day trial period, "248 slots were traded with a market price that varied from \$12,000 to \$500,000 per slot."⁴³

³² See Maffeo, *supra* note 10, at 1574.

³³ *Id.*

³⁴ *Id.*

³⁵ *Id.*

³⁶ *Id.*

³⁷ *Id.*

³⁸ *Id.* at 1574-75 (citing *Nw. Airlines, Inc. v. Goldschmidt*, 645 F.2d 1309, 1318 (8th Cir. 1981)).

³⁹ See *id.* at 1575.

⁴⁰ *Id.*

⁴¹ *Id.*

⁴² *Id.*

⁴³ *Id.* (citing U.S. DEP'T OF TRANSP. REPORT TO CONGRESS: A STUDY OF THE HIGH-DENSITY RULE 26 (1995)).

In 1984, the Interim Operation Plan restrictions were lifted, and the high-density rule came back into effect.⁴⁴ The same problems that existed before the air traffic controllers' strike still remained: congestion and inefficient Scheduling Committees.⁴⁵ But the success of the temporary slot trading did not go unnoticed, because Congress began considering ways to permanently incorporate slot trading into the high-density rule.⁴⁶

C. THE BUY-SELL RULE

In December 1985, the FAA adopted the "buy-sell rule" for slot trading.⁴⁷ The rule allowed air carriers and commuters to sell slots at the four high-density airports.⁴⁸ Unlike the trial rule, the buy-sell rule "permitted non-air carriers to hold slots—something which is significant for carriers wishing to use their slots as security as well as communities that may wish to ensure the preservation of service to a high density airport."⁴⁹ The most significant provisions of the buy-sell rule include the "grandfather clause," the exemption for essential services ("EAS") and international services, the "use it or lose it" provision, and lotteries for open slots.⁵⁰

First, the grandfather clause may have been the most controversial provision of the rule because it dealt with the means by which air carriers and commuters received the initial allocation of slots.⁵¹ It allocated slots to air carriers and commuters already holding permanent slots on December 16, 1985.⁵² Those on the losing end of the grandfather clause, primarily small carriers and new entrants, objected to the rule.⁵³ Their objections were based on the fact that those grandfathered in already had "economic and practical advantages."⁵⁴

The transportation department responded to this criticism by stating that such initial benefits were necessary in order to establish a buy-sell system and at the same time, minimize any difficulties that could affect service. In addition, the transportation

⁴⁴ *Id.*

⁴⁵ *See id.*

⁴⁶ *Id.* at 1575-76.

⁴⁷ *Id.* at 1576.

⁴⁸ *Id.*

⁴⁹ Gleimer, *supra* note 11, at 887.

⁵⁰ Maffeo, *supra* note 10, at 1576-77.

⁵¹ *See* Gleimer, *supra* note 11, at 890.

⁵² *Id.* at 887.

⁵³ Maffeo, *supra* note 10, at 1576.

⁵⁴ *Id.*

department claimed that the "grandfather clause" was in effect a recognition of the investment and commitment that these carriers had made in the past concerning personnel, equipment, communication networks, and planning.⁵⁵

Second, to counteract the windfall incumbents received under the grandfather clause and to create a pool of slots for new entrants and smaller carriers looking to expand, the FAA proposed a one-time five percent lottery.⁵⁶ O'Hare, LaGuardia, and Washington National carriers had to forfeit five percent of their slots, and all these slots went into a pool.⁵⁷ New entrants (carriers just entering the market) and limited incumbents (carriers with a limited amount of slots, which at O'Hare was less than eight slots) did not contribute to the pool.⁵⁸ Instead, the new entrants and limited incumbents were the beneficiaries of the pool slots.⁵⁹ Certain exemptions on slots that would be withdrawn from carriers were made for international flights and slots deemed necessary by the Department of Transportation for essential services (or service to remote areas).⁶⁰

The FAA set out procedures for the five percent withdrawal lottery.⁶¹ Importantly, the FAA mandated slots in peak hours be contributed so that favorable slots (throughout the day) would be available for new entrants and the limited incumbents.⁶²

Next, the buy-sell rule implemented a "use or lose" provision to open up slots for those seeking to enter or expand their market at the high-density airports.⁶³ The provision mandated carriers to use their slots for a minimum amount of time (initially sixty-five percent,⁶⁴ but the amount moved up to eighty percent), or they would lose their slot.⁶⁵

To monitor slot usage, the FAA required that reports be filed fourteen days after the end of each two month period, with the obligation to file the report imposed on the holder of the slot. If

⁵⁵ *Id.*

⁵⁶ Gleimer, *supra* note 11, at 890.

⁵⁷ *Id.*

⁵⁸ *See id.*

⁵⁹ *Id.*

⁶⁰ 49 U.S.C. §§ 41714(a)–(b) (2000).

⁶¹ *See* Special Slot Withdrawal and Reallocation Procedures, 51 Fed. Reg. 8632 (Mar. 12, 1986).

⁶² Gleimer, *supra* note 11, at 890.

⁶³ *Id.* at 889.

⁶⁴ *Id.* at 889 n.49.

⁶⁵ Maffeo, *supra* note 10, at 1577.

a review of these reports indicated that the minimum usage requirements were not met, the FAA could withdraw the slot.⁶⁶

The FAA maintained that the slots did not come with property rights and insisted that they could be withdrawn at any time by the FAA.⁶⁷ In fact, the high-density rule could be repealed (if congestion problems improved) and airlines would have no property loss claim for useless slots under their control.⁶⁸ In part, the FAA did not want airlines to think of the slots as containing property rights because it envisioned slots being put towards the most efficient use.⁶⁹ In other words, the FAA believed that airlines would return slots to the lottery if they were not being used or not being used efficiently.⁷⁰ However, the buy-sell rule worked better than the FAA had anticipated in creating a market for slots.⁷¹ Slots became valuable and no one wanted to hand them back to the FAA uncompensated.⁷²

The FAA retained ultimate control over the slots. It maintained that "[t]he FAA has the right to create, eliminate or withdraw slots for any reason unless they are allocated to essential services (EAS) or international services" (which were both outside of the high-density rule slot allocation system).⁷³ In order to deal with which slots would be used "to fulfill . . . EAS obligations, the FAA assigned by lottery withdrawal priority numbers to each slot."⁷⁴ Those small carriers who operated on a small number of slots did not have to participate in the withdrawal lottery.⁷⁵

⁶⁶ Gleimer, *supra* note 11, at 889.

⁶⁷ *In re McClain Airlines, Inc.*, 80 B.R. 175, 178 (Bankr. D. Ariz. 1987).

⁶⁸ *Id.*

⁶⁹ See *In re Gull Air, Inc.*, 890 F.2d 1255, 1258 (1st Cir. 1989) (stating the FAA's argument that "slots are not property of the carrier to which they are allocated, but rather operating privileges subject to absolute FAA control"); Hardaway, *supra* note 4, at 64 (stating that the FAA believed the slot market would "improve efficiency").

⁷⁰ See Hardaway, *supra* note 4, at 64-65.

⁷¹ See *id.* at 58-59.

⁷² See, e.g., *Gull Air*, 890 F.2d at 1257-58, 1260-61 (disallowing bankrupt airline to sell its slots for \$80,000 because the FAA had the authority to withdraw an airline's slots when it failed to comply with the FAA regulation mandating slots be used at least sixty-five percent of the time over a two-month period); *In re Braniff Airways, Inc.*, 700 F.2d 935, 942 (5th Cir. 1983) (finding that the FAA could recover slots from an airline that was in bankruptcy because the slots were not property of the bankruptcy estate).

⁷³ Maffeo, *supra* note 10, at 1576.

⁷⁴ Gleimer, *supra* note 11, at 888.

⁷⁵ *Id.*

D. THE SLOT MARKET CREATED BY THE BUY-SELL RULE

While the FAA maintained that slots were not property, slots became very valuable. The market value of slots varied greatly depending on "the airport, the time allocated, the season, the category of operators able to use it (air carriers or commuters), and other factors linked to availability of gates."⁷⁶ Other factors that might affect a slot's value include the size of the aircraft permitted in the slot and other operational restrictions such as noise abatement procedures.⁷⁷ Some reported sales from 1990–1991 include: twenty-one slots at O'Hare were sold to United Airlines for \$60 million; eight slots at LaGuardia were sold to USAir for \$6 million; American Airlines bought twelve LaGuardia slots and ten Washington National slots for over \$21 million; and Continental bought thirty-five slots at LaGuardia for \$54 million.⁷⁸ It has also been reported that slots have reached the two million dollar price range at both O'Hare and LaGuardia airports.⁷⁹ Such a high value makes sense given that United has reported that a slot worth \$2 million at O'Hare generates over \$5 million in revenue.⁸⁰

The FAA exercised little control over the sale, lease, and exchange of slots.⁸¹ For the most part, the FAA approved transactions so long as the administrative requirements were met.⁸² Such requirements included: (1) the slot was from the transferor's then-approved FAA base; (2) there was written evidence of the transferor's consent; and (3) the recipient had to refrain from using the slot until written confirmation had been received from the FAA.⁸³ While this information is maintained in FAA records, the commercial details of a sale or trade are not approved or tracked by the FAA.⁸⁴ Rather than using the FAA, airlines used the Air Transport Association (the U.S. airlines' trade association) as a broker or clearinghouse for slot exchanges.⁸⁵ Therefore, reports of sales were somewhat specula-

⁷⁶ Maffeo, *supra* note 10, at 1579.

⁷⁷ *Id.*

⁷⁸ *Id.* at 1580.

⁷⁹ *See id.* at 1579, 1580.

⁸⁰ Gleimer, *supra* note 11, at 901–02.

⁸¹ *See id.* at 897.

⁸² *Id.*

⁸³ 14 C.F.R. §§ 93.221(a)(2)–(4) (2008).

⁸⁴ Gleimer, *supra* note 11, at 903.

⁸⁵ Keith G. Debbage, *Airport Runway Slots: Limits to Growth*, 29 ANNALS OF TOURISM RES. 933, 940 (2002).

tive since information primarily came from other sources, such as reports to the Securities Exchange Commission or bankruptcy litigation.⁸⁶

The FAA's plan was that airlines would freely and voluntarily sell slots that they were not using, but it turned out that airlines were willing to hold on to slots no matter the cost.⁸⁷ Slots had more than the reported monetary value, because holding a slot was preventing a new entrant from competing; in effect, they gave slot holders a major competitive advantage.⁸⁸ Carriers still had to meet the use-or-lose requirements, but they did this by leasing out slots so that competitors could not gain permanent slots.⁸⁹ Carriers would "'park' excess air carrier slots with their affiliated commuter airlines or code-sharing partners to keep them out of the hands of their competitors."⁹⁰ One study by the Department of Transportation followed the dwindling slot market and found that sales between unrelated carriers fell "from 110 per quarter in 1986 to 28 per quarter in 1987 to 12 per quarter in 1988."⁹¹ The buy-sell rule was heavily criticized for making the large carriers stronger while making new entrants and smaller carriers weaker.⁹²

Congress reacted to the criticism in the 1994 FAA Reauthorization Act by allowing for slot exemptions for new entrants providing service to high-density airports (with the exception of Washington National).⁹³ Specifically, the Act authorized the Secretary of Transportation to grant an exemption for a new entrant carrier where the exemption was in the public interest and exceptional circumstances required it.⁹⁴ The requirement of exceptional circumstances proved to be an extremely high standard as very few exemption requests were granted.⁹⁵ The fact that a route was already in service by another carrier precluded a finding of exceptional circumstances.⁹⁶ In 1996, however, the Government Accountability Office ("GAO") delivered a report (that had been commissioned by the 1994 Reauthoriza-

⁸⁶ Gleimer, *supra* note 11, at 900-01.

⁸⁷ *Id.* at 907-08.

⁸⁸ *Id.* at 908.

⁸⁹ *Id.* at 910.

⁹⁰ *Id.*

⁹¹ Maffeo, *supra* note 10, at 1581.

⁹² Gleimer, *supra* note 11, at 910.

⁹³ See 49 U.S.C. § 41714(c) (2000).

⁹⁴ *Id.*

⁹⁵ Maffeo, *supra* note 10, at 1582.

⁹⁶ See *id.*

tion) entitled *Airline Deregulation: Barriers to Entry Continue to Limit Competition in Several Key Domestic Markets*.⁹⁷ Not surprisingly, the report found that the new carriers' inaccessibility to slots prevented them from entering the high-density airport markets.⁹⁸ The report criticized the Department of Transportation's unwillingness to grant exemptions through a narrow interpretation of the exceptional circumstances requirement.⁹⁹ The limited view taken by the Department of Transportation discouraged both market entry and applications for exceptional circumstances.¹⁰⁰

In response to the GAO report, the Department of Transportation stated that it would no longer use the narrow interpretation of "exceptional circumstances" and would construe the term in a way that encouraged competition.¹⁰¹ The Department of Transportation laid out guidelines for meeting the criteria. The new criteria would allow an exemption not only for applicants who would offer new, non-stop services that did not exist, but would grant an exemption where a carrier "demonstrated potential to offer low-fare competition [and there was only] a single carrier service and the market could support competition, or the existing carriers [did] not provide meaningful competition."¹⁰²

E. AIR-21

The Airline Deregulation Act of 1978 aimed to encourage competition in the airline industry and break down barriers to

⁹⁷ See U.S. GOV'T ACCOUNTABILITY OFFICE, GAO/RCED-97-4, AIRLINE DEREGULATION: BARRIERS TO ENTRY CONTINUE TO LIMIT COMPETITION IN SEVERAL KEY DOMESTIC MARKETS (1996).

⁹⁸ *Id.* at 2.

⁹⁹ *Id.* at 8.

¹⁰⁰ *Id.* at 9.

¹⁰¹ Maffeo, *supra* note 10, at 1583.

¹⁰² *Id.*

The first decision showing this new interpretation of the rule had been applied concerned a request by Frontier Airlines. The Department of Transportation recognized the need to introduce a new service and create competition with an incumbent service and more specifically a low cost service. The DOT judged that substantial benefits can be achieved through increasing competition at slot-constrained airports in situations where consumer would be able to obtain significantly lower fares in non-competitive or underserved markets.

entry.¹⁰³ However, it could not break down the slot system because there were not enough slots to go around; slots at high-density airports were extremely hard to obtain (even when buying through the buy-sell rule).¹⁰⁴

The Wendell H. Ford Aviation Investment Reform Act for the 21st Century ("AIR-21") was passed in April of 2000.¹⁰⁵ AIR-21 phased out the high-density rule (and slot restrictions) at LaGuardia, Kennedy, and O'Hare.¹⁰⁶ Slot restrictions were to be eliminated at O'Hare airport by July 1, 2002, and at the LaGuardia and Kennedy airports by January 1, 2007.¹⁰⁷ While Chicago and New York both anxiously awaited the AIR-21 slot expirations, they have yet to be completely eliminated.¹⁰⁸ While the high-density rule was phased out by AIR-21, congestion and delays at these historically crowded airports have meant that the FAA has had to continually keep tabs on these airports and allocate slots through flight caps.¹⁰⁹

II. A CONGRESSIONAL HUB CARRIER SLOT PREFERENCE AT O'HARE

To understand the current proposed rule for a hub carrier slot preference at O'Hare, it is important to first examine the background of the specific FAA rules instituted at O'Hare.

A. BACKGROUND TO THE DEVELOPMENT OF A HUB CARRIER PREFERENCE

1. *O'Hare's Design and Congestion*

O'Hare is a vital transportation link for the Midwest region, for North America, and for the world. It is the only airport in the United States that is the hub of two major airlines. Serving 47 scheduled passenger airlines and 23 cargo carriers, O'Hare pro-

¹⁰³ *Id.* at 1585.

¹⁰⁴ *Id.*

¹⁰⁵ *Id.* at 1586.

¹⁰⁶ *Id.* at 1587.

¹⁰⁷ *Id.*

¹⁰⁸ See Lorene Yue, *FAA Extends O'Hare Caps, Encourages Competition*, CHI. BUS., Aug. 23, 2006, <http://chicagobusiness.com/cgi-bin/news.pl?id=21824>; *Air Travelers Association Opposes Air Slot Restrictions, Slot Auctions, and Congestion Pricing Proposals, as the New York Aviation Rulemaking Committee Concludes Its Proceedings*, BUS. WIRE, Dec. 11, 2007, <http://allbusiness.com/government/government-bodies-of-fices-government/5329196-1.html>.

¹⁰⁹ See, e.g., *Congestion and Delay Reduction at Chicago O'Hare International Airport*, 71 Fed. Reg. 51,382, 51,386 (Aug. 29, 2006) (to be codified at 14 C.F.R. pt. 93).

vides nonstop service to 127 domestic and 48 international destinations. In part because Chicago is the largest population and economic center in the middle of the country, O'Hare "plays an important role in the National Airspace System (NAS) as a dual airline hub, a major mid-continent market for nearly every major airline, and a key international gateway."

O'Hare is not only one of the busiest airports in the world. Unfortunately, recently it has also become one of the most congested. Its delay record is at least twice as bad as that of the next two airports that suffer from excessive delays, Atlanta and Newark. Nearly 70,000 airport operations at O'Hare were delayed in 2004, for a total of almost 4,000,000 minutes. As the [O'Hare Modernization Act] states, "[t]he reliability and efficiency of air transportation for residents and businesses in Illinois and other [s]tates depends on efficient air traffic operations at O'Hare."¹¹⁰

Because most passengers at O'Hare are connecting to other airports, the effects of O'Hare's congestion are felt around the country and the world.¹¹¹ According to the FAA's Record of Decision, "O'Hare has consistently been the number one problem related to delays with the National Airspace System in the United States today."¹¹²

Much of its delay and congestion is blamed on O'Hare's poor runway design.¹¹³ The design contains an "outdated configuration of seven intersecting runways (which include a 'runway triangle' created by the three original intersecting runways that lie north of the present terminals) by creating six parallel and two crosswind runways."¹¹⁴ The intersecting runway design means that "the ability to use one runway is limited by whether an aircraft is using any of the others."¹¹⁵

2. *Slot Allocation in the Face of Congestion*

As previously discussed, O'Hare was designated a high-density airport when the high-density rule first came about in 1968.¹¹⁶ Although initially temporary, the rule was made permanent and went through significant changes after deregulation of the in-

¹¹⁰ St. John's United Church of Christ v. City of Chicago, 502 F.3d 616, 634 (7th Cir. 2007) (quoting O'Hare Modernization Act, 620 ILL. COMP. STAT. ANN. 65/5 (West 2003)).

¹¹¹ *Id.*

¹¹² *Id.*

¹¹³ *Id.* at 620.

¹¹⁴ *Id.*

¹¹⁵ *Id.*

¹¹⁶ Gleimer, *supra* note 11, at 878.

dustry.¹¹⁷ However, after the buy-sell rule was adopted in 1985, the next major change did not come until 2000. In 2000, Congress relaxed slot restrictions and made the following changes at O'Hare:

- (1) Beginning May 1, 2000, exemptions were granted to airlines to provide air service to small airports using aircraft with a seating capacity of less than seventy-one;¹¹⁸
- (2) New entrant or limited incumbent air carriers were granted thirty slot exemptions;¹¹⁹
- (3) Beginning May 1, 2000, slots were no longer required to provide international air service;¹²⁰
- (4) Beginning July 1, 2001, the slot control restrictions applied only between 2:45 p.m. and 8:14 p.m.;¹²¹ and
- (5) Slot restrictions were lifted entirely after July 1, 2002.¹²²

In phasing out the HDR, however, Congress recognized the possibility that there could be an increase in congestion and delays at the affected airports. Therefore, in the section that phased out the rule, it made clear that "[n]othing in this section . . . shall be construed . . . as affecting the Federal Aviation Administration's authority for safety and the movement of air traffic."¹²³

On July 1, 2002, the high-density rule phase-out at O'Hare went into effect and slot restrictions were lifted.¹²⁴ At first, congestion problems were kept at a minimum; however, this minimum is credited to the decrease in passenger travel subsequent to the September 11th terrorist attacks.¹²⁵ The lull in congestion did not last long. By 2003, O'Hare's hub carriers, American Airlines and United Airlines, added a large number of operations and re-timed other flights, which resulted in congestion and delay.¹²⁶ From April 2000 through November 2003, the hub carriers significantly increased the number of scheduled operations

¹¹⁷ *Id.* at 880.

¹¹⁸ 49 U.S.C. § 41717(b) (2000).

¹¹⁹ *Id.* § 41717(c).

¹²⁰ *Id.* § 41717(e).

¹²¹ *Id.* § 41717(a).

¹²² *Id.* § 41715(a).

¹²³ Congestion and Delay Reduction at Chicago O'Hare International Airport, 71 Fed. Reg. 51,382, 51,383 (Aug. 29, 2006) (to be codified at 14 C.F.R. pt. 93) (quoting 49 U.S.C. § 41715(b)(1)).

¹²⁴ *Id.*

¹²⁵ *Id.*

¹²⁶ *Id.* The report explains that "American increased its scheduled operations at O'Hare between the hours of 12 p.m. and 7:59 p.m. by nearly 10.5 percent. Over the same period, United increased its scheduled operations at O'Hare by over 41 percent." *Id.*

(by over fifty percent combined) but reduced their overall seat capacity.¹²⁷ This combination of more flights and less people on those flights translated into devastating congestion. "By November 2003, O'Hare had the worst on-time performance of any major airport."¹²⁸

Dealing with growing frustrations from passengers and carriers, Congress took action to reduce O'Hare delays in the form of 49 U.S.C. § 41722.¹²⁹ The statute:

[A]uthorized the Secretary of Transportation (Secretary) to request that scheduled air carriers meet with the FAA to discuss flight reductions at severely congested airports to reduce overscheduling and flight delays during hours of peak operation if the Administrator determines that it is necessary to convene such a meeting and the Secretary determines that the meeting is necessary to meet a serious transportation need or achieve an important public benefit.¹³⁰

Not surprisingly, in 2004 the Secretary of Transportation and the FAA Administrator found that such a meeting was necessary at O'Hare.¹³¹

However, meeting separately with agency officials beforehand, United and American voluntarily reduced their scheduled flights.¹³² This way, American and United could work out their schedules without subjecting themselves to unknown (and possibly more restrictive) regulation. Hence, the meeting was unnecessary, and the FAA issued an order implementing the agreed-

¹²⁷ *Id.* Regional jet operations of 375 per day were added by O'Hare's two hub carriers. *Id.*

Overall, American and United added over 600 regional jet operations per day. At the same time as they added regional jet operations, they reduced mainline jet operations. The result was actually a decrease in seat capacity by each carrier at O'Hare of more than 5.5 percent from April 2000 to November 2003 while flights increased by an average of 150 per day. In November 2003, more than 40 percent of American's and United's O'Hare flights were operated with regional jets, many to large and medium hubs.

Id.

¹²⁸ *Id.* O'Hare's arrivals were on time only 57% compared to the FAA goal of 82%. Departures were on time only 67% of the time compared to 85% at other major airports. *Id.*

¹²⁹ *Id.*

¹³⁰ *Id.*

¹³¹ *Id.*

¹³² *Id.*

upon reduction of five percent of scheduled operations during peak hours.¹³³

While the flight reductions did have an impact, it was not enough to ease the congestion at O'Hare.¹³⁴ Delays at O'Hare represented more than a third of all delays in the United States.¹³⁵ FAA officials began discussions with American and United to address the continued congestion.¹³⁶ As a result, both American and United agreed to additional schedule reductions to decrease delay and congestion.¹³⁷ The resulting order required:

[B]eginning no later than June 10, 2004, . . . (1) [an] additional schedule reduction of 2.5 percent of each carrier's total operations in the 1 p.m. through 7:59 p.m. hours including arrival reductions during specific times; (2) a reduction in the number of scheduled arrivals in the 12 p.m. hour; and (3) reductions to continue through October 30, 2004.¹³⁸

Before the additional 2.5% reduction went into effect, delays reached an all-time high of 14,495 in May 2004.¹³⁹ American's and United's compliance with the agreed-upon additional reduction in June eased delays somewhat, but not enough to satisfy the FAA.¹⁴⁰ At the heart of the problem was that American and United were the only parties to the agreed-upon reduction.¹⁴¹ Hence, other airlines had continued to add flights while the hub carriers cut their schedules.¹⁴² This fact made the hub carriers less willing to continue to make reductions.¹⁴³ Realizing they had reached an impasse, the Secretary of Transportation and the FAA Administrator called for scheduling the previously deferred reduction meeting.¹⁴⁴

¹³³ *Id.* Specifically, "this reduction was to be effective between 1:00 p.m. and 8:00 p.m. for six-months, beginning no later than March 4, 2004." *Id.*

¹³⁴ *Id.*

¹³⁵ *Id.*

¹³⁶ *Id.*

¹³⁷ *Id.*

¹³⁸ *Id.* (citing Operating Limitations at Chicago O'Hare Int'l Airport, Docket FAA-2004-16944-3 (2004)).

¹³⁹ *Id.*

¹⁴⁰ *Id.*

¹⁴¹ *Id.*

¹⁴² *Id.* at 51,383-84.

¹⁴³ *Id.* at 51,384.

¹⁴⁴ *Id.*

On August 4, 2004, the meeting between the Department of Transportation and the carriers convened.¹⁴⁵ The meeting resulted in further flight reductions by United and American and slight increases for new entrants and limited incumbents.¹⁴⁶ United and American agreed to reduce arrivals by about 5% during peak hours, bringing their total agreed flight reductions to 12.5% each.¹⁴⁷ Based on information obtained through the meetings, the FAA issued a comprehensive order that lowered the maximum number of landing slots from 120 to 88 per hour throughout most of the day.¹⁴⁸ The flight caps went into effect "in November 2004 on a temporary basis [but were] extended three [more] times to alleviate congestion at O'Hare."¹⁴⁹

The Final Rule (the third extension of the O'Hare flight caps) was issued on August 29, 2006.¹⁵⁰ The rule went into effect October 29, 2006, and is scheduled to terminate on October 31, 2008,¹⁵¹ at which point the new runway under the O'Hare Modernization Plan should be available "to accommodate more than 50,000 additional forecast operations annually."¹⁵²

The rule restricted arrivals from 7:00 a.m. through 8:59 p.m. on weekdays and from noon through 8:59 p.m. on Sundays.¹⁵³ The number of arrival slots during those periods was cut to eighty-eight per hour and to fifty during each thirty-minute period from 7:00 a.m. through 7:59 p.m.¹⁵⁴ The rule allowed increased slots (ninety-eight) between 8:00 p.m. and 8:59 p.m. Monday through Friday and Sunday, with the fifty-per-half-hour limitation applying.¹⁵⁵ The FAA also retained the "use or lose" provision requiring airlines to use slots eighty percent of the time or lose them.¹⁵⁶

¹⁴⁵ *Id.* According to the report, the meetings were conducted with each carrier separately for antitrust reasons. *Id.*

¹⁴⁶ *Id.*

¹⁴⁷ *Id.*

¹⁴⁸ *Id.*; Yue, *supra* note 108.

¹⁴⁹ Yue, *supra* note 108. See also Congestion and Delay Reduction, 71 Fed. Reg. at 51,384.

¹⁵⁰ Congestion and Delay Reduction, 71 Fed. Reg. at 51,382.

¹⁵¹ 14 C.F.R. § 93.21 (2008).

¹⁵² *FAA Imposes Final Slot Rule at Chicago O'Hare*, ATW ONLINE, Aug. 24, 2006, <http://atwonline.com/news/story.html?storyID=6183>.

¹⁵³ 14 C.F.R. §§ 93.23(a)(1), (a)(2).

¹⁵⁴ *Id.* § 93.23(1).

¹⁵⁵ *Id.* § 93.23(2).

¹⁵⁶ *Id.* § 93.31(a).

The rule also gave a slot preference to new entrants and limited incumbents in order to promote competition at O'Hare.¹⁵⁷ The rule specified that if O'Hare is able to add one or more flights per hour (above the eighty-eight slot cap) without causing delays, those landing rights would go to new entrants or incumbents first.¹⁵⁸ The eighty-ninth and ninetieth flight slots would be awarded via a lottery system to new entrants or limited incumbents (those with eight or fewer arrivals per day).¹⁵⁹ Slots for the ninety-first flights and beyond, should the FAA allow them, would be awarded via lottery to current airlines operating out of O'Hare.¹⁶⁰

The FAA estimated that the Final Rule would reduce delays at O'Hare by thirty-two percent, generate \$475.6 million in savings through 2008 (including \$212.7 million for airlines), and cost less than \$1 million.¹⁶¹

United Airlines, American Airlines, the city of Chicago, and members of the Illinois Congress had lobbied the FAA to open any new capacity at O'Hare to any carrier because awarding it only to new or small carriers "created a disincentive for the airport's two [hub] carriers to invest in capacity improvements."¹⁶² However, consumer advocates lauded the FAA for its pro-competition stance. One editorial supported the FAA rule:

United and American control 83% of the flights at O'Hare. And while they lost more flights than others when the caps took effect two years ago, the limits also cemented their hold on the airport. Carriers like JetBlue, which might offer passengers more flight options and lower fares, were boxed out or prevented from expanding.¹⁶³

3. *Promise of Expansion: The O'Hare Modernization Plan*

In 2001, the U.S. Senate Commerce, Energy, and Transportation Committee held hearings to examine the congestion and delays at O'Hare and the subsequent ripple effect it had on na-

¹⁵⁷ See Congestion and Delay Reduction at Chicago O'Hare International Airport, 71 Fed. Reg. 51,382, 51,388 (Aug. 29, 2006) (to be codified at 14 C.F.R. pt. 93).

¹⁵⁸ 14 C.F.R. § 93.30(h).

¹⁵⁹ *Id.* § 93.30(c).

¹⁶⁰ *Id.* § 93.30(d).

¹⁶¹ Congestion and Delay Reduction, 71 Fed. Reg. at 51,398.

¹⁶² Yue, *supra* note 108.

¹⁶³ Editorial, *FAA Rule Rightly Promotes O'Hare Competition*, CHI. BUS., Aug. 28, 2006, <http://www.chicagobusiness.com/cgi-bin/mag/article.pl?id=26375>.

tionwide aviation delays.¹⁶⁴ "During the course of these hearings, the Committee strongly hinted that if the City of Chicago and the State of Illinois did not reach a decision on airport expansion before September 1, 2001, Congress would likely intervene."¹⁶⁵

Soon after the hearings, the city announced a plan to expand O'Hare known as the O'Hare Modernization Program ("OMP").¹⁶⁶ "The OMP proposed to correct some of the inefficiencies created by the airfield's outdated configuration of seven intersecting runways."¹⁶⁷ "On December 5, 2001, the Mayor of Chicago and the Governor of Illinois announced that they had reached an agreement on the central components of the proposed OMP."¹⁶⁸

Under the OMP, O'Hare's existing seven runways will be reconfigured into a more modern parallel layout and a new west terminal with additional gates will be added.¹⁶⁹ The OMP will cost a projected \$6.6 billion (in 2001 dollars) to be funded by Passenger Facility Charges, General Airport Revenue Bonds, Federal Airport Improvement Program funds, and, of course, O'Hare's two major hub carriers.¹⁷⁰ The hub carriers, American and United, have already committed to pay \$2.9 billion for phase one of the O'Hare project.¹⁷¹ While the carriers said that they would not commit more funds until the first two runways open in October of 2008, the carriers have entered into phase two funding discussions with OMP officials.¹⁷² Phase two is now expected to cost more than \$4 billion (in 2007 dollars).¹⁷³

The O'Hare Modernization Plan is designed to incrementally increase capacity starting in 2008.¹⁷⁴ The addition of the first

¹⁶⁴ See *St. John's United Church of Christ v. City of Chicago*, 502 F.3d 616, 620 (7th Cir. 2007).

¹⁶⁵ *Id.*

¹⁶⁶ *Id.*

¹⁶⁷ *Id.*

¹⁶⁸ *Id.*

¹⁶⁹ Aaron Karp, *Ryan & Daley Agree on O'Hare Expansion & New Airport*, AIR TRANSP. INTELLIGENCE, Dec. 6, 2001; O'Hare Modernization Program, Learn About OMP, <http://tinyurl.com/6lhvap> (last visited Aug. 15, 2008).

¹⁷⁰ Learn About OMP, *supra* note 169. See also Greg Hinz, *A New Push at O'Hare*, CHI. BUS., Nov. 12, 2007, <http://chicagobusiness.com/cgi-bin/news.pl?id=27089>.

¹⁷¹ Hinz, *supra* note 170.

¹⁷² *Id.*

¹⁷³ *Id.*

¹⁷⁴ Congestion and Delay Reduction at Chicago O'Hare International Airport, 71 Fed. Reg. 51,382, 51,384 (Aug. 29, 2006) (to be codified at 14 C.F.R. pt. 93).

new runway in 2008 is projected to allow for “over 50,000 additional forecast operations with an average annual delay per aircraft no higher than exists today.”¹⁷⁵ In 2010, OMP expansion is forecasted to increase by 90,000 operations “with a decrease in average annual delay per aircraft of approximately 33% below today’s delay per aircraft at O’Hare.”¹⁷⁶ The final phase, to be completed in 2013, is expected to “accommodate approximately 1.12 million annual forecast operations (an increase of more than 140,000 annual operation[s] over today’s activity level) with an average annual delay per aircraft nearly 70% below today’s delay per aircraft.”¹⁷⁷

On September 30, 2005, the FAA approved the revised Airport Layout Plan and other federal actions related to the implementation of the OMP.¹⁷⁸ Despite the initial slowdown stemming from an injunction preventing the OMP from acquiring land necessary for the runway expansion,¹⁷⁹ the injunction has been thrown out and the O’Hare expansion is now on track.¹⁸⁰ With the new expansion getting closer to reality, the fight for additional slots has already begun.¹⁸¹

B. A HUB CARRIER SLOT PREFERENCE

In September 2007, the U.S. House Committee on Transportation and Infrastructure released House Report 331 explaining the 2007 FAA Reauthorization (House Bill 2881), which has passed in the House and is now pending in the Senate.¹⁸² Representative Jerry Costello (D-IL) inserted bill language into the report directly addressing O’Hare flight caps and, more importantly, who should get preference on landing slots once O’Hare expands and the flight caps are lifted.¹⁸³ The bill language is not binding on the agency; however, it could influence the FAA

¹⁷⁵ *Id.*

¹⁷⁶ *Id.*

¹⁷⁷ *Id.*

¹⁷⁸ *Id.* at 51,397.

¹⁷⁹ See *St. John’s United Church of Christ v. City of Chicago*, 502 F.3d 616, 621 (7th Cir. 2007).

¹⁸⁰ See Hinz, *supra* note 170.

¹⁸¹ See *id.* See also H.R. REP. NO. 110-331, at 115 (2007).

¹⁸² GovTrack Bill Status of H.R. 2881: FAA Reauthorization Act of 2007, <http://www.govtrack.us/congress/bill.xpd?bill=h110-2881> (last visited Aug. 29, 2008).

¹⁸³ Paul Merrion, *UAL, American Muscle Out O’Hare Competition*, CHI. BUS., Oct. 20, 2007, <http://chicagobusiness.com/cgi-bin/news.pl?id=26833>.

in interpreting the rule in that it provides evidence of legislative intent.¹⁸⁴

The first part of the report language expresses the Committee's dislike of caps at O'Hare and pushes the FAA to focus its efforts on long term expansion.¹⁸⁵ It states:

The Committee believes that the cap on flights currently placed on O'Hare International Airport is a short-term solution to manage congestion and delay until enhancements from the O'Hare Modernization Plan ("OMP") begin to come on-line. To mitigate congestion and expand capacity at O'Hare International Airport, the Committee believes the FAA should implement long term solutions that utilize the increased capacity and benefits expected from the OMP.¹⁸⁶

The next part specifically addresses the need for a hub carrier preference and reasons why such preference should be given to hub carriers (American and United) based on their prior voluntary flight reductions.¹⁸⁷ It states:

Further, as new capacity becomes available at O'Hare International Airport, preference should be given to hub carriers, given that they temporarily agreed to a 12.5 percent reduction in their peak-hour schedules to reduce congestion in 2004, and little has been done to restore or redistribute capacity to accommodate for that voluntary reduction.¹⁸⁸

American Airlines and United Airlines are obviously pleased with the report language granting them a preference for additional slots created by the OMP.¹⁸⁹ An American spokesperson was quoted as saying, "This [provision] would ensure that before new entrants or other carriers were granted more capacity, we would be made whole again."¹⁹⁰ In addition to the provision serving as a sort of restitution for previous flight reductions, American and United have also argued that they should receive preference on new runway space because they have paid for most of the expansion.¹⁹¹

The other O'Hare airlines, as well as many consumers, are not happy about the report language granting the two already-domi-

¹⁸⁴ *Id.*

¹⁸⁵ H.R. REP. NO. 110-331, at 115.

¹⁸⁶ *Id.*

¹⁸⁷ *Id.*

¹⁸⁸ *Id.*

¹⁸⁹ See Merrion, *supra* note 183.

¹⁹⁰ *Id.*

¹⁹¹ Hinz, *supra* note 170.

nant carriers preference over additional slots.¹⁹² Many had envisioned the expansion as translating into a chance for discount airlines to enter the O'Hare market and drive prices down.¹⁹³ A Chicago editorial expressed the frustration stating, "[W]e consider [the provision] blatantly unfair to the 38 million travelers who use O'Hare every year. Allowing United and American to keep control of O'Hare would rob travelers of a key potential benefit of the expansion—price competition."¹⁹⁴

While the FAA Reauthorization Bill has yet to go before the Senate, U.S. Senator Richard Durbin (D-IL) is reported to be sympathetic to American and United's argument that they should receive preference for new runway space.¹⁹⁵ It is possible that he could push the Senate to amend the FAA Reauthorization to include the O'Hare hub carrier slot preference.¹⁹⁶

III. SLOT ALLOCATION THEORIES

A. HOW WOULD A RUNWAY PREFERENCE WORK?

The language in House Report 331 directs only a result that "preference should be given to hub carriers,"¹⁹⁷ and provides absolutely no guidance on how the FAA would go about obtaining such a result. This begs the question, "How would such a preference work?"

The default at non-slot controlled airports (which is most airports) is the "first come-first served" method where those with landing rights simply wait their turn. Such a system has proven entirely unsuccessful in the past at O'Hare. But, if the FAA stays true to its word and lifts the caps at O'Hare in October 2008 (and the Congressional Report seems to urge that the FAA follow through in doing so by saying that short term caps are not a solution), then it is possible that O'Hare would revert to this system. Under this system, however, a preference of any kind is unworkable because the whole system is based on "first come-first served." Since the size of an airplane makes it impossible to simply jump to the head of a runway line, it seems that the

¹⁹² See Merrion, *supra* note 183. According to the Bureau of Transportation Statistics (June 2006–June 2007), eighty-four percent of O'Hare's passengers are flying on United, American, or their regional jet partners. *Id.*

¹⁹³ See *id.*

¹⁹⁴ Editorial, *Travelers Lose if UAL, AA Control O'Hare*, CHI. BUS., Oct. 29, 2007, <http://chicagobusiness.com/cgi-bin/mag/article.pl?id=28698>.

¹⁹⁵ Merrion, *supra* note 183.

¹⁹⁶ *Id.*

¹⁹⁷ H.R. REP. NO. 110-331, at 115 (2007).

House Committee Report's insertion of a hub carrier preference implies that some sort of slot control will be necessary at O'Hare subsequent to the runway expansion. Several different slot allocation methods could be employed.

1. *High-Density Rule Allocation*

Under the high-density rule, the initial allocation of rights was doled out based on the slots airlines were already using. The FAA simply made an administrative determination of how many slots each airline was entitled to and made the allocation. Slots were not bought or sold, they were not auctioned off, and there was no lottery to determine allocations.

The high-density rule was and is extremely disliked by the airlines—both small carriers who are not able to expand under it and larger hub carriers who are forced to reduce flights. No one seems to be in favor of reverting back to a high-density rule system, but it seems that the Congressional Report most closely resembles an allocation similar to that under the high-density rule. Under the high-density rule, allocations came without payment but simply because airlines had used the slots in the past, and here the argument is that the hub carriers should get a preference (presumably, in this situation, without payment) because they had the rights in the past.

2. *Auctions/Open Market*

Another way of allocating slots is to simply let the free market sort things out: airlines bid on slots and the slots go to the highest bidders. While this is seemingly an efficient allocation of resources, analysts do not agree on whether an auction allocation works in practice. "Some argue that a market system puts slots to their highest valued use."¹⁹⁸ However, others argue that because having rights to a slot necessarily deprives a competitor airline of using the slot and competing in the market, it behooves larger airlines to maintain rights to slots even if they do so at a loss.¹⁹⁹ One analyst demonstrates how a misallocation can occur in an auction/open market situation:

If a larger firm outbids a smaller firm for a slot or refuses to sell at marginal cost, the following results occur: 1) a barrier to entry is created, and the incumbent firm will face a more steeply declining demand curve, thus enabling it to set prices at a profit-

¹⁹⁸ See Hardaway, *supra* note 4, at 66.

¹⁹⁹ See *id.* at 65.

maximizing and misallocative level above marginal cost (but equal to marginal revenue), and 2) large firms will, in order to avoid losing a slot under the "use it or lose it" clause of the "buy-sell" rule, use that slot for a lower valued flight even if it does not cover variable costs; it will do so in order to preserve the oligopoly premium for its other flights. The result is a misallocation of slot resources.²⁰⁰

While larger carriers embrace the idea of an open market where slots could be easily purchased, their admiration for this system likely stems from the fact that it allows them to control the market: they can pay more for slots (even those they do not need) and prevent competitors from obtaining slots necessary for competition. While American and United would likely embrace this system if it were to be implemented after the O'Hare expansion, the FAA would be unlikely to relinquish all control of the slot system.²⁰¹ Additionally, as stated above, the House Committee Report language of a hub carrier preference presumes that there will be control over slots. In a free market system, the FAA would be out of the picture and not granting preferences to any airline.

3. *Lottery*

Under the buy-sell rule of 1986, five percent of slots were to be forfeited by large carriers and placed in a pool from which new entrants could obtain slots. That five percent pool was to be allocated by lottery. While this sort of system made sense in a post-airline-deregulation world, where many new entrants were coming into the airline industry, it does not make sense when a preference is to be given only to hub carriers. Because there would only be two airlines in the pool, any attempt to employ a lottery would essentially be similar to an administrative determination under the high-density rule.

4. *Scheduling Committees*

As discussed above, Scheduling Committees were used prior to deregulation of the airline industry. The Committees reached decisions through unanimous decision-making. This unanimity, however, became impossible after deregulation.

²⁰⁰ *Id.*

²⁰¹ See Congestion and Delay Reduction at Chicago O'Hare International Airport, 71 Fed. Reg. 51,382, 51,389 (Aug. 29, 2006) (to be codified at 14 C.F.R. pt. 93).

While Scheduling Committees are widely used in Europe,²⁰² such a system would be extremely difficult to reinstitute. And, because preferences would be impossible to implement within a decision-making body made up of competitors, this is certainly not the slot allocation method contemplated in the House Committee Report language.

B. ARGUMENTS SUPPORTING HUB CARRIER PREFERENCE

1. *Property Right*

The first argument a supporter of a hub carrier preference at O'Hare would put forth is that slots are property.²⁰³ The O'Hare hub carriers would thus be able to claim a property right in the slots they had given up in order to reduce congestion. Important to this argument would be a recognition that the slots the hub carriers "voluntarily" gave up were actually forced from the carriers under threat of a scheduling meeting (resulting in an unknown FAA ruling).²⁰⁴

While the FAA has insisted that slots are not property, there are several bankruptcy cases holding that slots do constitute property despite the FAA's disclaimer.²⁰⁵ For example, the court in *In re McClain Airlines, Inc.* held that slots are property.²⁰⁶ In that case, McClain Airlines had received eight arrival and departure slots at O'Hare, but the airline went bankrupt shortly after going into business due to certification difficulties.²⁰⁷ The FAA claimed that during the course of the airline's business, it failed to meet the "use or lose" requirement (then requiring a minimum use of sixty-five percent), but the debtor refuted that he failed to meet the "use or lose" requirement and claimed the slots as property.²⁰⁸ The *McClain* court held that the FAA's claim that slots are not property is not determinative because the aim of the buy-sell rule ("to 'minimize government intervention' and provide 'maximum reliance on market forces to deter-

²⁰² Ian Jones, Ivan Viehoff & Phillipa Marks, *The Economics of Airport Slots*, 14 FISCAL STUD. 37, 40-41 (1993).

²⁰³ See Maffeo, *supra* note 10, at 1578; Gleimer, *supra* note 11, at 902-07.

²⁰⁴ See Congestion and Delay Reduction, 71 Fed. Reg. at 51,383.

²⁰⁵ See generally *In re McClain Airlines, Inc.*, 80 B.R. 175 (Bankr. D. Ariz. 1987); *In re Am. Cent. Airlines, Inc.*, 52 B.R. 567 (Bankr. N.D. Iowa 1985).

²⁰⁶ *McClain Airlines*, 80 B.R. at 179.

²⁰⁷ *Id.* at 176-77.

²⁰⁸ *Id.* at 177.

mine slot distribution'") is not reconcilable with the contention that freely traded slots do not constitute property.²⁰⁹

In addition to bankruptcy courts' recognition of a property right in slots, financial institutions' use of slots as collateral demonstrates a recognition of a property interest.²¹⁰ While a prudent creditor will supervise such an arrangement closely (and monitor "use or lose" provisions), a slot's value as security demonstrates that it is treated as having a property right.²¹¹

Finally, the reality is that slots are very valuable. There is a slot market, and slots have been bought and sold for upwards of a million dollars.²¹² Even if the FAA denies that there is a property right, it is clear that there is some sort of claim to a slot. In *In re Gull Air, Inc.* (later overturned by the First Circuit Court of Appeals), the judge described Gull's claim in a slot:

[P]ressed to the wall, (Gulls' slot) would be a property right. But I don't know that I have to find that it is a property right in its total sense. It's a license in which the debtor has a proprietary interest since the regulation gives the debtor the privilege to sell it.²¹³

While a landing slot has characteristics of a property right, even if it is not classified as such, the benefits of a hub-and-spoke system can be used to justify a hub carrier preference.

2. *Benefits Stemming from Hub-and-Spoke System*

Today the hub-and-spoke system is the dominant system in U.S. airports.²¹⁴ Under this system, airlines pick up passengers at smaller spoke cities and fly them to a main airport (the hub).²¹⁵ The advantage of this system is that passengers, whether located at the hub or at a spoke, can easily access a wide range of destinations.²¹⁶ For the spoke city passenger, the hub system provides access to more routes, because the passenger

²⁰⁹ *Id.* at 179.

²¹⁰ See Gleimer, *supra* note 11, at 902-07.

²¹¹ *Id.*

²¹² *Id.* at 900-03.

²¹³ *In re Gull Air, Inc.*, 890 F.2d 1255, 1257 (1st Cir. 1989) (emphasis omitted); see also I.R.S. Gen. Couns. Mem. 39,606 (Feb. 8, 1987) (treating landing slots as a government license for income tax purposes).

²¹⁴ *Airline Competition: Clear Skies or Turbulence Ahead?: Hearing Before the S. Subcomm. on Antitrust, Business Rights, and Competition*, 106th Cong. 38 (2000) [hereinafter *Hearing*] (statement of Donald J. Carty, Chairman, President, and CEO, American Airlines).

²¹⁵ See Sabel, *supra* note 8, at 775.

²¹⁶ *Hearing*, *supra* note 214, at 35.

can get to a hub and have his or her pick of destinations from the hub.²¹⁷ Also, at one hub there are usually many airlines (all connecting to their own hub city); thus, competition in the spoke cities keeps a check on prices.²¹⁸ As Donald J. Carty, the (now former) Chairman, President, and CEO of American Airlines stated while testifying in front of the Senate Antitrust Subcommittee regarding the hub-and-spoke system:

For passengers living in hub cities, the hub and spoke system provides frequent service, numerous nonstop destinations and vigorous competition. For all the talk about the alleged evils of hubs, nearly every city in America would love to be one. Hub-originating passengers enjoy non-stop service to scores of destinations—far more service in terms of both frequency and destinations than the local population could support without the “feed” traffic from other cities.²¹⁹

While Chicago O'Hare certainly does offer various routes, there are also studies demonstrating that prices at O'Hare are not increased due to its status as a hub. First, O'Hare is the only hub airport with two (rather than one) hub carriers, which means that the airlines must compete against one another for fares.²²⁰ Another study found that Chicago O'Hare has the “second highest penetration of low fare carriers out of 11 major hub cities and it also has the lowest weighted average fare of any of the 11 major hub cities examined.”²²¹

A hub-and-spoke system also has the very important benefit of contributing to the local economy. With a hub airport comes not only jobs, but a carrier that is invested in the local airport and its success. The hub carriers are essential to the O'Hare expansion and are contributing much of the \$6.6 billion bill (in 2001 dollars).²²²

²¹⁷ *Id.*

²¹⁸ *Id.* at 35–36.

²¹⁹ *Id.*

²²⁰ *O'Hare Soon to Be Last Dual Hub for Major Carriers*, AIR TRAFFIC CONTROL ASS'N NEWS, Jan. 19, 2005, http://www.atca.org/singlenews.asp?item_ID=2174&comm=0.

²²¹ See Congestion and Delay Reduction at Chicago O'Hare International Airport, 71 Fed. Reg. 51,382, 51,389 (Aug. 29, 2006) (to be codified at 14 C.F.R. pt. 93).

²²² Learn About OMP, *supra* note 169.

C. ARGUMENTS AGAINST HUB CARRIER PREFERENCE

1. *No Property Right*

In arguing against a hub carrier preference, one would assert that hub carriers have no property interest in slots that they gave up or that they were initially given (by “grandfathering” in their slots). A hub carrier has no claim over a slot because the FAA is authorized to take it back. Additionally, while not binding, the FAA has asserted time and time again that slots are not property rights. There is also a good deal of case law supporting the proposition that slots do not come with property rights.²²³ In *In re Braniff Airways, Inc.*, a bankruptcy court found that a slot did not constitute property because the value in the slot came from the government; the slots had no intrinsic value in themselves.²²⁴ Similarly, in *In Re Gull Air, Inc.*, the court denied slots property right status because the interest could be reclaimed at the will of the FAA.²²⁵ In fact, the FAA could decide to completely end the high-density rule and slot allocation at all airports, and slots would have no value at all.²²⁶

2. *No FAA Authority*

In the report accompanying the Chicago O’Hare Final Rule, the FAA set forth its authority as the following:

The FAA’s statutory authority to regulate the navigable airspace does not expressly direct the agency to consider any specific factor in allocating airspace rights. Absent such expression, we must look to the public interest in determining criteria for assignment of these Arrival Authorizations. In considering the public interest, we are guided by the policy goals prescribed for the Secretary and the pro-competition policies followed by Congress in adopting legislation on matters such as slot exemptions and airport grant programs. The courts have approved the Secretary’s reliance on the pro-competition policies in allocating slots under the HDR.

As we articulated in the August 2004 Order, Congress has set forth a policy of promoting deregulation and competition in the

²²³ See, e.g., *In re Gull Air, Inc.*, 890 F.2d 1255, 1264 (1st Cir. 1989); *In re Braniff Airways, Inc.*, 700 F.2d. 935, 942 (5th Cir. 1983).

²²⁴ See *Braniff*, 700 F.2d. at 942.

²²⁵ See *Gull Air*, 890 F.2d at 1261–62.

²²⁶ See Policy Regarding Airport Rates and Charges, 73 Fed. Reg. 3310 (Jan. 17, 2008) (proposing a landing fee system based on congestion pricing; such a system could lead to doing away with the slot system all together).

airline industry by means of the Airline Deregulation Act of 1978 and subsequent legislation.²²⁷

From the FAA's own statement of its authority, it appears that its policies are to be guided by the public interest and the pro-competition principles set down by the Secretary of Transportation. Since a hub carrier preference would be the opposite of a pro-competition stance, effectively preventing smaller carriers from expanding (or even operating, in the case of a new entrant), it is arguable that the FAA does not have authority to enforce such a provision.

3. *Fairness and Competition*

Contrary to the hub carriers' fairness argument, smaller carriers can argue that basic principles of fairness and equity demand that a hub carrier preference be abandoned. With a preference, hub carriers have demonstrated cut-throat tactics to box smaller carriers out of the market. Hub carriers have been known to hold on to non-profitable slots and operate at a loss just to prevent another airline from taking the slot and entering the market. Smaller carriers would argue that almost any alternative (open market/auctions, lotteries, or congestion pricing) would be preferable to a hub carrier preference.

A hub carrier preference would reduce smaller carriers' presence in the market, and even if it did not drive the smaller carriers out of business, competition would decrease and airplane ticket prices would thus increase. The FAA referenced the importance of smaller/discount carriers to keep pricing down, saying:

Entry, particularly by low-fare airlines, is an essential ingredient for airline competition. Studies of airline industry competition under deregulation have concluded that low-fare entry has a substantial impact on price and service. For instance, Southwest initiated service into Philadelphia in May 2004, and since that time the fares in Philadelphia have shifted from being 19 percent higher to 2 percent lower than fares in comparable domestic markets (comparing the Fourth Quarter 2003 to the Fourth Quarter 2004). A policy that fails to provide any special treatment for new entry, the approach recommended by United and other larger incumbents, would curtail competition that leads to

²²⁷ See Congestion and Delay Reduction at Chicago O'Hare International Airport, 71 Fed. Reg. 51,382, 51,388 (Aug. 29, 2006) (to be codified at 14 C.F.R. pt. 93).

substantial fare reductions, increased service, and enables more people to travel.²²⁸

This illustration exemplifies the negative impact that a lack of competition has on prices and on consumers. While higher prices might be a positive thing for the hub carriers, it will not be good for anyone else.

IV. SHOULD O'HARE HUB CARRIERS GET A SLOT PREFERENCE?

A. NO PROPERTY RIGHT IN SLOTS

First, while there is a split of authority in bankruptcy courts as to whether slots constitute property, the elimination of the high-density rule at O'Hare in 2002 and the possible total elimination of slots at O'Hare (after expansion) mean that slots will likely not be considered a property right in the future. In fact, slots might not have any value in the future.

But if American and United did not have a property right in slots that they gave up to reduce congestion, then why is Congress proposing that they be made whole again? First, it seems that Congress is using terms of fairness rather than talking in terms of property rights. Congress may be intimating that those carriers who voluntarily worked with the FAA and gave up the most slots should not be put last in order in receiving additional slots. But the most important factor in why Congress said it was only fair for American and United to get first preference in slots is the hub carriers' role in funding the O'Hare Modernization Plan. So, the basic rule that Congress is promulgating is: if you pay for it, you will be rewarded.

B. O'HARE EXPANSION IS TOP PRIORITY

The one thing that all parties interested in the hub carrier preference at O'Hare agree on is that the O'Hare expansion (or the OMP) is essential. The congestion, delay, and national frustration caused by O'Hare's dysfunctional runway and setup have been well-documented. The OMP must be completed for O'Hare to continue to thrive as an airport, and the primary financers of the project are the hub carriers. The question then becomes, if allowing the hub carriers (American Airlines and United Airlines) first preference on O'Hare slots would secure OMP financing, is it worth the sacrifices to new entrants, limited

²²⁸ *Id.* at 51,389-90.

incumbents, and ultimately the consumer? For O'Hare, the answer to this question may be yes. As the only dual hub in the United States, O'Hare is likely the only airport that can and should support a hub carrier preference. With two strong carriers at the airport, there will be competition (assuming no illegal agreements are made between the two). While it is an unpopular stance to hand over precious runway space to the already-dominant carriers, such a move will secure the future of the airport.

O'Hare is a unique airport in a unique situation. There are few airports that are in as dire a need to modernize and expand as O'Hare. Even among the highly congested airports, there are few that have the physical capacity to expand (as LaGuardia is surrounded by water and Washington National has no space in which to expand). Moreover, O'Hare is the only airport with two hub carriers that can remain competitive even with a hub carrier preference. Such a preference, although backward in thwarting competition, may actually help O'Hare grow. While it might help O'Hare, such a preference could cause a detriment to other airports. The moral, then, is that slot preferences are best applied to the specifics of each airport.

