The Future of Air Travel: Three to Five Years Ahead

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William Jr. Coleman
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THE JOURNAL of Air Law & Commerce and the Dean of the Southern Methodist University Dedman School of Law, John Attanasio, presented a panel discussion to commemorate the second anniversary of the September 11th attacks. The following is the transcript from the discussion.

MR. ATTANASIO: I'm sure everyone remembers where they were two years ago on September 11th. I was listening to a radio station, getting ready for school, and a story came over saying that a small plane had crashed into the World Trade Center. And I was like, gosh, that would be a horrible thing even if a small plane crashed into the World Trade Center. And I turned on CNN. CNN was already on the spot. They thought it was a small plane that had crashed into the World Trade Center. And I turned on CNN. CNN was already on the spot. They thought it was a small plane that had crashed into the World Trade Center. And there was a thought of terrorism, but not much. And a few minutes later, a large plane crashed into the other tower of the World Trade Center, and the whole world changed. So what I'd like to do, to begin, is if we could pause for a few moments and remember those who suffered tragedy that day, passed away that day, and then we'll begin. (Moment of silence.)

MR. ATTANASIO: Okay. It gives me great pleasure to introduce our distinguished panel today. Mr. William Coleman became the nation's fourth Secretary of Transportation on March 17, 1975, when he was administered the oath of office in a ceremony conducted by President Gerald Ford at the White House. Secretary Coleman entered office following a distinguished career in law, business, and public service that included advisor and consultant to six former Presidents and the current President of the United States. At the time of his nomination, he was practicing law as a senior partner. He was also director of Pan
American, World Airways, Penn Mutual Life Insurance Company, First Pennsylvania Corporation, Philadelphia Electric Company, and Western Saving Fund. He was also a member of the Board of Governors of the American Stock Exchange and a Trustee of both the Rand Corporation and the Brookings Institute.

Secretary Coleman graduated magna cum laude in 1941 from the University of Pennsylvania and in 1946, he graduated magna cum laude from Harvard Law School, where he was first in his class and a member of the Board of Editors of the Harvard Law Review. He clerked for a United States Supreme Court Justice, Justice Frankfurter. In 1959, he was a member of the 24th Session of the United Nations General Assembly. He has held a number of government jobs, and he is an ardent defender of civil rights. He was one of the authors of the legal brief that persuaded the Supreme Court of the United States, in 1954, to outlaw segregation of public schools, that would be Brown vs. Board of Education.

He served as a member of the National Legal Committee, Director of the Executive Committee, and President of the NAACP Legal Defense and Education Fund. He has also served on the Board of Directors of Chase Manhattan Bank, IBM, Pan American, World Airways, PepsiCo, and the American Stock Exchange, among others. He holds honorary degrees from Harvard and Yale, the University of Pennsylvania, Howard, Tulane, Georgetown, and Columbia, just to name a few. In 1979, the President of France nominated him as Officer of the National Order of Legion of Honor. In 1995, he received the Presidential Medal of Valor.

Please welcome William Coleman.

MR. ATTANASIO: Donald J. Carty is retired Chairman and Chief Executive Officer of AMR Corporation. He served in that position since 1998. He also held the role of President of AMR Corporation, and prior to that, he served as President of the AMR Airline Group, American Airlines. Between 1989 and 1995, Mr. Carty was Executive Vice President for Finance and Planning for AMR and American Airlines, overseeing a broad range of strategic planning matters and a wide array of critical financial activities.

Mr. Carty had been American's Senior Vice President and Controller before leaving the airline in March of '85 to become President, CEO, and CP of Air Canada. In March of 1987, he returned to American and was elected Senior Vice President for
Airline Planning. Before joining American, Mr. Carty spent seven years in various management positions in Celanese Canada, Air Canada, and the Canadian Pacific Railway.

Mr. Carty is a graduate of Queen's University in Kingston, Canada, where he holds an Honorary Doctorate, and also from Harvard Graduate School of Business Administration. He serves on the Board of Directors of Dell Corporation, Sears Roebuck & Company, as well as Big Brothers Big Sisters of America, and a number of local civic organizations.

He is a member of the Board of Trustees at SMU, as well as the Harvard Business School Visiting Committee, the Advisory Board of the Kellogg Graduate School of Management at Northwestern University, and the SMU Cox School of Business Executive Board.

In September of 2002, he was appointed by President Bush to the National Infrastructure Advisory Committee. In January 2003, he was named an Officer of The Order of Canada, that country's highest honor for lifetime achievement.

Please welcome Mr. Donald Carty.

MR. ATTANASIO: John J. Nance is a graduate of this law school. He is a licensed attorney who received his bachelor’s degree from SMU and his J.D. from the SMU School of Law. He is a decorated Air Force pilot, a veteran of Vietnam and Operation Desert Storm/Desert Shield. He is also a Lieutenant Colonel in the United States Air Force Reserve, and is well known for his involvement in Air Force human factors flight safety education. John has piloted many aircraft. He flies his own aircraft and is a veteran Boeing-737 captain for a major airline. He’s flown 727s, 737s, 747s and C-147s for the Air Force. He’s logged over 13,000 hours in the air.

He is an internationally recognized air safety analyst and advocate, best known to North American television audiences as aviation analyst for ABC Television Network, and is aviation editor for Good Morning America. As such, he was intimately involved in the reporting of the events of September 11th. John has had multiple appearances on Larry King Live, the Oprah Winfrey Show, NPR, the Today Show, and many, many others. His editorials have been published in newspapers nationwide, including USA Today and the New York Times. He is a nationally known author of 13 major books, including four non-fiction and eight fiction best sellers, two of which, Pandora’s Clock and Medusa’s Child, both aired as major successful two-part mini series on television.
John is well known in resource management and expanded human performance training, and is a dynamic professional speaker and consultant. He speaks to a wide variety of audiences, including medical and pharmaceutical professionals, CEOs of major business-oriented corporations, and environmental, aviation, engineering, and travel oriented groups. He is a founding member of the Executive Committee of the National Patient Safety Foundation, and he is a member of the Executive Board of the SMU Dedman School of Law.

Please join me in welcoming John Nance.

MR. ATTANASIO: Before turning the podium to John Nance, I need to thank a couple of people. One is Grant Walsh of the Journal of Air Law & Commerce for sponsoring this. Another is Al Casey, former CEO of American Airlines and a number of other companies, also former Postmaster General. Al Casey, John Nance, and I did a conference a few years ago immediately following the events of September 11th with the Journal of Air Law & Commerce, and this is a follow-up to that conference. So I want to thank Al Casey and the Journal of Air Law & Commerce in particular.

MR. NANCE: Thank you very much, John. It’s a bit humbling to be here in the presence of such talent here, not only our good Dean, but also, of course, Mr. Coleman, with whom I have been familiar for many, many years, and Don Carty the same thing. Tremendous achievements on both people’s behalf for so long in aviation. Let’s start with this: 100 years ago, one century ago, there was a powered flight. I mean, we all know that. This year, in December, is the celebration of the Wright brothers’ first flight. I made the statement not too many years ago that arguably the greatest technological achievement of mankind was aviation, commercial aviation in particular. Arguably, I say. That’s always a good lawyer thing to throw in. What I want to do today is focus on the future of aviation, the next three to five years, as well as further down the road.

Let me start this way: Before we can truly discuss the effects of the free market, terrorism, change in customer habits, expenses led by new security measures, rising fuel costs, and the need to grapple with all the other things the airline industry has been faced with since 9/11, I think we need to focus on a couple of questions. I’m going to lay them out here and then pose them to the panelists. I’d like everybody to think about this:

How important is the airline industry to the people of the United States as a stable and predictable entity? That’s some-
thing we take for granted, but we really need to focus on that, because it’s a predicate for everything else that we’re going to discuss. How important is the industry? Secondly, how important is the airline industry to the economy of the United States? Two years ago, one of the questions that we grappled with was what’s going to happen if the airline industry does not recover? And we’re still limping along in many different respects. So if you’d use that as a predicate, gentlemen. Let me start, if I could, with former Secretary Coleman. The first question that I would like you to grapple with is this one: If you were giving a state-of-the-industry speech today on the airline industry, what would your summary outline say?

MR. COLEMAN: I think that the American people should recognize that the airline industry is a very, very extremely important industry. In fact, I think that at least 3 million people get their jobs directly or indirectly from the airline industry. Not only do you have those on the airline, but you have those in the aerospace industry, you have the federal screeners, you have the food shops at the airport. In fact, I’ve seen documents that would say somewhere between 12 and 13 percent of the American economy depends directly or indirectly upon the airline industry, including the aerospace part of it. Secondly—and there’s an argument both ways, and I’ve heard it both ways—that either the airline industry is, in part, subsidizing the defense industry in connection with building new aircraft, or vice versa, the defense industry is subsidizing the airline industry. Now, I’ve heard that argument both ways, but either way it shows it’s a plus. Having said that, I think the airline industry today faces about eight basic problems. And if they can recognize those, then I think they will have a solution to having the profitability that they should have. I take it I should stop here and hope somebody will ask me, first, what are the eight basic points; secondly, how do you get out of the box? And therefore, I turn it over to you, sir.

MR. NANCE: Thank you. Don Carty, let me ask you the same question. If you were giving a state-of-the-industry speech, how would you assess it?

MR. CARTY: Well, you’ve got to agree with Bill’s conclusion. The airline business is certainly fundamental to this country. And it is, after all, our only form of inter-city transportation that’s worth speaking of, and is likely to be for some time. It’s just the nature of our geography and demographics and those kinds of things. And it’s going to be increasingly important as
other industry globalizes, because, again, it's the only way of connecting places around the world. The state of the industry, however, is obvious—the entire industry is in pretty rough shape. Even the relatively successful carriers are struggling mightily. Obviously, this is an industry that's cyclical; there's a tendency for the business to be cyclical, to be affected by another downturn. But we have never seen the confluence of events that have impacted the industry in the last few years, ever in its history of a hundred years. Not only have we had an economic downturn, but we've also had the events of 9/11. Then the follow-up to all of that; which meant increased cost of security; which meant the fear of flying for many passengers; which meant concern about the harassment of flying as a consequence of those security measures; the resulting dramatic increase in the cost of insurance for this industry; the subsequent skyrocketing price of fuel as we anticipated the situation in Iraq; a major accident by American Airlines, that again, I think, shocked the confidence of much of the traveling public, at least with respect to one aircraft type. And if that weren't enough, we then had Iraq; we had SARS; and in the case of American Airlines, of course, we had a hailstorm out here at Dallas/Fort Worth that put a hundred airplanes out of circulation. So the industry is terribly damaged financially. The balance sheets of these companies are in the worst shape they've been in many, many years. A number of the major carriers are bankrupt, and others are teetering on the brink. And even, as I say, the successful new business model carriers, like Southwest, are having as much of a financial struggle as they've had in their 30-year history. So it's a tough time.

MR. NANCE: Let me follow up on that and ask you this: When we have this kind of challenge—two years ago, after 9/11, you and so many of the other chairmen, were almost instantly on Capitol Hill, just like the head of Boeing was, saying that something's got to be done, and got to be done fast. We're leaking money at an incredible rate. This industry is too important for the Congress and the United States to ignore. This is predicated, it seems to me, on a consideration, not only of a national interest in the airline industry and a continuation of that industry and the jobs and the economic impact, but also it brings forth a question of just exactly what should be done by the public and what should be done by the payors. There is an increasing, in my view, stampede towards the idea of a fee for service on everything. So that if we got it down to a ludicrous extreme, in
governmental units we would have a toll booth at the beginning of every residential street, because I don’t want to pay for your street, and I certainly don’t want to pay for his bridge. And we have this idea of privatization of various things, including air traffic control, coming up.

Within that context, considering that these are businesses, even though vital, and even though we’ve somewhat discarded the definition of public utility in dealing with deregulation, what should we do, as a people? How should we handle this? Let me start with you, Bill.

MR. COLEMAN: Well, I think that the airlines, in my judgment, acted rapidly, and Congress responded rapidly, and I don’t think that they really came to grips with the real problem. I also think that’s a problem that did come with it, in that the airlines haven’t taken advantage of it correctly. The Congress did pass the Transportation Safety System Stabilization Act. They committed $10 billion. The purpose of that bill really was to induce the airlines to reorganize. They haven’t really done that.

Instead, those that have gotten the guarantee under that $10 billion are not the airlines, with all due respect, that are going to make the difference in the long run. And whereas, with respect to United and US Airways, they haven’t been able to convince the Government that they should get it. I think that before the Government steps in, they first have to face up to the labor problem.

Now, having never run for public office, I’m not qualified to tell a Congressman or Senator as to what you should do, because obviously the unions exercise great pressure, but just look at it. I think the airline industry is the worst industry in the world with respect to the theory of how you carry out a labor dispute. When they walk off, that’s the end of the service. If you have a strike in the automobile industry, people can say: Well, I’ll just put off buying the car until General Motors or Ford starts up again. But in the airline industry, once you lose that passenger who’s going from Fort Worth to Washington today or tomorrow, that passenger is gone forever.

I think that you’re going to have to reorganize that industry. And the best precedent I know with respect to the labor negotiation is what they’ve done in the baseball league. You finally negotiated—you finally have two offers, and a mediator steps in and determines which is the fair offer, and that’s it. That’s the first problem. Everybody says that we are going to reorganize
the airlines, but you've got to control the course. You control the course, in part the labor movement, by having a labor compensation which makes sense based upon the amount of money you're making.

Secondly, I think it's a tragedy—I saw the other day in the *New York Times* where the money they put up in New York for the people that were adversely affected by the incident of 9/11, it turns out that most of that money has been paid to members of law firms or investment banking firms, because they could demonstrate for two or three days they couldn't sit at a computer and make a buck. I mean, that is no way that public money should've been spent. And those people that really suffered have not gotten much of that money.

And I think that if you go back and examine what the airlines actually got, I don't think they got the money for things which would make a difference in the long run.

MR. CARTY: I have to say this: I mean, I think the Government did act quickly, as quickly as they've ever acted, and they did so even though a number of them initially were skeptical. When they understood the magnitude of the problem that this breach of national security had caused, and the magnitude of the financial cost that had been posed on the airlines as a consequence of the new security requirements and new insurance requirements, all were convinced and that bill moved very quickly through both the House and the Senate, as fast as any bill has ever moved through. And I think those in the airline industry were grateful for that.

But I think I agree with Bill in this sense: It's time that the Government sat back and re-examined, from a public policy standpoint, what their role needs to be and what the airlines need to do. I'm not a great believer in the Government intruding into the day-to-day commercial aspects of the business. I don't think that's necessary. I think a vibrant and competitive market has worked well for the consumers in this country since deregulation. And I think once these businesses manage to transform themselves as they need to for the future, it will be good for the airlines as well. What the Government does have to do, I think, however, is they do have to take responsibility for national security. That isn't an airline—your question of, should you be paying for your neighbor's street. It seems to me it's really clear that the Government has a responsibility for national security to all of us.
At one time, aviation security was about aviation. When airplanes started flying into the World Trade Center, it's not about aviation anymore, it's about a much bigger issue than just airlines. And I think the Government shouldn't necessarily impose that on either the airlines or the passengers uniquely. I think it's part of the Government's role.

I think Bill raises another interesting question, and that is the question of whether or not the existing labor laws are working in the airline industry in the employees' interest, in the consumers' interest, or in the shareholders' interest. After the 50 or so years that the current labor bill has been in place, it probably is ripe for re-examination and re-formulation. But I would say this: I think that too often airline management, particularly the management of these traditional airlines that grew up in a regulated environment, have used the cost of labor as an excuse for not transforming parts of the business that management can control. I think one of the great things about what has happened, at least in a number of carriers—and I'm very proud of what's happened at American, is that there's been a really fundamental transformation of many of the aspects of doing business there—the management team is out there putting those in place, which will have a radical impact on the cost structure and the competitiveness of this airline with or without the labor savings. Now, initially, they obviously needed labor savings. But airline management can't constantly be saying this is uniquely a labor problem. A new form of business model entered this business, and management has to be responsible.

MR. NANCE: Well, there was, I believe, a quote by Don King: There is no right to strike against public interest anytime, anywhere, by anyone. And I personally have lived under two binding arbitration contracts, one for Braniff International, the long-gone, fondly remembered local airline, and Alaska Airlines, from which I just early retired. And I'm proud of those. I'm proud of the fact that I never ended up in a strike situation. That's just a personal comment. But it does seem to me that we've got to move in a direction boldly to eliminate the possibility of this kind of labor strike, especially with the reorganization we're facing, because the market simply will not take the level of rates that are being paid out there. Any fundamental disagreement with that?

MR. COLEMAN: No. I also agree that there has to be a fundamental decision made as to what the Government should do with respect to safety issues and what should be the burden on
the airline. And I think that someone has to study that issue. You know, the threat that around the airport somebody could have a rifle on his arm and be able to shoot down an airline, if that is a valid threat, I think that you have to sit down and say: Is that a function that the airline should take care of, by either raising its fare or having an additional ticket tax by the passengers, or is that just another normal defense function that should be borne by the general public?

But I think that the airlines have to get together and make an absolute decision on that and come in and try to convince Congress with respect to that. I don’t think that when deregulation was done, those that supported it felt that you would end up with two distinct types of carriers, one so-called network carrier, and the other one, the low-cost carrier, and then the low-cost carrier gets big enough to be able to snatch off the best routes of the other network carrier.

And now you have the threat of Europe. You know, you’ve got a whole Eastern Europe developing. It is highly possible that they will be bright enough to abandon the idea that every nation has to have its own aircraft and put together one or two major aircraft companies. And that would be a completely different threat to the United States than you have today. And those are the types of issues which I think management has to sit down—I said I have eight of them, and I’d love to be able to lay them out.

MR. CARTY: I’d kind of like to hear the eight.
MR. NANCE: Go ahead, Bill.
MR. COLEMAN: The airline is in a business which is basically fungible. It’s the same airplane, they take off about the same time, they land at the same airport, and therefore that’s their business, and therefore it’s very hard to compete saying, I’m doing something different than the other one. Next, I talked about the strike situation. I know of no other industry where the employee can have such a tremendous control over the negotiations. Then you have this whole problem with the low-cost carrier against the network carriers. And I think that there is an answer but I don’t think anybody has ever sat down and said, what should be the answer?

After that, you have what I mentioned, the international problem, where you have Eastern Europe developing in such a way, indeed all of Europe is developing, and if they got together and had fewer airlines, I think they would pose a greater competitive threat to the American airlines. Then you have, in the federal
statutes, a provision that no foreigner can own more than 25 percent of an American airline. The administration, and I think the previous administration, has tried to increase that to 49 percent, but Congress so far hasn't gone along. I think that it should go up to 49, perhaps it should go even higher. And one of the difficulties by having these percentages is that those lawyers trained at SMU and other good law schools somehow know how to get around them. And you get around them in such a way where you're not quite as efficient as you would be if you didn't have to.

Next you are facing today, because Judge Calisty cited, believe it or not, that the families of the people in September 11 had sued the airline, because the airlines should have had the vision that this would happen and should have been able to take care of it. I think that will cause difficulty. Now, I think there's something in the statute which says the maximum liability is $6 billion. Frankly, I haven't read the statute closely enough, or if I had, I don't remember, whether that's $6 billion per airline or $6 billion over the whole industry. But either way, $6 billion is not that much money today when you start getting involved in class actions.

The difficulty, as I see it, with the Transportation Safety System Stabilization Act is at least twofold: One is that I don't think that to just lend the money or give a guarantee so the airline can get back in business makes sense. They were supposed to reorganize. I don't think those that have asked for the money have been doing that. But secondly, can you imagine a governmental official, if two airlines come to him or her asking for a new route or new landing rights, and he or she knows that one airline has a guarantee from the federal government of $2 billion, which they have to pay back, and the other one doesn't, and if you make the argument: Well, if you give me this advantage, I'll be able to pay you back your $2 billion. In other words, you put those airlines at an advantage, which I think is really unfair.

Then you have the whole code-sharing problem. You also have the question of taxes, as to whether some of the taxes, which have been levied over the years on the airline and the passengers, should be reconsidered. Then you have the whole question of where you locate the new airports. Now, once you master those eight problems—and I hope my arithmetic is right—then I think you can sit down and advise the airlines what they should do to be able to have the proper service that they
deserve and ought to have, and what the American people really think they should have.

MR. CARTY: I have a couple of observations about a couple of points Bill made. The first issue is low-cost versus traditional network carriers. I think if we talk about the future, if you look out four or five years, network carriers will only survive if they have transformed themselves in a way that recognizes the existence of the new business model. Now, that doesn't mean they have to be Southwest, or they don't have to be JetBlue, but they have to be cognizant that in most of their markets, there is going to be a marketing presence characterized by very low-cost competition and very low prices. And if they can engineer their organization to be cognizant of that and still be profitable, they will thrive. There is no single business model that endures forever. The problem with the traditional network carriers is that a lot of the transformation that they've achieved since deregulation has been focused competitively on each other. And now the low-cost carriers are so pervasive, cover so many markets, that they need to be further re-engineered to be cognizant of that competitive fact as well. I think that is going on. I think that sometimes it takes a real hard time to make it happen, but I think it's now going on. I think it's well underway at American, and I think it's well underway at a number of other carriers. If that isn't achieved by carriers, they won't exist. Remember, we had 11 major carriers at the time of deregulation, and every one of them, except for Delta and American, have filed for bankruptcy or are reorganizing in bankruptcy. So there's been a radical change in the industry by traditional carriers not managing to transform themselves. And it's not uniquely an American phenomenon. You're starting to see the same thing in Europe. You're certainly seeing it in Canada with the Canadian carrier bankrupt. So one way or another, these companies are either going to go away, they're going to reorganize in bankruptcy, or they're going to transform themselves consensually, as American has been trying to do, and as Delta's been trying to do. And there really is no other option.

With respect to Bill's comment on foreign ownership, I couldn't agree more. The long run of this industry—I think as we all sit here 20 years from now, it's hard to believe there will be something called flag airlines. We don't have flag chemical companies, we don't have flag shoe companies, why would we have flag airlines? And I think the foreign ownership rules will go away. I think now is the time to engage in that debate ag-
gressively and show some American leadership in changing it. I think the American carriers, if they transform themselves into competitive entities, will be able to play a significant role on the world stage. And I think the problem with code-sharing, as Bill talked about, will go away when foreign ownership goes away. Code-sharing is simply a way of globalizing under the constraints of not being able to grow internationally.

I think all this is going to take some time, but I have an easier time, John, answering the question, what does the industry look like 20 years from now, than what does it look like three years from now. Because this period of transformation has a lot of uncertainty associated with it, uncertainty about which airlines will do the right things, which will do the wrong things, and how long will it take to go from the Government to get policy written.

MR. NANCE: I must leave you, but I'm going to pose a question in front of all of you that's very, I think, appropriate in regard to all the changes we've talked about. There is a tidal wave, if you will, of vicarious transportation methodologies coming down the pike, in the form of communications, and we've already seen the impact of this from September 11th. So as I turn this over to John, and thank you all very much, maybe I can put that in front of you first, Don.

MR. CARTY: It's a very good question, John, and it sort of runs to the earlier comments. With the change in technology and telecommunications, will airlines and transportation remain as important an element of the economic infrastructure as it did for a long time? After all, do we really need to go there, or do we need to communicate as effectively as we can? Thus far in the industry, I think that what we've seen in commerce is that the advance in telecommunication and technology have accelerated the pace of globalization. And ironically, instead of that hurting the airline business, it's helped it. Because ultimately you do have one-to-one contact with people you do business with around the world.

It's put a lot more pressure on us being more sophisticated in developing better networks internationally than we had 20 years ago, but it's been a net plus. As we go forward, however, I do think the advances in telecommunication and technology are going to reduce the demand, or certainly slow the growth of demand for business transportation. But while that's happening, of course, we have always known that there's an insatiable demand for leisure travel, and all you need to do is adjust the price to tap into that. And again, I think that makes it so impor-
tant that a carrier that wishes to survive becomes a far more efficient entity than many of these entities have been for the last 20 years, so the price of that product can reach the consumer that wants to consume it. People love to go places, places they've never been. So even if commercial aviation—aviation-related economic activity between businesses decreases, I think the industry has got a lot of growth left in it, particularly in some less developed parts of the world.

MR. COLEMAN: Don, I had occasion to pull the testimony of the Under Secretary of Transportation to the Senate Committee on Commerce, Science and Transportation that he gave on January 9 of this year. And he said that the economy between the lost-cost carrier and the Internet carrier is that the Internet carrier appeals to the business people, and that's where they expect to get the large part of their business from. Now, what used to be the case, that you have the airplane, and you have the business people in first class and in business, in the back of the airplane you have the lower fares and you have the leisure travel. But what's happened now, oftentimes, is the business person has a private jet. And, secondly, oftentimes, instead of flying down to Dallas for a meeting with the client, you have a conference call.

So I do think there's some threat to say that if your business plan makes the assumption that you're going to get the business traveler, and the leisure travel is going to go to low-cost carrier, which I think is happening. And I think that if you're really going to resolve this problem, you have to face up to the fact that once you agree that it's essential that they be large, profitable carriers, then how do you make the rules so that that's the result you come up with? I think to have a low-cost carrier, they come into the industry later, they don't usually have the same labor problems, in terms of the same amount. And then, once they begin to develop, they say, what are the best routes, and they pick those. And as a result of that, the major carriers are losing some of their business to the private jets, they're also losing some of it to the conference call. And thirdly the low-cost carriers—you know, the same way when Willy Sutton says, why do you rob a bank? That's where the money is—they know where the business is and therefore they will say I have enough airplanes now that I can fly from Chicago to Atlanta, Georgia, and I will take some of the business people. And, in fact, a good corporate manager may say, look, you can fly on this route by half the fare it takes to go on American, so that's what you have to do. So I really think that this is a challenge that you have to
look at before you decide which is the business plan that’s going to work.

MR. ATTANASIO: Before I open it up to the audience, I’d like to shift gears a little bit and focus you both, because you both have such expertise on this, on how much of an impact the airlines had on the economy. Not so much you mentioned earlier, Secretary Coleman, that how many people were employed directly or indirectly, but what I’m after is what kind of leveraging effect transportation provided. You mentioned earlier, Mr. Carty, that the airlines have an enormous impact, in terms of how many people they fly. How much impact? How many passengers are we talking about in a day? How much in the way of goods moved? How many business passengers as against how many leisure passengers? What are we talking about?

MR. CARTY: Obviously, we’re talking about hundreds and hundreds of millions of passengers a year, seven or eight-hundred million passengers. Now, it’s shortened a little bit in the last economic downturn, but it’s that order of magnitude.

MR. ATTANASIO: And in what area? In the United States?

MR. CARTY: In the U.S.

MR. ATTANASIO: U.S. traffic.

MR. CARTY: And that’s a huge number of people moving every day. You know, all you’ve got to do is go to one of the hub airports and watch the activity. You know, at DFW in a big day, 50,000 plus passengers coming through DFW is not an uncommon event. The same thing would be true of Delta’s hub in Atlanta, and both United and American’s hub in Chicago and Northwest’s hub in Detroit. Huge numbers of people traveling. Now, historically, that’s kind of split evenly 50/50 between business and leisure. In an economic downturn, you get the effect that Bill talked about, that leisure becomes a greater percentage of it. It becomes a greater percentage partially because the business traveler can’t be stimulated, he’s not going to travel unless there’s an opportunity, the leisure passenger can be. As the economy turns down, the airlines average price weekend—as the business travelers go away, he gets replaced by the lowest possible fare, because you push the fare down a little bit to capture more passengers. And that’s why it’s such a cyclical business. You lose the best of your business and you stimulate the worst of your business. Now, when I say “worst,” I mean in terms of price. I haven’t seen recent months’ data, but in the summer of an economic downturn, which is what we’ve just been through, I would be surprised if it wasn’t 70 or 80 percent.
MR. COLEMAN: I guess most people are too young to remember, but if you can get a picture of what Dulles looked like before it opened in Washington, and you thought it was way out in the wilderness, nothing was around it, if you land at Dulles now you'll see nothing but major buildings and advertisements of all types of companies that have their businesses around there. And I think that's true throughout the country. I think, for example, in Pittsburgh, where US Airways has a hub, they have shopping centers. It's the biggest mall in Pittsburgh, and it's a dynamic business. I really think that you have to recognize that when you go through the airport and see all the different types of people.

And then you have the whole question of leisure travel. People do travel, they want to travel. And I thought that the original concept, when Boeing built the 747, was that those people who travel in the back of the bus, those people who travel back three seats to a row, they pay a much lower fare, and they'd get there the same time, and that, I thought, was the way that it was supposed to work. When I was Secretary and we were faced with the question of deregulation, and we did not pass it in the airline business, I was told that the moment you had this, you're going to have 79 airlines, and they're going to compete with each other, and therefore they're going to take care of the prices, you'll have no problem. It hasn't worked out that way. The major airlines are going down, as John said. Some of them have disappeared. And now you have the small ones that started going, serving small cities, but now they will run from someplace in California very convenient to someplace in Washington. And they obviously have to be taking business from United and from American Airlines and the other airlines that would run that route. And whether you go out of L.A. or out of Santa Barbara, it really doesn't make that much difference. And that's what's happening in the business, and I do think that the businessmen and businesswomen have to face up to that and decide, how do you go about managing a very, very valuable, necessary asset, but do it in such a way that you make money on it. Because in a capitalist society, if you don't make money on it, then it has to deteriorate in quality and it just doesn't work.

MR. CARTY: It's a fundamental part of our economy, John. But the challenge of business transformation is not unique to this industry. If we had said to ourselves at a conference 20 years ago, my goodness, if Wal-Mart drives Montgomery Ward out of business, we'll be in terrible shape. But that wasn't true. Mont-
gomery Ward is gone and Wal-Mart is five times bigger than what was then the biggest retailer in the country. What happens if IBM goes out of the PC business? Well, they’re not out of the PC business, but their marketshare, compared to a Dell or anybody else, is inconsequential. I think the market takes care of itself. But the challenge for existing airlines is to recognize that and transform themselves. And if they can’t transform themselves, they’ll be the Montgomery Wards of the future. And they’re faced with enormous challenges, because the change that gave rise to this new competitive set was a change in regulation. And we had adopted ourselves for a regulated environment with a certain set of rules.

So the challenge of the CEO—with all due respect to my good friend Herb Kelleher, the challenge of Gerald Arpey at American Airlines versus Herb Kelleher—if Herb Kelleher runs a great airlines, he does; if Gerald Arpey is to run a great airlines and he doesn’t, he’s got to change the tires when he’s going down the highway at a hundred miles an hour. But that’s the challenge. If they don’t transform themselves, they won’t be successful. And so many companies and so many airlines and so many industries have. We will have an airline industry. What it will look like, and who are the players in it, is going to depend on the innovative and creative new start-ups, and the creativity and management’s and leadership’s skills to transform the existing companies.

MR. COLEMAN: Don, may I ask you a question?

MR. CARTY: You bet.

MR. COLEMAN: Suppose you were Secretary of Transportation. The President of the United States called you and said, look, John, this industry lost $10 billion last year. The major carriers seem to be failing. What should I do and what should be the policy? I want to scrap everything we’re doing, but I want you to come up with a policy for the Government, which will get us back to where you have airlines profitable, serving the people, and to the extent that we have competition from abroad, we can manage that in such a way that it’s not a great disadvantage. Now, how would you redo the airline?

MR. CARTY: I would very much focus on what both you and I talked about: Taking responsibility for security and safety oversight and enforcing those rules and freeing up the market as much as I could. And that would include not only the domestic market, but it would include the international markets because American ingenuity in business has been successful. Where
we've had failure, we've had tremendous success, tremendous re-invention. Again, I will be going back to my PC example. Five years ago, ten years ago, there were a lot of people saying the Japanese were going to take over the PC business. Well, no one told Michael Dell. And now the Japanese are a pale shadow of Michael Dell. I think we need a marketplace that enables Americans to use their creativity. Great challenge to traditional guys. We may lose and see the bankruptcy of more of them. It will be unfortunate. But I think the best thing the Government can do is take responsibility for Government things, safety, security, the airspace. I think there's a lot of work the Government needs to do on the airspace to really free up the airspace in the competitive environment, provide the technology that's available to us. And I think those are the things the Secretary of Transportation should impose.

MR. ATTANASIO: One last question before I open it up to the audience. How much has terrorism impacted business?

MR. CARTY: Well, it's impacted it in a number of ways, John. In the first instance, of course, it scared people off. And I think we've largely recovered from that. The second thing it did is it imposed an economic burden on the airlines and ultimately its customers of the cost of the security we put in place to try to diminish the threat of terrorism. Initially we put in place a system that not only cost a lot of money but imposed on our passengers a tremendous harassment factor, if you like. I think the Government is making progress there. This was all done in an enormously short amount of time. And I think people now are focused on how do we automate, how do we take advantage of technology, doing all the things that—in fact, my way of thinking, the Government has done a better job than I'd thought they'd do a year and a half ago when they started this. I think we've had some good leadership in Washington on that. But to say it hasn't affected us in terms of cost and therefore price to the consumer would be very naive.

And to think that it didn't accelerate the bankruptcy of US Air and United—they probably would've gone bankrupt anyway, but it clearly did accelerate that. And it accelerated this terrible economic spiral that the airlines are in. But before September 11, 2001, management at American sat down around a table and said, we are moving into an economic downturn. Economic downturns are always tough on airlines. What do we need to do to take the next step in restructuring this business? We thought it would be an evolutionary restructure over four or five years,
and we woke up six months later to find out it had to be accomplished in a year or we would be out of money. And I think that’s the biggest short-term impact that this change had on us.

MR. ATTANASIO: Secretary Coleman, do you have any remarks on that before we open it up for audience questions?

MR. COLEMAN: No. I must say that American does it better than the airline that I flew to Jacksonville, Florida on Monday does, so—I won’t identify which one that was, but I wasn’t very impressed with them.

MR. ATTANASIO: It’s okay.

MR. COLEMAN: But I was very impressed with American and the way they could move you through, and it was much faster and just made more sense. I think the American people have responded to an unthinkable challenge much better than we give them credit for. You know, you always thought that those two oceans really protected you. We saw that it didn’t.

And in six months thereafter, the Congress instructed the Department of Transportation and other parts of the Government to come up with a plan. And I think in six months, they did a tremendous job. I also would say that I have great admiration for Transportation Secretary Mineta, that the moment he heard of the crisis, his first order was to get every one of those commercial airplanes down to the ground. And that’s the only reason why, I think, we picked up the fact that one plane over Pennsylvania was headed for the White House. So I really think that we criticize politicians, you know, on the night shows, but I really think that he acted responsibly and correctly. And I think the airlines have done a good job in trying to meet what is really a threat, but yet do it, as far as possible, consistent with our right of privacy and the fact that we don’t like distinctions made based upon things which we can’t control.

MR. ATTANASIO: We’ve got a few minutes for questions from the audience.

AUDIENCE MEMBER: My name is Pete Schulte, and I am a second-year law student here at SMU. In the last four years, I’ve flown probably 200,000 miles. I worked for one of the big four accounting firms, flew about every week. And being based in Dallas, you can imagine what airline I flew 95 percent of the time.

MR. CARTY: Thank you.

AUDIENCE MEMBER: When you fly enough, you get status on an airline. Before September 11th, it was a nice to go sit up
in first class. It was a pleasure to get in American Airlines, say, I hope I get the upgrade and sit in first class. Well, this summer I was again traveling for work, and I was flying American Airlines. And I know after September 11th American Airlines and other carriers cut a lot of their meals and a lot of their services. First class is not like it used to be, okay? There's nothing special about it. It's almost like flying in coach. So this summer I had an opportunity to fly JetBlue, which is one of the low-cost airlines in New York City, and I actually—I'm not bashing a particular airline—I didn't have any better service on JetBlue than I did on American Airlines. So my question is this: That is your competitive advantage. The network airlines have the first classes, the low-cost carriers don't, because it keeps their costs down. American Airlines and the other carriers have already stopped providing a lot of the services that attract business travelers to first class. How do you change business travelers' mentalities, saying, hey, it's nice to be pampered in first class, it's nice to spend $1200 versus $400 for the same flight?

MR. CARTY: It's a very good question. Obviously, what these traditional carriers are trying to do is they're trying to find the balance, the right economic balance across their product line between various services customers want and various services customers value. And wanting things is easy, but what they're trying to determine is, how they can have—because the nature of these operations—somewhat higher costs than other carriers anyway. You can't fly to Tokyo on a 737, so you're going to need a different airplane to do that. The question is, what kind of revenue premium, what kind of appeal can you make to the customer which will create unique revenue pools that a low-cost carriers can't get out, and what services does it take to put those together, then how do you make sure that the revenue pool that you achieve doesn't exceed the cost premium? Because if it does, you don't have a viable business model in today's world. Because the single thing that customers value most is pricing. And that's not just leisure passengers anymore, because so much business travel is bought on a negotiated basis. So the notion that there's a $1200 fare out there, try to find someone to pay it. There is no business that would pay $1200 anymore. They sit down—you know, if you're a member of the big four, I can guarantee you PriceWaterhouse or Ernst & Young have a contract with three or four major airlines, and they don't pay list price. So that's the reality of the marketplace. The price and schedule are far more important than any of these other services. With
that being said, we want to identify those that have values and
will help us create unique revenue pools and unique revenue
premiums, but they can't create such unique cost premiums that
you're out of business. That's the transformation I'm talking
about. It's partly that, and it's partly simply re-examining your
entire business and re-engineering it; in fact, that's underway as
well. But have they got exactly the right answer yet? The an-
swer, obviously not. That will be a constant juggling thing. But
it is clear that the majority of the people that don't want to sit in
first or business class for price and value reasons aren't prepared
to pay you a huge amount of money for food. They like it,
you'd like you to give them a meal, but they're not going to pay
anything for it. They will ride a Southwest that won't give you a
meal if the price is different, which is their way of saying, I'm not
going to pay for a meal. That's a balancing act.

AUDIENCE MEMBER: I'm Lisa Tulk, a third-year law student.
Secretary Coleman was discussing the United States District
Court Judge who went ahead and ruled that it's okay for 9/11
victims to sue the airlines. Do you think this sets a dangerous
precedent for unreasonable and unforeseeable instances that
occur on the airlines, and what impact do you think that will
have in the future?

MR. CARTY: Well, you guys are the legal minds, and I'm not.
All I can say is it's the most stupid thing I've heard in my life.
And that isn't a legal opinion, that's a personal opinion. The
fact of the matter is, the legislation that the Secretary referred
to, at the time that the Government passed this act, it did three
things:

One, they simply gave a grant of money to the airlines to pay
for the downtime and lost traffic; then, as Bill pointed out, they
created a pool of money that carriers could potentially borrow,
and that was the $10 billion pool; the third, which was enor-
mously important to American and United, because we saw this
coming was, to cap our liability at the limits of our insurance,
and, at the same time they did this, they created a fund that they
hoped most of the victims would access. Now, because there are
lawyers out there, some were convinced not to access that fund.
And I think we're obviously going to have some litigation here,
and how it will end up, I don't know. I do know the insurance
company also rigorously defends this one. The notion that they
should've anticipated the airplane being hijacked and flown
into the building, to me, is just crazy.

MR. ATTANASIO: Counsel?
MR. COLEMAN: Well, I was—I haven’t checked our new business. I don’t know which side we’re on.

MR. ATTANASIO: Tell us what you really think.

MR. COLEMAN: I remember one time I was in New York and Judge Rifkin, who is a great judge, had just joined the firm. So like every young associate, I said, well, I have to appear before this guy to impress him so maybe next time he has a big case he will to ask me to be one of the associates.

So I had a problem I was working on. I prepared it better than anything else I’ve ever done in my life. And I asked to see the judge. I said, I have a problem, I went in, and I laid out the problem the best way, at the end of which he said: Well, I’m sorry, Mr. Coleman, you haven’t told me the most important fact. Now, you can imagine my chagrin. I said what do you mean, sir? You haven’t told us who our client is. So I have some caution to say, but I was surprised and it scares me that part of the plaintiffs are actually insurance companies, and it does raise an issue. But you knew it was coming because the fund set up—Mr. Kenneth Fienberg, who I thought did a good job, and had worked it out where people got somewhere between $350,000 to $6.1 million, reported the other day that only 30 percent of the possible applicants have made their application yet, and you’ve got to make it by the 22nd of December. So it’s clear that part of the bar has gotten a chance for a much better lawsuit, and that’s why you have this lawsuit. And the question is, can the Congress now amend the statute so as to limit the liability here? But I think it’s a serious threat to the industry that this type of lawsuit will go on and probably go on for the next five or six years.

MR. ATTANASIO: One more question.

AUDIENCE MEMBER: As you know, there’s a significant debate going on now about the Patriot Act and its impact on civil liberties and what have you. Can you tell us whether or not the Patriot Act is having an impact on the airlines in terms of requirements, and if so whether, it’s good or bad?

MR. CARTY: I’m hesitating because I may or may not be entirely current with all of it. But it certainly—it wasn’t having an impact on it when I left the company in the spring of this year. There were a lot of issues about privacy early on that we juggled with with the Department and Homeland Security folks day in and day out. But whether there’s a direct impact from the Act, I can’t tell you the answer to that. Do you know, Bill?
MR. COLEMAN: Well, one of the difficult problems, and I don’t know whether it’s because of the Patriot Act, is the whole question of how you develop the rules of the person that you will check as against the person you let go through. Now, you know, the assumption is that any person 80 years of age, with white hair, and with a crutch, is not one who’s going to do something in an airplane. On the other hand, someone who appears to be from the Middle East, 21, that may be or maybe not, but yet the whole question of profile has come up, and I think that’s one of the questions that has got to be worked out. I think another question that you’ve got to face is that the constitutional law—and I will be the first one to say something is constitutional, is the least good you can say about it. And often time the Government has to do much more. But in reading the cases, other than a case of Bevins versus the FBI, I don’t think there’s a case which says that if a federal official stops you and searches you and then lets you go, that that violates the fourth amendment. And I just put to you the question that if one of those people going through security at Boston had been stopped and searched, could he have a lawsuit because they picked something on him? And I think that this whole issue has to be really looked at. And I would be the first one to say that as you approach these problems now, they will be different from the way you will look at them four years from now when we make—what’s the name—where right after you did what you did on the west coast, but four years later you said you couldn’t hold the same people in the middle part of the country, because we were near to winning the war. And I just think that as you criticize what the Government is doing, that you’ve got to take a look at history and see, over long run history, what people have done.

MR. CARTY: We’re compelled as airlines to have our systems interface with the Government computer that has the profiling, but it isn’t our profiling algorithm. And we simply do what we’re told. The question I think that Bill makes is good, but it’s the Government’s debate over what the algorithm can look like, what is appropriate, and what’s not appropriate. I think that’s public policy.

MR. COLEMAN: You take the instance where that person took his children in New Hampshire, drove them across the country. Well, he was picked up only because he used a credit card, and they had the credit card and they sent out the word, and that’s how they picked them up. And if you can make the argument that if the Government had been able to get every
credit card and found out that the 19 people were flying across the country using credit cards, paying for their training and pick that up, I think it’s kind of hard to say, well, gee, that’s an invasion of privacy if that saved 3,000 lives. So I really think this is a real debate, but I really think, as you look at it, that everybody has to really examine what the issues are and what the result ought to be based upon this recognition as the threat changed.

MR. ATTANASIO: Well, we better conclude this at this point. I want to thank Al Casey for organizing this. I want to thank our distinguished parties for being with us today. Thank you.
Comments