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October 5, 1994

The Honorable Anne K. Bingaman
Assistant Attorney General
Antitrust Division
United States Department of Justice
10th Street and Constitution Avenue, N.W.
Washington, D.C. 20530

Re: Request for Business Review by
<u>Business Travel Contractors Corporation</u>

Dear Ms. Bingaman:

On behalf of our client, Business Travel Contractors Corporation ("BTCC"), we are submitting this request to the Antitrust Division for a Business Review pursuant to 28 C.F.R. § 50.6 (1994).

BTCC is a new corporation formed to increase the array and availability of air travel for American businesses by creating an opportunity for BTCC customers to purchase domestic (i.e., within the 48 continental states) air transportation services on a net fare basis. Because such net fares should reduce travel costs and increase competition in the air transportation industry, BTCC believes that its actions are fully consistent with the antitrust laws, and should be so recognized by the Department.

In support of its request, BTCC provides the following information:

BTCC is a privately-held corporation, formed in 1994. Its business address is 900 East Eighth Avenue, Suite 300, King of Prussia, Pennsylvania 19406. BTCC is owned by its management employees. No air carrier or potential BTCC customer has, or will be permitted to acquire, any ownership interest in the BTCC.

BTCC reflects the vision of a number of individuals with significant experience as business travel managers, who formed the new company to provide enhanced travel services to the business community. Chief among these services, and the primary focus of this business review request, is BTCC's intent to create an opportunity for its customers to purchase domestic air transportation services on a net fare basis.[1] It seeks to do so by entering into agreements on behalf of these customers with any participating airline that is willing to offer domestic air transportation services on the terms described below.

This new method of purchasing air travel represented by the net fare concept responds to the increasing corporate frustration with the present business travel environment. American businesses have seen significant increases in their business travel expenditures, particularly air transportation, in recent years. Although they have attempted to deal with this problem in a number of ways, including the adoption of elaborate corporate travel policies and the negotiation with airlines of selective discounts from published fares, the fundamental problem of spiraling costs remains.[2]

Purchasing business travel on a net fare basis is a response to this concern. It seeks to reduce the costs and increase the efficiency of domestic business air travel in a number of ways: (1) by eliminating (or "unbundling") commissions, overrides,[3] and frequent flyer program costs from the purchase of air transportation services;[4] (2) by reducing the internal costs of operating and

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[1] As required by the Department's policies concerning business review letter requests, these activities represent only proposed business conduct on the part of BTCC, which has not yet implemented the contemplated activities. See 28 C.F.R. § 50.6.

[2] Indeed, some of the attempted "solutions" such as implementation of corporate travel programs may themselves have further increased costs by requiring significant investments in personnel and data necessary to monitor and enforce the programs. In many instances, these efforts are only marginally successful in controlling costs. See, e.g., Jonathan Dahl, "Many Bypass the New Rules of the Road," Wall Street Journal (Sept. 29, 1994) at B1, col. 3 (recounting employee efforts to circumvent corporate travel policies).

[3] Override commissions or overrides are payments to travel agents in addition to the relatively standard 10 percent of fare value paid by airlines for travel agent services on domestic tickets. In their most common form, overrides are a percentage commission paid on sales by a travel agent of a specific airline's tickets above some benchmark. This benchmark is usually relative to the travel agent's sales of the airline's tickets to sales by other travel agents in the same area of that carrier's tickets. In most cases, overrides are an attempt to shift market share.

[4] A key aspect of the BTCC proposal is that the travel agent will be compensated by the buyer, and not by the seller as is currently the case. This change should have a number of

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managing corporate travel departments, which will no longer be necessary in their present form to monitor compliance with corporate travel policies; and (3) by creating a simplified fare structure for the purchase of business travel, which eventually should facilitate more efficient means of making reservations, issuing, and delivering tickets.

BTCC hopes to play a key role in this cost reduction effort. It will attempt to obtain, on behalf of its customers, the opportunity to purchase net fares from any air carrier willing to offer such fares throughout its domestic route system. Such net fares, which BTCC has named for discussion purposes "Business Contract Fares," are intended to have several distinctive characteristics:

(1) the fares will be net of commissions, overrides, frequent flyer programs or other inducements (e.g., upgrades) to corporate employees, and other direct marketing costs;

(2) the fares will be available on all domestic city pairs served by a participating airline;[5]

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[4](...continued)
implications: (1) to the extent that BTCC customers can negotiate agreements with travel agents for booking, ticketing, and other services for less than the current 10-15 percent commissions/overrides received by the travel agents from airlines and reflected in ticket prices paid by the corporation, the corporation's total air transportation expenditures should decline; (2) to the extent that current override commissions and other airline marketing programs bias agents toward booking travelers on more expensive flights, this bias will be eliminated and the corporation will save the difference from the more expensive flight; and (3) with the travel agent's incentive to bias the ticketing process eliminated, it may be possible to reduce or eliminate current costly monitoring systems to ensure compliance with corporate travel policies. Similarly, the elimination of frequent flyer awards and other traveler incentives should reduce the tendency of travelers to seek flights based on award mileage rather than schedule convenience and/or price and also will eliminate the costs of oversight and monitoring of employee conduct.

[5] Unlike current corporate discount programs, which generally offer discounted fare availability only on selected city pairs, Business Contract Fares will be offered on all flights, and thus should eliminate the effort currently associated with identifying the most attractive fare options that may or may not be available for any particular city-pair routing. There is, however, no minimum or threshold number of city pairs in which a carrier must offer service in order to contract with BTCC; thus, a new start-up carrier serving only a limited number
(continued...)

(3) the fares will be available for a specified period of time (eighteen months is currently contemplated), and will be subject to adjustment only for fuel price changes;[6]

(4) the airlines' agreement with BTCC will establish the maximum fare that can be charged as a Business Contract Fare by that airline on a particular city pair; the airline remains free, in response to competitive conditions or otherwise, to charge any fare below that maximum fare at any time; and

(5) the fare structure that will be proposed to individual airlines by BTCC will be based on and reflect recent actual corporate travel costs, minus marketing expenditures, and will be primarily mileage-based.

The need for lower fares and greater simplicity in the business travel area has been widely discussed in recent years and a number of initiatives have attempted to deal with the problem. In preparing to launch its new business, BTCC undertook a detailed review of this issue and became convinced that the problem facing corporate travel departments was not simply rising fare levels alone. The time and effort required to search for the lowest fares, the monitoring of employee travel to ensure that such fares were in fact utilized, the oftentimes contrary incentives of travel agents (lured by desire to meet override thresholds or the prospect of higher commissions on higher fares), and individual employee travelers (lured by frequent flyer programs and other marketing incentives) all combined to defeat cost containment efforts.

BTCC anticipates that by introducing an additional purchasing option not currently available, the Business Contract Fare concept will increase choices and reduce the total air transportation costs of its corporate customers. BTCC further anticipates that its proposal should present an attractive opportunity for other industry participants such as airlines and travel agents. From the airlines' perspective, the net fare concept will allow them to avoid commission, override, and other marketing expenditures that may

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[5](...continued)
of city pairs will be just as able to participate as the largest established air carrier. For each, the only requirement is that both offer the Business Contract Fare on all domestic city-pair routes they fly.

[6] Again, this period of guaranteed fare availability is intended to reduce search and transaction costs in making travel decisions. The knowledge that the Business Contract Fare cannot be greater than a specified amount on any particular city pair provides needed certainty with respect to the purchase decision and is a critical element in helping corporations plan and budget for future travel expenditures.

increase their costs of doing business without necessarily producing increased volume commensurate with their efforts. For travel agents, net fares will permit a shift to fee-based reimbursement systems, which may help alleviate the current limitations of commission-based reimbursement.[7] Thus, the activities of BTCC should serve to promote competition in all industry sectors.

The mechanics of how BTCC intends to implement the net fare concept are straightforward. BTCC will act on behalf of its corporate customers in obtaining the agreement of air carriers to offer Business Contract Fares pursuant to the terms described above. It will work with other industry participants such as computer reservation systems to adopt the steps necessary to purchase air transportation using net fares in a simple and convenient manner. It will make the information about the existence of such fares and the procedures necessary to utilize them available to its customers.[8] The actual purchase of specific air transportation services (including flight reservations, ticket delivery, etc.) and the payment for such services will be handled directly between a BTCC customer, its travel agent, and an individual air carrier.

In order to ensure a volume of transactions making it worthwhile for airlines to offer Business Contract Fares, BTCC customers will commit to use Business Contract Fares for at least 90 percent of their business travel on city-pair routings for which such fares are available.[9] A customer will not be required to make any commitment regarding the likely extent of air travel on any individual city pair or on a particular airline; the volume commitment is simply intended

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[7] Because commission-based reimbursement results in significantly lowered revenues (for the same efforts) when fares are lowered, travel agents are finding that their cash flow and budgets increasingly are at the mercy of airlines' marketing efforts. As tickets fall into the $50 to $100 price range, agents may find that their commission does not even cover out-of-pocket expenditures associated with making a reservation and issuing a ticket. Moreover, by simplifying the fare search and by eliminating extraneous influences on itinerary selection process (such as frequent flyer awards), the Business Contract Fare concept should ease some of the current work load pressures on travel agents.

[8] A contractual agreement with BTCC will be necessary for a corporation to purchase Business Contract Fares and BTCC will charge its customers for the services it provides.

[9] Depending on the number of participating air carriers, it is possible that Business Contract Fares will not be available on all city pairs. If a BTCC customer does not, over the course of the initial contract period, meet its volume commitment (as measured by reports to the BTCC staff) the customer's agreement to participate in BTCC will not be renewed.

to reflect the customer's anticipated use of Business Contract Fares as a whole.

In essence, BTCC will function as a joint buying group to promote the more efficient purchase of business air travel. In order to avoid any concerns with possible buyer power, the only possible competitive concern raised by such joint buying activity,[10] BTCC intends to limit the total number of customers it will serve. It will take steps to ensure that, as a group, its customers collectively account for less than 35 percent of the purchases of air transportation services in any relevant market.[11]

At present, BTCC's customer commitments fall comfortably within this guideline. To date, sixteen corporations have committed to become BTCC customers.[12] Although it is hoped that the business of BTCC's customers will present an attractive business opportunity to airlines,[13] these corporations are likely to represent an exceedingly small proportion of potential purchasers of air travel generally or even of business air travel. No matter how the market is calculated,[14] these customers do not represent a significant

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[10] Because BTCC customers do business in a wide variety of industries and, for the most part, are not direct competitors, there is no likelihood that their participation in a buying group will lead to any reduction in competition in the markets in which they do business.

[11] In a number of contexts, including (most recently) the Statements of Antitrust Enforcement Policy and Analytical Principles Relating to Health Care and Antitrust, the Department has expressed the view that buying groups representing less than 35 percent of potential purchasers are unlikely to give rise to any competitive concern, where, as here, the good or service to be purchased represents less than 20 percent of the selling price of the finished good or product. Statements of Antitrust Enforcement Policy and Analytical Principles Relating to Health Care and Antitrust, U.S. Dept. of Justice and Federal Trade Commission (Sept. 27, 1994).

[12] A list of these companies is provided in Attachment A. Confidential treatment pursuant to 28 C.F.R. § 50.6 is requested for Attachments A, B, and C because they contain confidential and proprietary information of BTCC and its customers.

[13] Current BTCC customers average approximately 1,900 daily passengers. See note 15 infra.

[14] In previous analysis of air transportation issues, the Department has consistently used city pairs as the relevant product and geographic market for analyzing competition issues. While the Department has recognized that there may be important
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share, much less 35 percent, of any relevant market.[15] If air transportation were viewed as a nationwide market, current BTCC customers account for less than one-half of one percent (0.44 percent) of all air travel purchases.[16] Nor do they represent a significant share of purchases for any individual airport or city pair, as demonstrated by the more detailed analysis provided in Attachment B. The analysis contained there is based on BTCC customers' recent purchases of domestic air travel; BTCC anticipates that these past purchases offer a useful indicator of future air travel purchases by BTCC customers.

As its business becomes established and the benefits to its customers become apparent, BTCC hopes to attract additional customers for its services. In so doing, however, BTCC will ensure that the additional volume of air travel purchases represented by new customers does not cause BTCC to exceed the 35 percent threshold. With the exception of this overall size restriction, there are no other limitations or restrictions on the customers who can purchase services from BTCC, although it is anticipated that the companies most likely to utilize BTCC's services will be larger corporate entities with significant business travel needs.[17] Nor are there

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[14](...continued)
differences between the demands of business travelers and those of leisure travelers, it has not, to our knowledge, faced an occasion where the definition of a separate business or leisure market was central to its analysis.

[15] In part, this is the natural result of the geographic dispersion of the participating customers. To illustrate this point, a list of the headquarter cities of current BTCC customers is presented at Attachment C.

[16] Using actual travel data for its customers for the period January-April 1994, BTCC calculated this figure by comparing BTCC customer traffic of 1,884 passengers per day each way ("PDEW") with the first quarter 1994 industry total (derived from the Department of Transportation's Origin & Destination ("O&D") survey) of 430,957 PDEW. As discussed in Attachment B, the use of four-month data for BTCC customers versus the three-month O&D survey has the effect of overstating the BTCC customer share.

[17] In considering this business letter review request, the Department should, in the view of BTCC, consider not just BTCC's current customer base but also the anticipated growth in the number of its customers, not to exceed the 35 percent level. While the Department through the business review process is generally willing to provide an expression of its enforcement intentions only with respect to the structure currently before it, it has in the past indicated that as long as a proposed venture maintains its operating rules as presented and keeps its
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any aspects of the BTCC's operations that would prevent other entities from seeking to offer similar services to other customers.

BTCC is sensitive to the need to prevent its operations from becoming a conduit or opportunity for the exchange of price information among participating air carriers. For this reason, among others, it has and will in the future conduct all discussions with air carriers on individual basis. It will not transmit, comment on or otherwise share information concerning one carrier's plans to any other carrier. In launching its service, BTCC also has decided not to utilize requests for proposals in soliciting agreements from air carriers to offer Business Contract Fares. Instead, BTCC will prepare a fare proposal derived from recent actual corporate purchasing experience and present that proposal, as an expression of the terms on which its customers are willing to purchase air transportation services, to each interested U.S. airline, which may decide to participate on a nonexclusive basis. By utilizing such methods, BTCC hopes to avoid any suggestion of collective negotiations or information sharing with participating airlines.

There will be no limit on the number of airlines that can agree to offer Business Contract Fares. Although existing carriers will have to express their intent to participate by a specified date,[18] new entrant airlines can begin offering Business Contract Fares as soon as they initiate operations. An airline's decision to offer Business Contract Fares will not impose any restrictions on that airline's ability to offer the same or lower fares to any other customer, nor are any other agreements intended that would in any way restrict competition among the participating airlines.

One consequence of the BTCC initiative and its net fare proposal is that travel agents will no longer receive commissions or other marketing compensation from airlines on tickets sold pursuant to a Business Contract Fare. In purchasing travel utilizing Business

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[17](...continued)
membership below some stated appropriate level (e.g., 35 percent), the Department will not challenge the proposal. See, e.g., Business Review Letter to National Cardiovascular Network, Inc. (Sept. 28, 1993). BTCC specifically requests that the Department express its view concerning the anticipated growth of BTCC's customer base.

[18] This fixed sign-up date is aimed solely at ensuring the orderly launch of the Business Contract Fare concept. After this initial sign-up period, BTCC will likely establish additional sign-up periods during which existing air carriers can agree to participate. (The precise frequency and timing of these sign-up periods remain to be determined, but it is anticipated they will occur approximately once a year.) As noted previously, new air carriers can agree to participate as soon as they begin operations.

Contract Fares, the purchasing corporation (i.e., the BTCC customer) will be responsible for reimbursing the travel agent for any services provided such as making the reservation, printing the ticket or physical delivery of the ticket. The precise nature of the services to be provided to individual customers and the amount they will pay travel agents for these services will be determined through negotiations and agreements between the travel agent and the individual corporate customer. BTCC will not be involved in arranging for these services, in suggesting any prices or fees, or in negotiating the terms of any such agreements. It is reasonable to expect that different customers will be interested in different levels of service, and this may create the opportunity for a broader range of travel agencies to compete for the BTCC customers' business.

As a customer-led initiative, BTCC is aimed at reducing costs and increasing efficiency in the purchase of business air travel, and thus is unlikely to raise any antitrust concerns. It might be asked, however, why BTCC's involvement and action on behalf of a group of companies is necessary in order to introduce the net fare concept and make it work. Why couldn't any interested company seek to obtain net fares on its own without the aid of an apparent middleman?

The simple answer is that, despite widespread interest in and support of the net fare concept, individual companies have been unsuccessful in their efforts to convince airlines to offer them the opportunity of purchasing domestic air transportation on any type of an unbundled or net fare basis.[19] Even the single largest United States corporation does not represent a sufficient volume of business to convince airlines to undertake the steps necessary to offer such fares. These include not only the business risks associated with the concept but also the direct and indirect expenditures necessary to implement the net fare concept. Even if an airline were willing to assume the risk of implementing a net fare program, it probably would be unlikely to do so for a single corporation (even one of its largest customers) because it would not find it worthwhile to create a separate and unique set of procedures to cover just one customer -- no matter how big. Only by offering a larger business opportunity, i.e., the prospect of a number of major U.S. corporations as potential customers, will it be possible to convince an airline to undertake the risk and work associated with a new way of doing business.

BTCC customers, it is hoped, will represent such an opportunity. By uniting in a single entity an attractive volume of business, BTCC

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[19] IBM's unsuccessful effort earlier this year to purchase air travel services net of any frequent flyer program benefits is simply the most recent example. See, e.g., Jennifer Lawrence and Bradley Johnson, "IBM Fails to Ground Frequent Flier Efforts," Advertising Age (Mar. 14, 1994), at 44; William J. McGee, "Miles for Discounts Might Still Happen," Business Travel News (Mar. 31, 1994), at 1.

and its customers are relying on market forces to attract the interest and participation of a sufficient number of carriers to make the net fare concept work.

In addition, from the customers' side, there are various costs that must be incurred in implementing the net fare concept and making it work. These costs are more efficiently borne by BTCC, on behalf of all its customers, rather than being incurred by each company individually. To offer maximum benefits, the net fare concept requires the participation of a significant number of airlines. While individual companies, on their own, might not find it worthwhile to invest the effort and resources necessary to organize and implement this effort, these costs are much more manageable (and hence attractive) when undertaken on behalf of a larger group. BTCC, through its key management employees and consultants, also brings considerable industry background and skills to the process of obtaining the agreement of various airlines to offer net fares.

The activities of BTCC and the introduction of net fares such as the Business Contract Fare cannot cause a reduction of competition in any market. Indeed, by increasing choices in the sale and distribution of air transportation services, it should promote competition and thereby benefit the consumers of air transportation services.

While BTCC believes that the information accompanying this request is fully sufficient for purposes of the Department's inquiry, it is, of course, prepared to provide any additional information requested by the Department. Please contact me at (202) 879-4668 or Kathryn Fenton at (202) 879-3746 if you have any questions concerning this request or require any additional information. We look forward to a prompt and favorable response to this request for a Business Review.

Sincerely,

Phillip A. Proger /KMF

Phillip A. Proger

Kathryn M. Fenton

Kathryn M. Fenton

Enclosures

cc: Roger W. Fones, Esq.

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