

October 20, 2000

Hon. A. Douglas Melamed  
Acting Assistant Attorney General  
Antitrust Division  
Department of Justice  
950 Pennsylvania Avenue, NW  
Washington, DC 20530

Dear Mr. Melamed:

Pursuant to the Antitrust Division's Business Review Procedures, 28 C.F.R. §50.6, Delta Air Lines, Inc. (Delta) and Société Air France (Air France) (collectively the "Parties") submit this business review request in connection with a proposed joint venture to create an air cargo alliance for international shipments out of the United States. Initial founding partners will be Delta, a Delaware corporation, and Air France, a corporation organized and existing under the laws of France. Other air cargo carriers may be invited to join at a later date.

This letter requests the Antitrust Division's position only with respect to the Delta-Air France combination, and the Parties recognize that each additional air carrier that seeks to join the joint venture could be subjected to a separate review. In conjunction with this business review request, the Parties are submitting for your review all specified information and documentation required under the Antitrust Division's pilot program, 58 FR 6132.

#### **I. Nature and Purpose of the Agreement**

Delta and Air France are planning to enter into a cargo joint venture for all of their international air cargo shipments that originate in the United States, principally to Europe, but to other international destinations as well, such as Mexico, Latin America and Asia/Pacific. The Joint Venture ("JV") will not, initially, include air cargo shipments to Canada.

The purpose of the JV is to combine the carriers' strengths to enable them to augment their services and to reduce the costs of air cargo service that each Party individually provides and to create additional value for the parent companies. The JV will not be an airline and all freight shipments will continue to be transported on the airway bills of the Parties. The JV will offer customers access to a larger, combined network through a single point of contact. It also will offer one range of products to better serve customers' needs. The objective is to accomplish this by managing the marketing and selling of the entire capacity each carrier has available to sell on U.S.

export flights (passenger and freighter). This includes the parent companies' own flights as well as capacity that is made available to the parent companies by other airlines. As a result, from one source the customer (based on current schedules) will have access to: non-stop service to 33 destinations in Europe, Latin America, Japan; connecting service through Paris to many destinations in Europe, Africa, the Middle East and Asia; and direct freighter service from three U.S. gateways. The JV will increase the ability of Delta and Air France to compete in the international freight marketplace.

An independent joint venture company ("JVC"), known as *DALAF CARGO, LLC*, will be created by the Parties to implement this joint venture. The JVC will be organized in the State of Delaware and have a principal place of business in Atlanta, Georgia. The Parties will appoint a Board consisting of an equal number of executives from each parent to control the JVC. The Board will control the business operations of the JVC and will be charged with such tasks as providing strategic guidelines, specifying products to be marketed, setting the budget including revenue targets, and approving new partners and major contracts.

To ensure integration of the Parties' air cargo networks, the JVC will provide marketing and sales services to all of the Parties' international cargo business (excluding Canada) out of the United States, including but not limited to product definition (e.g., express, pallets/containers, oversized freight, etc.), marketing, sales, reservation, space control and yield management. The JVC will market and sell the entire freight capacity of both parties available on international flights outbound of the United States.

The JVC will be managed by a CEO who will be appointed by and be responsible to the Board and who will be assisted by an experienced team of individuals currently employed by both Parties (primarily from the U.S.-based international sales departments of the Parties) and new hire personnel. The JVC management will be responsible for all day-to-day decisions of the JVC including securing office space, negotiating contracts with shippers and forwarders and its parent airlines, and will operate largely independent of the Parties. However, the JVC management will also be allowed to draw on the experience and resources of the Parties.

The JVC will be organized as a limited liability company (LLC) owned equally by Air France and Delta, and will record at most a nominal annual profit or loss. Instead, sales revenue will continue to be collected directly by the airline parent that issued the airway bill. The JVC's source of revenue will be an operating fee charged to the parents to cover the costs of its operations. Synergies produced by the JVC as a result of increased revenue and/or decreased costs for each of the Parties will be determined and shared by the Parties. This benefit sharing model and the cost sharing formula are outlined in the JV agreement. Start up costs for the JVC will be shared equally by the Parties.

The JV will be for an initial term of ten years with a right by either party to terminate after five years by providing notice of termination one year prior to the fifth anniversary. There

are other termination provisions, including in the event of breach of the JV agreement, or if the JVC does not attain the goals set for it by the founding Parties.

At the outset, the JVC will market the combined Delta and Air France capacity on the following flights planned to be effective for the summer 2001 period:

- 14 weekly Air France all-cargo flights from the U.S. to France (including four weekly flights via Prestwick or Shannon).
- 134 weekly Air France combination flights from the U.S. to France.
- 291 weekly Delta combination flights from the U.S. to Europe (including 35 weekly flights to France).
- 187 weekly Delta combination flights to Mexico, Central and South America and Asia/Pacific.
- 4 weekly Air France all-cargo flights from the U.S. to Mexico City, and
- 4 weekly Air France combination flights from the U.S. to Papeete, French Polynesia.

To sell the cargo space, the JVC will have one centralized call center located in Atlanta which will concentrate the technical and commercial expertise regarding cargo availability on the outgoing international flights of both airlines. By combining the resources of the two existing cargo reservation operations of Air France and Delta, the JV will seek to achieve a higher level of cost productivity and to provide a higher level of service to its customers. In addition to this centralized call center, customers will be able to reach their local sales representatives in each of the four regional sales areas, each led by a regional sales director.

The JVC will seek to offer a single drop off point and warehousing activities at each U.S. gateway. This will make delivery of shipments easier for the customer and allow the Parties to consolidate facilities to reduce costs.

## **II. Ability and Incentive of Joint Venture and Parties to Compete**

While each of the Parties agrees to recognize the JVC as its exclusive representative and marketer of international export cargo services, given the governing and management structure of the JVC, the Parties will retain little day-to-day business control over the JVC. As stated earlier, the Board is charged with the tasks of providing strategic guidelines, specifying products to be marketed, setting the budget including revenue targets, and approving new partners and major contracts, and determining pricing and output levels.

The JV agreement provides that the Parties will remain autonomous and reserve their respective independent decision making authority. To that end, the Parties are able to schedule their passenger aircraft fleets as each deems commercially advantageous. Air France also has an air freighter fleet. With regard to these aircraft (and freighters owned by any other carrier that subsequently joins the JV), the Board will determine the optimal integration and scheduling of flights operating from the United States, provided that the freighter aircraft operator will retain the right to decide, for sound commercial or operational reasons, to alter the schedules determined by the Board. There will be no changes in the manner in which Delta and Air France operate pursuant to their passenger code sharing agreement and, for the most part, the carriers' representatives to the JVC Board will not be involved in the day-to-day business of air passenger service.

### **III. Relevant Market and Market Shares**

The market that will be served by the JV will be the U.S. export market, primarily U.S. - Europe, for both general freight and express freight. U.S. - Europe is a relevant market for the purpose of this analysis because while all airlines are restricted as to where they can fly, almost all cargo moves to its destination on a connecting basis, with connections to another flight, a trucking service or both.<sup>1</sup> In Europe in particular, where the countries are relatively small geographically and internal borders are open, a great deal of air cargo destined for, e.g., France, is trucked in from airports in neighboring countries. Moreover, unlike passengers, cargo shippers generally do not care whether their shipments are on a nonstop flight. Their principal service concern is that the cargo gets to its destination in good condition and on time, and their primary interest is the shipment price. This is true in particular of freight forwarders and brokers, who account for a significant percentage of transatlantic air cargo shipments. Thus, there is no question that in the air cargo market connecting service competes with nonstop service. In such a market pricing is regional rather than local and the region is at least as large as Europe.

Both Delta and Air France presently have small shares of the U.S. - Europe air cargo market. The airlines are only two of approximately 85 major and minor air passenger and cargo carriers that compete for this business. Major airfreight competitors of Delta and Air France in the market described above include large airlines with dedicated freighter capacity such as Lufthansa, Swisscargo, and KLM as well as the integrators such as Federal Express and United Parcel Service. Air France operates 12 B747 freighters. Delta does not operate any freighters. Both carriers sell belly space on a space available basis on their passenger flights as do the numerous U.S. and foreign carriers operating combination flights on the transatlantic routes (e.g., American, British Airways, Continental, Northwest, U.S. Airways, Virgin Atlantic, etc). Delta and Air France are limited in the air cargo service they can offer. Delta cannot operate a local air cargo network within Europe; Air France cannot operate within the U.S. or nonstop generally from the U.S. to countries in Europe

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<sup>1</sup> The Parties' share of the overall U.S. export international air cargo market (e.g., transpacific, Latin America/Caribbean) is very small and will not separately be analyzed here. U.S. - Europe and U.S. - France are analyzed because they are the only "markets" in which the Parties' combined share is significant.

other than France. National airline ownership laws and bilateral civil aviation agreements do not allow airlines to merge operations to form multinational airline companies similar to the multinational companies that have formed in other industries. International airline alliances, a number of which have received antitrust immunity, are the next best substitute. Thus, the JV will also compete with established immunized joint ventures that cover transatlantic cargo services such as KLM-Northwest, United-Lufthansa-SAS and American-Swissair-Sabena.

As evidenced by the attached Exhibits, Delta's and Air France's combined shares of the U.S. - Europe market and of air cargo to all of Europe are quite small, ranging from 12.1% to 12.7% from 1997-2000 (first quarter) for Europe. Exhibit 3. Other than France, there is no major US-Europe country market in which Delta's and Air France's combined share of the air cargo market is greater than 20%. (The very small US-Greece market is an exception with combined shares in the 25% to 30% range in some years). Exhibit 7. Every market, including France, is served by many other carriers either via nonstop flights or indirectly via online or interline connections or via truck. *Id.* The carriers' largest combined share is, of course, in France, but even there the carriers' combined share ranges from 32.2% to 35% from 1997-2000 (first quarter). Exhibit 4. Moreover, United, Continental, Federal Express, and American Airlines all have larger percentages of U.S. - France air cargo shipments than Delta.<sup>2</sup> Exhibits 5-7.

In the case of France, antitrust immunity may not be available until 2003 (when all civil aviation restrictions in the market will expire) because the current civil aviation agreement is not Open Skies and, in any event, the JV currently plans to operate without antitrust immunity (subject to Business Review clearance). However, as far as air cargo is concerned, the remaining bilateral restrictions do not constitute a meaningful barrier to free and open competition in cargo services. As of April 2000 there are no restrictions on routings, frequencies or prices charged for cargo services between the U.S. and France. Exhibit 9, Air Transport Agreement. Four U.S. cargo carriers are authorized to provide U.S.-France operations as of April 2000 (one is limited to French points other than Paris), in addition to the eight U.S. combination carriers and numerous third-country European carriers that serve the U.S.-France market via their homeland hubs. Federal Express operates 13 weekly freighters from the U.S. to Paris (CDG) and it operates a hub at CDG for shipments beyond Paris.

The high degree of current competition also is evidenced by the Parties' top ten customer lists, which are attached as Exhibit 8. While in a few cases both Delta and Air France serve the same customer, in no instance is the same customer the largest customer for both of them for

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<sup>2</sup> The competitors' market share information is based on the Department of Transportation T-100 data. The Delta and Air France market share numbers may be inflated when using the Department of Transportation T-100 data given that the T-100 reflects all freight transported on flights to a European country regardless of the true origin and destination of the shipments and given that virtually all Air France shipments to Europe are via France. Thus Air France's market share in the US-France market under the T-100 information reflects all air cargo going to any destination in Europe.

service to the same country. For example, AEI and Emery are the largest Delta customers for air cargo to France in 1999; BAX and SDV were the largest Air France customers for that year. *Id.*

#### **IV. Pro-competitive Benefits**

At present, the air cargo business is an adjunct to Delta's and Air France's passenger business. Schedules are largely dictated by passenger concerns and, on any given flight, cargo space is limited. Cargo sales personnel are often limited to selling only the space available on specific flights, and they lack the information and network they need to route cargo via alternative routings where pricing and availability might be better. The objective of this joint venture is to expand cargo sales inventory through the formation of an air cargo network that will pool the capacity and sales forces of its member airlines. The joint venture will have access to the full cargo capacity of its parent airlines, enabling it to sell more frequent service and to shift shipments to make space available for time sensitive or large shipments of cargo. Customers will further benefit by being able to deal with one entity for their service needs, and the parent airlines will benefit from having one source to deliver a consistent marketing message focused on the U.S. export market.

The combined sales force will have a stronger presence in the U.S. market through a new geographical organization that will provide more complete coverage than either Delta or Air France offers today. This will allow more sales calls to more shippers by sales people who are able to offer all of the JV Parties' services. In this way the transaction process will be both streamlined and more productive.

The JVC will sell the network of each Party airline together as one network. It will combine the strengths of each Party's network into one comprehensive network that can address all the needs of the customers. The JVC will offer both capacity in the bellies of nonstop passenger flights from a number of U.S. gateway cities to 22 cities throughout Europe and main deck, large capacity freighter service from 3 U.S. cities to Paris (CDG). Today Delta operates a transatlantic network that links 3 U.S. gateways with 22 European destinations, while Air France operates from 12 U.S. gateways --3 with freighters--to its hub at Paris (CDG). With the JV Delta will no longer have to route a Los Angeles customer's shipment to Paris cross-country to ATL or JFK to connect with a Paris flight; with the JV, that shipment could go nonstop on Air France's Los Angeles flight. By the same token, an Air France customer's urgent shipment to Germany can be routed directly on the Delta Frankfurt nonstop rather than going first to Paris, to then be trucked into Germany. This 'gateway' factor produced by the JV's synergies will enhance service offerings to customers making service both more "frequent" and more "direct" thus creating value for both customers and the airlines.

In short, there will be more flexibility in routing according to a particular customer's needs: direct flights for more urgent shipments, freighters for heavy, oversized shipments, and increased options of indirect service for less urgent shipments. The JVC will establish a set of network management principles that outline what types of freight, what routing, and what airline to use to optimize the combined networks of the Parties. These principles will serve as a guide only and will not predetermine the acceptance and routing of any individual shipment.

Since the objective of the JV is output expansion, the venture will have pro-competitive effects. The Parties will be able to increase their small market share only if they are able to offer high quality service at a very competitive price. While pursuant to this arrangement Delta and Air France will no longer compete for the transportation of air cargo from the United States, eliminating that competition is essential to the joint venture's success. The JV could not succeed without including Air France's U.S.-France capacity, since that is virtually all of the capacity that Air France has to offer.

## V. Legal Analysis

The JV meets all of the criteria of a legal joint venture. *See, e.g., Arizona v. Maricopa County Medical Soc.*, 457 U.S. 332, 356-57 (1982). Before approving a joint venture, the Department of Justice and Federal Trade Commission evaluate whether the joint venture will result in any of the following anti-competitive effects on the market: (1) a significant increase in market concentration or a concentrated market power; (2) adverse effects on competition; (3) barriers to entry into the market, and (4) a failure to achieve significant net efficiencies. *1992 Horizontal Merger Guidelines*. None of these effects will result from this JV.

The JV also satisfies the *Antitrust Guidelines for Collaborations Among Competitors*, issued in draft by the Federal Trade Commission and the Department of Justice on October 1, 1999. Section 3.3 of the *Guidelines* describes the rule of reason analysis that will be applied here, and it looks at the following factors: (1) the nature and purpose of the agreement; (2) the absence of market power; (3) the market share and concentration; and (4) the pro-competitive effects of the agreement, *i.e.*, whether the agreement harms competition by increasing the ability or incentive profitably to raise prices or reduce output, quality, service, or innovation below what would prevail in the absence of the agreements. This agreement is between two carriers that combined will have a relatively small share of nearly every possible relevant market and in the market where their share is significant, entry and output expansion is easy. Indeed, in all except the U.S.-France market, the combined shares will fall well within the safety zone for competitor collaborations reflected in Section 4.2. The JV thus will not create or enhance any market power. It will, however, create a more effective air cargo competitor, which is why the JV should not be challenged.

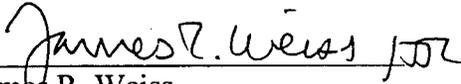
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Acting Assistant Attorney General  
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**VI. Conclusion**

As previously stated this review request, along with the supporting documentation, is being submitted under the Antitrust Division's pilot program. The Parties request prompt consideration of their request, and hereby state that they have conducted a good faith search for the requested information and documents and have provided all responsive material.<sup>3</sup>

Please contact either one of the below-signed if you would like any additional information concerning this matter.

Sincerely,



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cc: Roger W. Fones, Esq.  
Enclosures

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<sup>3</sup> The documents submitted as Exhibit 2 to this letter are business plans relating to the joint venture and which contain confidential business information relating to each party's services and customers as well as future plans and strategies. The parties respectfully request that these documents remain confidential pursuant to 28 CFR 50.6 section 10(c), as their disclosure would have a detrimental effect upon each party's operations.