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THE WHITE HOUSE
WASHINGTON

June 26, 1976

MEMORANDUM FOR: ED SCHMULTS
FROM: JIM CONNOR
SUBJECT: Service to Saipan CAB Case

The attached letter was received from the Department of Transportation after the President made his decision on the Service to Saipan CAB Case.

It is forwarded to you for recommendations on handling.

Attachment:

John W. Barnum's letter of 6/25/76

original to E.S.

Sent to file 7/7/76



THE DEPUTY SECRETARY OF TRANSPORTATION
WASHINGTON, D.C. 20590

June 25, 1976

MEMORANDUM FOR THE PRESIDENT

SUBJECT: Service to Saipan Case

In reaching a decision on the Saipan Case, it may be useful for you to have an expanded explanation of why the Department of Transportation believes that the actual experience on the route to be awarded should be monitored carefully and that the policy of economic viability of international routes should be reaffirmed. (As a former director of Pan Am, Bill Coleman has delegated DOT responsibility on this case to me.)

In your November 11, 1975, letter to the Board you stated: "It is important to our foreign policy that our U. S.-flag carriers be viable and that routes awarded should be economic." You asked the Board to address the economic viability of the Saipan-Japan route, and they have done so in their second opinion. This is a major step forward and, consistent with the new Section 801 procedures you have announced, we do not suggest that you disapprove the award merely because DOT and the Board arrived at different conclusions with respect to the viability of the route.

Differences in economic forecasting methodology do not raise foreign policy issues. The basic concept--that international routes must be economically viable--is, however, a matter of foreign policy concern for at least two reasons.

First, and most importantly, the strength of the U. S. flag international air transportation system depends on the continued existence of privately owned, efficiently operated and profitable U. S. carriers. In contrast to many countries, the U. S. government does not subsidize its international air carriers. If our carriers are to maintain their presence in the international system, operations which sap their financial vitality must be avoided.

Secondly, the award of new international route authority to a U. S. carrier immediately brings into play the bilateral framework within which international air transportation operates. Thus decisions on entry and capacity raise issues that must be negotiated between governments. It does not serve the interest of the United States to be put in a position where foreign governments can seek a valuable

right for their carriers as a consequence of our granting an uneconomic route for one of ours. While this may not be a matter of concern in the instant case, it demonstrates the intermingling of foreign policy and economic issues when uneconomic routes are awarded.

Given the policy that international routes should be economically viable, it follows that those which are not viable and which do not have a reasonable prospect of being viable in the near term should not be served. In the Saipan Case, the usual uncertainty of forecasting economic performance is exacerbated by lack of experience on the route. The Board believes that Continental/Air Micronesia would earn a small operating profit of \$125,000 on the route in 1977, but the Board also recognizes that its economic estimate is uncertain.

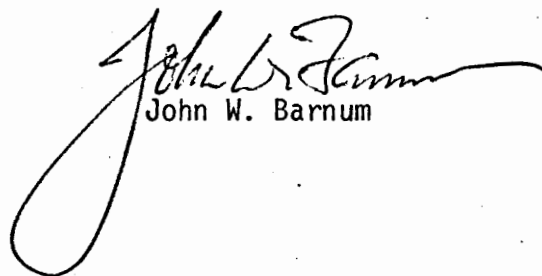
We recommend a monitoring procedure so that, in the event the Board's expectations prove to be unduly sanguine, we can be assured that action will be taken to prevent the continued operation of an uneconomic service which undermines the U. S.-flag system. Unless a monitoring process is begun at your formal suggestion, the practical chance that any agency would be able to persuade the Board to suspend the route after several years is very small.

Although DOT believes that the Saipan-Japan route will prove to be uneconomic and that future action to correct that situation will be necessary, we do not believe that this route should be subject to requirements more stringent than those generally applicable to international routes. Therefore we recommend that your letter to the Board with respect to this case contain a statement concerning the applicability of the policy of economic viability to all international routes.

This is particularly important because the Board presently has under consideration a number of international route cases, including the North Atlantic Route Proceeding involving all routes in that heavily traveled sector of the air system. As often happens, a basic Administration policy statement--in this instance that of the importance of economic viability--has been announced in the context of a particular case. To avoid the possible necessity of returning a number of recommended decisions to the Board for consideration of this important foreign policy element, your letter to the Board in this case should reaffirm the basic policy as being applicable to all international routes. DOT suggests, therefore, that your letter also advise the Board that you will transmit to them in the near future a statement as to how the policy is to be applied to new and existing routes. They will then be on clear notice that economic viability is to be considered an integral part of all international route decisions.

Your decision in the Saipan Case will be the first to come after the new Executive Order on Section 801 procedures. Many will examine it carefully as illustrative of the concerns which receive Presidential attention. Having stated the policy of economic viability in your November 11 letter, a failure to restate that policy now might lead some to conclude that economic viability is not of Presidential concern under Section 801. The economic viability of airline routes is just such an issue of foreign economic policy with diplomatic implications. Finally, your November letter expressing that policy has since been applauded by U. S. and foreign flag carriers, foreign governments and the U. S. financial community, which has been greatly troubled by the financial weakness of our two principal international carriers, and a perceived retreat from that position might be viewed as significant.

I think it is significant that the Department of State, NSC and CIEP concur in our recommendation.



John W. Barnum