

**INITIAL REGULATORY FLEXIBILITY ANALYSIS**  
**FOR**  
**PROPOSED CONSUMER RULEMAKING**  
**REGARDING**  
*TRANSPARENCY OF AIRLINE ANCILLARY FEES*  
*AND OTHER CONSUMER PROTECTION ISSUES*

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For

**The United States Department of Transportation**

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## ACRONYMS AND ABBREVIATIONS

ANPRM – Advance Notice of Proposed Rulemaking

BLS – Bureau of Labor Statistics

BTS – Bureau of Transportation Statistics

CPI – Consumer Price Index

FAA – Federal Aviation Administration

NPRM – Notice of Proposed Rulemaking

NPV – Net Present Value

OMB – Office of Management and Budget

OTA – Online Travel Agent

RIA – Regulatory Impact Analysis

TMC – Travel Management Company

## EXECUTIVE SUMMARY

This document presents the Initial Regulatory Flexibility Analysis to accompany the US Department of Transportation's (the Department) Notice of Proposed Rulemaking (NPRM) to enhance airline passenger protections in relation to: the display of airline-imposed ancillary service fees; customer service plans for ticket agents; code-share disclosure; and expanding the pool of carriers that report information to the Department, and the information they report. As directed by the Regulatory Flexibility Act of 1980, as amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA), as well as Executive Order 13272, the Department is required to consider the potential impact of its regulations on small entities, including small businesses, small nonprofit organizations and small governmental jurisdictions.

The Department has explicit authority to protect consumers from unfair or deceptive practices and to ensure safe and adequate service in air transportation. The Department has published Final Rule in both 2009 and 2011 aimed at enhancing airline passenger protections. The 2009 and 2011 Rules were met with strong positive consumer response and have been followed by significant improvements in some measures of airline performance (such as notable decreases in lengthy on-tarmac delays).

Yet the Department continues to receive significant numbers of complaints regarding transparency of air ticket price, fee and information, and indications of complaints regarding travel agencies related to the sale of air travel. In addition, the United States Government Accountability Office (GAO) has issued two reports which make recommendations regarding the need for greater price and fee transparency for air travel purchases.<sup>1</sup>

The DOT believes that regulation is warranted to ensure fair advertising and communication of critical information to air travel consumers as well as minimum customer service standards such that consumers are protected from unfair treatment.

This Rule will impact small carriers. For regulatory evaluations, small carriers are those that operate service with planes with 60 or fewer seats.<sup>2</sup>

Provisions 3 and 4 are estimated to impact three small carriers and cost \$0.9 million in the first year and \$1.9 million over ten years (discounted at 7%). Provision 2 is estimated to impact approximately 87 carriers at a cost of \$3.2 million during the first year and \$23.8 million over a ten year period (discounted at 7%). The total estimated impact is thus \$5.1 million in the first year and \$24.7 million over ten years.

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<sup>1</sup> *Airline Passenger Protections: More Data and Analysis Needed to Understand Effects of Flight Delays*, Sept 2011 and *Consumers Could Benefit from Better Information about Airline-Imposed Fees and Refundability of Government-Imposed Taxes and Fees*, 2010.

<sup>2</sup> See 14 CFR Chapter 11. Note that the Small Business Administration definition of small carriers is not used.

## 1. Introduction

This document presents the Initial Regulatory Flexibility Analysis to accompany the US Department of Transportation's (the Department) Notice of Proposed Rulemaking (NPRM) to enhance airline passenger protections in relation to: the display of airline-imposed ancillary service fees; customer service plans for ticket agents; code-share disclosure; and expanding the pool of carriers that report information to the Department, and the information they report.

The Regulatory Flexibility Act of 1980, as amended, requires Federal agencies to conduct a separate analysis of the economic impact of rules on small entities. The Regulatory Flexibility Act requires that Federal Agencies take small entity's particular concerns into account when developing, writing, publicizing, promulgating, and enforcing regulations. To this end, the Act requires that agencies detail how they have met these concerns, by including an (Initial and later a Final) Regulatory Flexibility Analysis (RFA). The Initial RFA must include:

1. A succinct statement of the need for, and objectives of, the rule.
2. A description and an estimate of the number of small entities to which the rule will apply (or an explanation of why no such estimate is available).
3. A description of the compliance requirements of the rule and their costs.
4. A description of the steps the agency has taken to minimize the significant adverse economic impact on small entities.

## 2. Reason for Agency Action

The Department has explicit authority to protect consumers from unfair or deceptive practices and to ensure safe and adequate service in air transportation. The Final Rules published in 2009 and 2011 aimed at enhancing airline passenger protections were designed to ensure minimum levels of consumer comfort and customer service, and more transparent information flow between consumers and air carriers. The Department undertook these rulemakings in response to a history of persistent flight delays, significant on-board delays, increasing customer complaints, and a report by the DOT Inspector General in 2000 which concluded that carriers had not done enough to ensure minimum passenger care. The 2009 and 2011 Rules were met with strong positive consumer response and have been followed by significant improvements in some measures of airline performance (such as notable decreases in lengthy on-tarmac delays).

Yet the Department continues to receive significant numbers of complaints regarding transparency of air ticket price, fee and information, and indications of complaints regarding travel agencies related to the sale of air travel.

In addition, the United States Government Accountability Office (GAO) has issued two reports which make recommendations regarding the need for greater price and fee transparency for air travel purchases. In September 2011, the GAO issued a report, *Airline Passenger Protections: More Data and Analysis Needed to Understand Effects of Flight Delays*, which recommended that DOT "collect and publicize more comprehensive on-time performance data" and suggested requirements similar to two of the provisions of this Rule ("requiring airlines with a smaller

percentage of the total domestic scheduled passenger service revenue, or airlines that operate flights for other airlines, to report flight performance information.”)

The GAO’s July 2010 report, *Consumers Could Benefit from Better Information about Airline-Imposed Fees and Refundability of Government-Imposed Taxes and Fees*, included recommendations that DOT gather greater information on carrier fees, issue additional requirements to gather greater information on carrier fees, and ensure that the disclosure of baggage and other optional fees and that such information “be consistently disclosed across all distribution channels used by the airline.” This recommendation is very similar to provision 6 of this proposed Rule.

The DOT believes that regulation is warranted to ensure fair advertising and communication of critical information to air travel consumers as well as minimum customer service standards such that consumers are protected from unfair treatment.

### **A Balanced Approach to Air Travel Information Transparency**

If the market for airline services met textbook definitions of “perfect competition” and “perfect rationality,” consumers would bring about “welfare-maximizing” outcomes through their role in the automatic dynamics of demand and supply. Product attributes such as customer service and airline transparency about prices and conditions of supply would satisfy consumer expectations without the need for government regulatory intervention.

The ability to access full information related to a transaction, whether or not each consumer actually does access and use that information, is a pre-requisite of “perfect competition.”

Yet, the volume of passenger complaints regarding certain attributes of customer service and product transparency convinces the Department that the market is not, at present, delivering welfare-maximizing outcomes. But it is not certain whether this is the result of imperfect competition (such monopoly or oligopolistic behavior) or imperfect rationality (i.e. just businesses making ‘bad’ or not smart choices). The difference between the two is not trivial and helps dictate the degree to which government intervention is warranted. If monopolistic behavior of the airlines (or GDSs) were the main reason behind the consumer issues examined here, a strong or ‘aggressive’ regulatory response would be justified. On the other hand, if airlines or GDSs are simply behaving, as consumers often do, with a degree of myopia, short-sightedness or other such “heuristics” of real-life, then the preferred approach would be one that seeks the basic consumer protections through minimal government intervention, allowing the forces of the marketplace to work to greater market efficiency.

The Department reached out extensively to air travel stakeholders, including individual carriers, airline trade associations, and consumer groups. Considerable comment and significant disagreements were voiced on provision 2, regarding the display of ancillary service fee information. Some stakeholders presented the department with the argument that monopolistic practices (such as price shrouding and obfuscation) explain the absence of full disclosure and transactability of ancillary service fees on GDSs and OTAs. Other evidence suggests that airlines are exhibiting a form of behavior known as myopia, in which they focus on

the short-run benefits (greater control of access to customers, or decreased fees to GDSs) to their long-term detriment (greater overall consumer satisfaction and demand).

The airline industry is concentrated among a small number of firms, which itself might create the conditions for monopolistic behavior. On the other hand, the federal government deregulated the airline industry in 1978 on the grounds that, while the industry is indeed concentrated, the market for air travel is sufficiently “contestable” to sustain competitive outcomes. The Department of Justice is examining this issue further.

The poor market outcomes being witnessed today in terms of product transparency and transactability are at the partially the result of what Behavioral Economists call rationality-limiting heuristics – essentially decision-making short cuts that are based on previous experience, not on a rational examination of all possibilities – though they could also be the product of more anti-competitive behavior. Research conducted for this analysis was inconclusive regarding the degree to which observed industry behavior is only a result of myopia; or delayed contesting actions by some carriers; or of a fundamental problem with current industry structure. Therefore, it is recommended that the Department adopt an incremental approach, one that will hopefully ‘nudge’ carriers, GDSs and travel agents into developing a private industry-based solution.

### **3. Proposed Regulation**

In this rulemaking, the Department is considering further enhancing the protections afforded to passengers in several areas:

1. Clarify and incorporate into regulation the definition of a “ticket agent” under USDOT regulations;
2. Require that carriers provide the necessary information regarding their basic ancillary service fees to either:
  - All ticket agents to whom they provide flight purchase information so that the ticket agents can display those ancillary service fees; or
  - All ticket agents to whom they provide flight purchase information and that sell air transportation (provision of information to GDSs not required)
3. Expand the pool of carriers that report on-time performance, mishandled baggage, denied boarding and oversales data to the Department (often called “reporting carriers”) from carriers which account for at least 1.0% of domestic scheduled passenger revenues (as currently required) to those carriers which account for at least 0.5% of domestic scheduled passenger revenues;
4. Expand reporting requirements for reporting carriers to include that the carriers file an additional set of reports that includes their domestic code-share partners’ on-time performance, mishandled baggage, denied boarding and oversales data;
5. Set minimum customer service standards for ticket agents (similar to those required of carriers);

6. Ensure the disclosure of code-share segments in all marketing carriers’ schedules, advertisements and communications with consumers;
7. Additional display requirements for ticket agents to disclose to consumers all carriers marketed (for which the Department is only seeking comments and not proposing rule text):
8. Prohibit undisclosed display bias by ticket agents; and
9. Prohibit post-purchase price increase of baggage fees in connection with the broader prohibition on post-purchase price increases.

In the Regulatory Impact Evaluation prepared to accompany the Proposed Rule, the Department considered adopting, or not adopting, each component individually, as well as three alternative scenarios to specific provisions which were considered but not proposed. These provisions, plus the three alternative scenarios are summarized in the table below.

**Table 1: Proposed Provisions and Alternatives**

Provision	Requirement Description
1	Definition of Ticket Agent
2	Carriers provide basic ancillary service fee information to ticket agents: either to all ticket agents to which it provides its fare information, including GDSs, or all ticket agents to which it provides its fare information, if the ticket agent sells to consumers
Alt C	<i>Carriers provide ancillary service fee information to ticket agencies and GDSs, so that consumers can purchase ancillary services from ticket agencies/GDSs</i>
3	Expand the definition of a “reporting carrier” to one which accounts for at least 0.5 percent of domestic scheduled passenger revenues (the current requirement stipulates only carriers with at least 1.0 percent of domestic scheduled passenger revenues)
4	Expand reporting requirements for reporting carriers to include an additional, combined set of reports for both the carrier’s own flights and its code-share partners flights’ on-time performance, mishandled baggage, and denied boarding and oversales
Alt A	<i>Expand the definition of a “reporting carrier” to include all those which account for at least <b>0.25 percent of domestic scheduled passenger revenues.</b></i>
Alt B	<i>Expand reporting requirements for reporting carriers to include an additional, separate set of reports which contains data only for carriers’ code-share flights</i>
5	Minimum customer service standards for ticket agents
6	Disclosure of code-share segments in schedules, advertisements and communications with consumers
7	Disclosure of carriers marketed by ticket agents
8	Prohibition on undisclosed biasing
9	Prohibition of post-purchase price increase for ancillary service fees

#### **4. Types and Numbers of Affected Small Entities**

This Rule will impact small carriers. The Department defines small carriers based on the standard published in 14 CFR 399.73: “For the purposes of the Department’s implementation of chapter 6 of title 5, United State Code (Regulatory Flexibility Act), a direct air carrier or foreign air carrier is a small business if it provides air transportation only with small aircraft as defined in § 298.3 of this chapter (up to 60 seats/18,000 pound payload capacity).”<sup>3</sup>

Small travel agencies and tour operators are explicitly excluded from the provisions that might otherwise impact them.

Several provisions of this Proposed Rule apply only to “reporting carriers,” so called because of specific requirements to report additional information to the US Department of Transportation. Reporting carriers must report information to BTS monthly on lengthy tarmac delays, on-time performance, and baggage handling, and or quarterly for denied boarding and oversales and incidents relating to transport of animals. Currently, reporting carriers are those carriers with at least 1% of domestic scheduled passenger service revenues. As the airline industry has undergone consolidation in recent years, the number of reporting carriers in the U.S. has decreased from 16 carriers in 2011 to 13 carriers in 2012 (Table 2). In the past two years, United has acquired Continental, ExpressJet has acquired Atlantic Southeast, and Southwest has acquired AirTran. Among the current 13 reporting carriers, six are mainline carriers (Alaska, American, Delta, Hawaiian, United, and US Airways), four are low-cost model major airlines (Frontier, JetBlue, Southwest, and Virgin America), and three are regional carriers (American Eagle, ExpressJet, and SkyWest).

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<sup>3</sup> See 14 CFR Chapter 11. Note that the Small Business Administration definition of small carriers is not used.

**Table 2: Reporting Carriers: Domestic Passenger Carriers (At Least 1.0% Of Domestic Scheduled Passenger Revenues), 2012**

2012 Reporting Air Carriers:	
1	Alaska
2	American
3	American Eagle
4	Delta
5	Frontier
6	Hawaiian
7	Jet Blue
8	Sky West
9	Southwest /AirTran*
10	United/Continental*
11	US Airways
12	Express Jet/ Atlantic Southeast*
13	Virgin America

Notes; U.S. air carriers that have at least one percent of total domestic scheduled-service passenger revenues.

\* indicates Airlines that were merged. Comair was a reporting carrier in 2011, but no longer is one in 2012.

Source: US DOT

The reporting carriers represent a substantial portion of the entire market in the U.S. While reporting carriers only reflect approximately a fifth of carriers with scheduled passenger service in the U.S., they account for nearly 60% of all departures and more than 80% of all enplanements (see Table 3).

**Table 3: Scheduled Passenger Service on U.S. Carriers (domestics and international), 2010**

	Carriers		Departures		Enplanements		Avg. Enplanements per Departure
	Number	Percent of Total	Number	Percent of Total	Number	Percent of Total	
Reporting Carriers	13	22%	6,032,139	59%	604,351,061	82%	100
Other U.S. Carriers	46	78%	4,153,659	41%	130,830,733	18%	31
<b>Total</b>	<b>59</b>		<b>10,185,798</b>		<b>735,181,794</b>		<b>72</b>

Source: Air Carriers: T-100 Segment (US Carriers Only), 2010, RITA, TranStats

These figures also indicate that a substantial minority of carriers (78%), departures (41%) and enplanements (18%) relate to carriers which do not report much of the additional statistics to BTS which allow the government and consumers to better understand carrier performance.

Provision 3 would expand the definition of a reporting carrier to those with at least 0.5% of domestic passenger service revenues. This would require some small carriers (as per the definition used for regulatory analyses) to begin collection and reporting additional data to BTS, to post additional information on their website, and other requirements to which they were previously not subject. Provision 4, expands the reporting requirements for all reporting carriers (under old and new definition), which also impacts some small carriers. Table 4 lists those carriers which would newly become ‘reporting carriers’ under the proposed rule, as well as the carriers which would become ‘reporting carriers’ under an alternative scenario which was not adopted.

**Table 4: Additional Small Airlines If Extend the “Reporting Pool”**

	Airline Name	Minimum Passenger Seats per Departure
<b>Additional Carriers (under 0.5% threshold)</b>	AIR WISCONSIN	50
	HORIZON	70
	MESA	37
	PINNACLE	49
<b>Additional Carriers (under 0.25% threshold)</b>	COLGAN	34
	MESABA	34
	PSA	50

Source: BTS, T-100 Segment data, calculated by HDR study team, 2011.

Several of the provisions differentiate between marketing and non-marketing carriers and/or their code-share partners. In 2010, there were 59 U.S. carriers provided scheduled passenger and cargo services within, to and from the U.S. Approximately half of those carriers sell tickets directly to the public and are thus considered ‘marketing carriers.’ Carriers that do not sell tickets directly to the public operate their flights under code-share agreements with other marketing carriers and are listed on the contracting carriers’ schedules. For example, among the 13 reporting carriers, three carriers do not sell tickets to the public and operate flights for their code-share partners: American Eagle operates flights for Alaska, American and Delta; Sky West operates flights for Airtran, Alaska, Delta, United and U.S. Air; ExpressJet operates flights for United and U.S. Air and Delta. A few small regional carriers, such as Mesa and Great Lakes, operate both under contract and independently-marketed flights.

## 5. Impacts on Small Entities

**Provision 1** is a codification and clarification of an accepted use of the term ticket agent, and as such is not expected to have any impact on any small carriers or ticket agents.

**Provision 2** would require that carriers provide information on their ancillary service fees to ticket agents. This provision is expected to cost an average of approximately \$36,000 per carrier, a figure which was originally estimated for large carriers. Since this provision will apply to all carriers that market tickets in US, small carriers would be impacted.

For this analysis, the number of impacted small carriers is estimated using previous calculations of the share of total number carriers which are classified as small carriers. According to analysis prepared for the Enhancing Airline Passengers Protections (EAPP) II, approximately 52% of U.S. carriers' fleets only contained aircrafts with less than 60 seats in 2009.<sup>4</sup> Assuming that 52% of the current estimated number of carriers that would be impacted are small carriers (87 carriers), the estimated costs to those small carriers would total \$3.2 million for the first year and \$23.8 million over a 10-year period (discounted at 7 percent).

**Table 5: Estimated Costs for Small Entities to Provide Ancillary Service Fee Information to Ticket Agents**

<b>Small Entities</b>	<b>2013-2022</b>	<b>2013</b>
Number of Impacted Carriers	167	167
% of carriers are small carriers	52%	52%
Estimated number of small carriers impacted by provision	87	87
Annual labor hours to provide information to ticket agents	8.00	8
Hourly Labor Cost for Reporting	\$90.10	\$97.97
Annual cost each airline needs to pay to ATPCO to transmit ancillary service fees to GDS	\$36,000	\$36,000
<b>Total Component Costs (millions)</b>		
<i>Total Component Undiscounted Costs (millions)</i>	\$31.7	\$3.2
<b><i>Total Component Discounted Costs (millions) (7%)</i></b>	<b>\$23.8</b>	<b>\$3.2</b>

Under the proposed **Provisions 3 and 4**, the total estimated costs to small carriers would be \$0.9 million for the first year and \$1.9 million for a 10-year period (discounted at 7 percent) if the reporting carrier threshold is 0.5% of domestic scheduled passenger service revenues. The costs to small carriers would be up to \$1.4 million for the first year and \$3.9 million for the 10-year study period (discounted at 7 percent) if the threshold were to be changed to 0.25% of domestic scheduled passenger service revenues, an alternative considered by the Department but not adopted.

If Provision 4 requires marketing and code-share data to be reported in a combined format, there would be no extra cost for those new impacted reporting carriers as they don't market their code-share partners' tickets.

<sup>4</sup> U.S. DOT, Consumer Rulemaking: Enhancing Airline Passenger Protections II, 2011

**Table 6: Estimated Costs for Small Entities if Extending the Reporting Threshold to 0.5%**

<b>Small Entities (0.5% reporting threshold)</b>	<b>2013-2022</b>	<b>2013</b>
Newly added carriers that has plane less than 60 seats (0.5% threshold)	3	3
Set-up costs (large carriers only)	\$100,762.91	\$100,762.91
Hourly Labor Cost for Reporting	\$96.87	\$90.10
Annual Hours for Form 234 On-time Performance per Carrier	538	480
Annual Hours for Form 251 On-time Performance per Oversales per Carrier	16	16
Cost of Posting Delay Information on Line	<b>\$419,394.32</b>	<b>\$419,394.32</b>
Number of New Reporting Carriers that market their own tickets	<b>1</b>	<b>1</b>
<b>Total Component Costs (millions)</b>		
<i>Total Component Undiscounted Costs (millions)</i>	\$2.3	\$0.9
<b>Total Component Discounted Costs (millions) (7%)</b>	<b>\$1.9</b>	<b>\$0.9</b>

**Table 7: Estimated Costs for Small Entities if Extending the Reporting Threshold to 0.25% (Alternative Provision 3)**

<b>Small Entities (0.25% reporting threshold)</b>	<b>2013-2022</b>	<b>2013</b>
Newly added carriers that has plane less than 60 seats (0.25% threshold)	7	7
Set-up costs (large carriers only)	\$100,762.91	\$100,762.91
Hourly Labor Cost for Reporting	\$96.87	\$90.10
Annual Hours for Form 234 On-time Performance per Carrier	538	480
Annual Hours for Form 251 On-time Performance per Oversales per Carrier	16	16
Cost of Posting Delay Information on Line	<b>\$419,394.32</b>	<b>\$419,394.32</b>
Number of Newly Reporting Carriers that market their own tickets	<b>2</b>	<b>2</b>
<b>Total Component Costs (millions)</b>		
<i>Total Component Undiscounted Costs (millions)</i>	\$4.9	\$1.4
<b>Total Component Discounted Costs (millions) (7%)</b>	<b>\$3.9</b>	<b>\$1.4</b>

**Provision 5** applies only to travel agents or tour operators with annual revenues of more than \$100 million, which explicitly excludes small entities.

**Provision 6** is already in enforcement, and thus should require no new compliance efforts by small carriers.

**Provision 7** is only seeking comments, and therefore no costs are estimated.

**Provision 8** applies to the display of airfare information by ticket agents. The cost of this provision is not estimated in this RIA.

**Provision 9** prohibits post-purchase in increases in ancillary service fees applies to the display of airfare information by ticket agents. The cost of this provision is not estimated in this RIA. As the Department is proposing to codify existing guidance, all carriers are supposed to be complying with the substance of the requirement already and there should be no additional costs or benefits from this provision

**Table 8: Total Estimated Costs for Small Entities Under All Provisions**

Provision	Discounted Costs (millions) (7% discount rate)	
	2013-2022	2013
Provision 1	n/a	n/a
Provision 2	<b>\$23.8</b>	<b>\$3.2</b>
Provisions 3 and 4	<b>\$1.9</b>	<b>\$0.9</b>
Provision 5	n/a	n/a
Provision 6	n/a	n/a
Provision 7	n/a	n/a
Provision 8	n/a	n/a
Provision 9	n/a	n/a
<b>TOTAL</b>	<b>\$25.7</b>	<b>\$4.1</b>

## 6. Reporting and Recordkeeping

Provision 3 of this Rule would require small carriers to report information to BTS monthly on lengthy tarmac delays, on-time performance, and baggage handling, and or quarterly for denied boarding and oversales and incidents relating to transport of animals.

Provision 4 of this Rule would require small carriers to provide additional data for the code-share partners as well as for themselves as part of the regular monthly and quarterly reporting to BTS.

Provision 5 of this Rule, which would require large travel agents to adopt minimum customer service standards, does not to apply to small ticket agents.

## **7. Alternatives Considered and Steps Undertaken to Minimize Impact on Small Businesses**

The Department has taken several steps to minimize the impact on potentially affected small entities:

- For Provisions 3 and 4, the Department considered but did not adopt an alternative scenario in which 0.25% of domestic scheduled passenger service revenues.
- For Provision 5, which requires customer service standards for ticket agents, the Department explicitly excludes small ticket agents but specifying that the requirement applies only to ticket agents with revenues of over \$100 million annually.

DOT believes that potential costs to small carriers are not significant, and notes that most passengers fly with large carriers. DOT considered several alternatives to exempt small carriers from the Rule. One alternative covered only carriers that operate service with at least one aircraft of 60 or more seats, and thus, no small carriers. Another alternative which considered and then incorporated into the proposed rule, required customer services standards only for large travel agencies.