

Orders for the ERJ-170 & ERJ-190 by USAirways jetBlue and the financial restructuring of several major US carriers may have given the impression that pilot union scope clauses would be relaxed, giving way to new orders for large regional jets. The opposite has happened, and majors are the likely future operators of 70-100 seat regional jets.

The evolution of US regional scope clauses

Scope clauses have been the subject of bitter confrontation between airline management and the unions representing the pilots in the major US airlines. Scope clauses set out the number and size of regional jets (RJs) that a major airline permits its regional airline affiliate to operate. The speed with which scope clauses have evolved has dictated the rate of introduction of 50-seat RJs into regional carriers.

With the manufacturers' attention now turning to RJs larger than 50 seats, how will scope clauses affect the prospects for 70-100 seat RJs in the US? This article examines the evolution of the current scope clauses in order to predict the short- to medium-term market prospects for 70-100 seat RJs.

Background

Alaska Air/Horizon Airlines

Horizon Airlines is the only major regional operator in the US not constrained by a scope clause. Bombardier benefits from this through orders for its CRJ701, with the original purchase for 25 aircraft increased to 30 before two were converted to Q400 turboprop orders. Despite the lack of scope clause restrictions, further CRJ701 orders are unlikely.

In September 2003 Horizon signed an agreement with Frontier to operate regional flights as Frontier JetExpress from 1st January 2004. An initial fleet of four CRJ701s will increase to nine by 30th May.

In November 2003 Horizon revised its outstanding order for 14 CRJ701s by swapping two of them for Q400s, and then extending the delivery schedule for the remainder by reducing deliveries to only two a year until 2009. This suggests that about half of Horizon's existing

CRJ701 fleet will be transferred to the Frontier JetExpress operation.

American Airlines

American Airlines was one of the first airlines to make RJ scope clauses a public issue. In 1997, the airline's management made RJs for American Eagle a condition of contract negotiations. A strike was narrowly avoided following Presidential intervention, the airline got a scope clause allowing American Eagle up to 67 RJs with 50 seats and some with 70 seats, but there was no limit placed on the number of regional jets with 44 seats or less. In exchange, however, American's mainline pilots received a 9% pay rise over five years (double the initial offer) stock options and a no-furlough clause for the life of the contract. There were also a number of restrictions on the deployment of the RJs. At least 85% had to be used on routes that fed hubs, certain markets were excluded and they could not replace American jets on profitable routes. Following this, 42 ERJ-145s and 25 CRJ700s were ordered in 1997.

In the expectation that the scope clause limits would be relaxed, and in order to maximise its RJ fleet while awaiting the CRJ701s, American placed additional orders for eight ERJ-145s in 1998. In further anticipation, American ordered six more ERJ-145s in 1998.

In 2000 American proposed a new scope clause to its mainline pilots. This would have limited American Eagle to RJs with 50 seats or less in exchange for no limitations on the number that could be operated. American was effectively trading its 25 CRJ701s for an unlimited number of 50-seaters, but the proposal was rejected by the mainline pilots. Instead American placed its launch order for 130 44-seat Embraer ERJ-140s, because there was no limit on RJs of this size.

This is another example of the effect of scope clauses on the market for RJs. As well as dictating the overall rate of market growth, scope clauses have led to specific aircraft being designed to circumvent them. For example, the ERJ-140 is a unique, 44-seat version of the 50-seat ERJ-145.

Not only has the Embraer ERJ-140 been developed for American, but the CRJ440 has also been developed for Northwest.

Towards the end of 2002 American's combined deliveries of Embraer ERJ-145s and CRJ701s were going to exceed the 67 aircraft limit, and it was forced to return 14 ERJ-145s to their lessor. These aircraft were subsequently leased to Trans States Airlines for operation as American Connection.

The next major development came in 2003 as part of a package of pilot concessions to help American Airlines avoid bankruptcy. American Eagle will be allowed to operate 110 RJs with a seat capacity of up to 50 seats for every 100 mainline aircraft operated. The mainline fleet currently totals about 600, and so American Eagle could therefore operate 660 RJs of up to 50 seats. In return, the existing CRJ701s will be transferred to the mainline operation. This will have little impact on the small RJ market, since American will simply swap its outstanding orders for Embraer ERJ-140s to -145s. It will be a serious blow to Bombardier's chances of placing more CRJ700s, however.

The fight to operate the CRJ700s has put American's mainline pilots, represented by the Allied Pilots Association (APA), in direct conflict with the pilots at American Eagle represented by the Airline Pilot's Association (ALPA).

The APA, a union exclusively for American's mainline pilots, is determined to prevent the regionals encroaching on the mainline fleet's operation.

ALPA, the USA's largest pilot union,

As part of an agreement allowing an unlimited number of regional jets with less than 50 seats, American Eagle has had to concede operation of its CRJ700s to American Airlines. This is one example of a US major carrier ensuring that scope clauses do not become gradually relaxed over time.



which represents both mainline and regional pilots, is seeing its American Eagle members' prospects diminishing as the CRJ701s are returned to the mainline.

America West

One of the last airlines to see the introduction of scope clause limits was America West. Its pilots ratified a new labour contract that incorporated a scope clause in December 2003. Pilot unrest grew as a result of Mesa Air Group's expanding fleet of RJs, starting with 50-seat CRJ200s, then 64-seat CRJ701s and finally 84-seat CRJ900s. Details of the latest agreement are not yet available, but it is expected to limit the number of CRJ900s to the 25 already committed to. Similarly, small jet expansion is expected to be limited to existing commitments with further growth tied to mainline expansion.

Continental

Continental's only scope clause limitation has been on capacity, which is limited to 59 seats or less for jets and 79 seats for turboprops. The result has been the carrier's massive orders for ERJ-145s for its wholly owned subsidiary Continental Express, currently totalling 30 ERJ-135s and 245 ERJ-145s. The regional operation was subsequently renamed ExpressJet and then partially sold through an IPO.

ExpressJet is the only operator to have deferred RJ deliveries on commercial grounds rather than scope clause limitations. In February 2003 ExpressJet deferred deliveries for a total of 27 ERJ-145XR's. Under the agreement with Embraer, deliveries became 36 in

2003 instead of 48, 21 in 2004 instead of 36, 21 in 2005 instead of just 2, and the final eight in 2006.

Delta Airlines

Until 2001, Delta Connection carriers could operate an unlimited number of RJs with seat capacity up to 70. In 2001 the seat capacity limit was lowered to 50, except for 57 'grandfathered' CRJ701s. Delta Connection's total size was limited to a set percentage of the mainline operation. Delta is scheduled to receive the last CRJ701 on firm order before the end of 2004.

The seat capacity limit prohibits all Delta Connection partners from operating aircraft with more than 70 seats, even when they are operating under their own reservations code. The real effects of this aspect of the scope clause were highlighted by Atlantic Coast Airline's (ACA's) recent plans to be a low-cost, independent airline.

ACA currently operates 30 Fairchild Dornier 328Jets for Delta Connection. Under the terms of the Delta scope clause, Delta can terminate its contract with ACA within 180 days should it operate jet aircraft with more than 70 seats. This part of the scope clause is clearly an attempt to prevent regional operators from becoming mainline competitors. Although ACA is committed to the Delta contract, its decision to end its United Express operation and go it alone as Independence Air, with a fleet of 25 A319/A320s, will put ACA in breach of the scope clause it has with Delta.

Delta's labour relations were relatively trouble free until 26th March 2001 when Comair's pilots went on strike. They stayed out until 22nd June,

no less than 89 days, and operations did not resume until 2nd July. The pilots gained a five year contract with pay increased on average by 23-31%, and other benefits. Delta in turn introduced a policy of hub diversification with Atlantic Southeast Airlines and Atlantic Coast Airlines brought into reduce the Cincinnati hub's dependence upon Comair. In many respects this was not only a dispute between the airline management and its pilots, but between the pilots and their own union, ALPA, which represented both the mainline and regional pilots. Seeing their interests being sacrificed for the benefit of the mainline pilots, a number of ASA and Comair pilots formed the RJ Defense Coalition to bring a legal challenge against ALPA and its support of scope restrictions imposed upon them.

Northwest

Northwest's original scope clause agreement with its pilots was ratified in September 1998. In return for a 12% pay rise, stock options and profit sharing, the airline gained the use of RJs linked to the growth of the mainline fleet. A capacity limit of 60 seats applied, but there was no limit on the number of RJs with less than 44 seats. Northwest's scope clause 'grandfathered' 36 Avro RJ85s, although limited to 69 seats.

The agreement was followed in February 1999 by Northwest's order for 54 CRJ200s. The 'less than 44 seats' clause was subsequently used in July 2001 when Northwest ordered 75 CRJ440s (CRJ200s configured with 44 seats). All 129 RJ aircraft are currently earmarked for operation by wholly-owned subsidiary Pinnacle.

ORDERS FOR 70-100 SEAT JETS

Aircraft type	Airline customer	Ordered	Backlog
CRJ701	American Eagle	25	7
CRJ701	ASA	12	0
CRJ701	Brit Air	12	2
CRJ701	Comair	20	4
CRJ701	Delta Connection	26	20
CRJ701	Horizon Air	28	12
CRJ701	Lufthansa	20	0
CRJ701	Maersk Air Ltd	5	0
CRJ701	Mesa	15	0
CRJ701	Shandong	2	0
CRJ701	Skywest	30	30
CRJ705	US Airways	25	25
CRJ900	Mesa	25	17
EMB170	Air Caraibes	2	2
EMB170	Alitalia	6	6
EMB170	Cirrus	1	1
EMB170	GECAS	5	5
EMB170	LOT	6	6
EMB170	Swiss	15	15
EMB170	US Airways	85	85
EMB190	Jetblue	100	100
EMB190	Undisclosed	10	10
EMB195	Swiss	15	15
CRJ701		195	75
CRJ705		25	25
CRJ900		25	17
EMB170		120	120
EMB190		110	110
EMB195		15	15
Bomb.		245	117
Embraer		245	245
Total		490	362
Total	(operators only)	475	347

United Airlines

United's scope agreement, as ratified in November 1997, allowed for a maximum of 65 RJs of no more than 50 seats. Until 2000, only 30 RJs could be operated with growth. After 2000, RJ fleet growth was linked to mainline fleet growth, with three RJs for every narrowbody added to the mainline jet fleet.

In October 2000, agreement was reached to increase the number of small jets by up to 150 through the direct replacement of turboprops, but still limited to 50 seats. Further jets could be added if the mainline fleet grew beyond 451 narrowbodies and 141 widebodies.

In November 2002 United's pilots ratified a new contract which included the modification to the scope clause. This established a new formula for the number of RJs (still limited to a maximum of 50 seats) that could be operated by United's partners. Given a mainline fleet of 384 narrowbodies and 112 widebodies, the United Express RJ fleet could grow to 243 aircraft with a further 50 available as direct turboprop replacements.

Almost immediately after this scope clause relaxation, in December 2002, United entered Chapter 11 bankruptcy protection. United was then able to obtain even further concessions from its pilots, including the raising of the seat limit from 50 to 70 seats. This was contingent upon special employment rights, similar to US Airways's 'Jets for Jobs', for furloughed United pilots. The details of the agreement, and in particular the number of 70 seaters that can be operated, are unknown, but United has already signed agreements with Skywest for 30 CRJ701s and Mesa for 15 CRJ701s.

As part of their deal to fly CRJ701s for United, a fixed percentage of Mesa and Skywest's First Officer jet positions will be set aside for United pilots. Their starting pay will be nearly double that of Mesa and Skywest's other new hire pilots. United Airlines will pick up the difference.

Until its entry into Chapter 11, United Express services were provided by three operators: Air Wisconsin, Atlantic Coast Airlines (ACA) and Skywest. United has subsequently agreed new terms with Air

Wisconsin and Skywest, but failed to do so with ACA which has subsequently decided to operate independently with its fleet of CRJs to be joined with 25 A319/320s. The CRJs and 30 Jetstream 41 turboprops continue to operate for United while the latter is in Chapter 11 bankruptcy protection, since they are bound by contract, but ACA's United Express operation will cease when United emerges from Chapter 11. Although United has added Mesa Airlines, there is still a big question mark over how United will fill the gap left by ACA, and in particular the 87 CRJ200s it currently has in operation. One option would be to set up a new wholly-owned subsidiary like US Airways' Mid Atlantic subsidiary. While the operator of these 87 CRJ200s may be undecided, there will definitely be a new RJ market opportunity, with United's regional affiliates, which could extend to more 70 seaters.

US Airways

US Airways' struggle to introduce RJs is probably the best example of how protracted and difficult the process can be. Until 1997, jets were the exclusive responsibility of the mainline operation. Then the first opening was made with an agreement that independent operators could fly RJs, although its wholly-owned subsidiaries were still prohibited.

The maximum number of jets was limited to the greater of 35 RJs or a number equal to 9% of the aircraft in the US Airways mainline fleet. Only 12 jets could be operated in the first year, followed by 15 in the second and then 25 in the third. A further limitation was that no RJ could be operated on a route that had been served by mainline jets in the previous 12 months, if mainline pilots were on furlough. Surprisingly, given the tough stance taken on the number of aircraft, the upper seat limit provided by this scope clause was a generous 69 seats.

Increasing the scope limit became a major pre-occupation with US Airways' management, and they made this known when they stipulated a requirement for no less than 422!. In April 2000 the unions conceded an increase from 35 to just 70! It took until April 2002 before an agreement was reached to increase this further to 140. At the same time the wholly-owned carriers were finally allowed to operate jets with less than 51 seats, although only under a 'Jets for Jobs' agreement. This was on the provision that half of future RJ jobs must be given to furloughed US Airways pilots at either wholly-owned carriers or independent operators. These pilots receive the RJ Captain's pay rates of that specific airline, whether they fly as Captains or as First Officers.

As US Airways' financial position

In addition to 50-seat jets, under Chapter 11 United's management has managed to raise the aircraft size limit under its scope clause to 70 seats. Although the number of 70-seat aircraft permitted is not known, United has already signed agreements for 45 CRJ700s with two of its regional affiliates.

worsened, further negotiations continued. Immediately prior to the company's Chapter 11 filing on August 11th 2002 further scope clause concessions were obtained. The RJ limit for US Airways Express carriers was raised to 465, comprising 150 small SJs (defined by USAirways as aircraft of 44 seats or less), and 315 medium SJs (45-50 seats) or large SJs (51-70 seats and a maximum take-off weight (MTOW) of less than 75,000lb).

Despite the high SJ limit on capacity and MTOW, the Embraer ERJ-170 and ERJ-175 (MTOWs of 81,300lb and 82,700lb respectively) were specifically included in the agreement, although both were limited to a maximum seat capacity of 76.

The small SJs and the first 70 medium SJs could be operated by any US Airways Express carrier, whether independent or wholly-owned.

The next 70 medium SJs were required to go to wholly-owned carriers or independents participating in the 'Jets for Jobs' programme.

The large SJs were only to be operated by US Airways' newly created MidAtlantic Airways subsidiary and crewed entirely by furloughed US Airways pilots. A later agreement reduced MidAtlantic to a 'preferred' regional subsidiary, and the only one allowed to operate the ERJ-170/175s. Other carriers could operate small jets with less than 71 seats under the 'Jets for Jobs' programme.

US Airways subsequently placed orders for 25 CRJ705s (a CRJ900 configured with 75 seats) and 85 ERJ-170s. In a demonstration of how union power is 'down, but not out', the CRJ705 order was subsequently modified to CRJ701s. Despite ERJ-170s being acceptable for Mid Atlantic, the CRJ705's MTOW was in excess of the 75,000lb limit allowed under the scope clause. The CRJ701s will be operated by Mesa Airlines, which under the terms of its agreement, will provide a minimum of 25 and a maximum of 55 CRJ700s.

Current 70-100 seat RJ orders

Although there is a popular belief that Europe is the principal market for larger RJs, this is not supported by the order book for the current generation of 70-100 seat RJs. Of the 475 operator orders,



excluding the 10 ERJ-190s for an undisclosed customer and the five ERJ-170s for GECAS, 391 (82%) have been for US operators. Of these, Alaska Air Group's Horizon Air has 28, American Eagle 25, America West Express 25, Delta Connection carriers 58, United Express operators 45, and US Airways 110.

Aside from the mainline operators, JetBlue has a further 100 commitments for the ERJ-190. Europe only accounts for 80 and the rest of the world four.

In addition to the orders tabled above, Air Canada has signed Memoranda of Understanding with both Bombardier and Embraer for 30 CRJ705s and 45 ERJ-190s (with 30 options and 45 options) respectively. Like United and US Airways, Air Canada's management had the benefit of being able to re-organise under the Companies Creditors Arrangement Act, the Canadian equivalent of Chapter 11. Significantly, when it announced these orders, Air Canada also disclosed that an arbitration process would be set up to decide whether these aircraft were flown by Air Canada or Jazz pilots. As a result, the definitive orders that follow the manufacturers' two MoU may vary depending upon the outcome of this process.

Alaska/Horizon has no limit, but is already slowing deliveries of its existing outstanding orders. American Eagle has handed over the flying of 51 or more RJs to the mainline carrier. America West's new scope clause is likely to limit the number of large RJs to the 25 CRJ900s already committed. Continental and Northwest both have 60-seat limits within their scope clauses. Delta is limited to the 58 CRJ701s already on order.

This leaves only two operators with

the immediate potential of further orders: United and US Airways, both of which benefited from Chapter 11 re-organisation to renegotiate their scope clauses.

United Express' commitments include Skywest's order for 30 CRJ701s. Mesa will provide its existing CRJ701s. Any ultimate replacement for ACA's lost capacity will probably also include some 70 seaters. As well as Chapter 11, US Airways also had the financial muscle of GECAS behind them and has largely inherited GECAS' existing order for ERJ-170s. United's and US Airways' combined commitments account for 155 of the 475 confirmed airline orders to date and, more importantly, 140 of the outstanding order backlog of 347.

Mainline operators

One thing that should not be overlooked is that scope clauses do not place limits on the number of RJs that can be operated, they simply limit the number than can be operated by regional partners of major airlines.

The higher cost structures of mainline operators cannot be balanced against the relatively few revenue-generating seats of the smaller RJs. As the RJs get larger the revenue side of the equation improves and mainline operations begin to make more sense. Larger RJs also start to come into conflict with the A318 and 717.

American is in the process of retiring its once 75-strong fleet of Fokker 100s. This increases the gap between the ERJ-145s/CRJ701s and the next smallest aircraft in its fleet: the 140-seat MD-80. Given the large fleet of ERJ-145 family aircraft in service and this large capacity gap, Embraer may well have a strong



advantage in pushing its ERJ-170/190 family to American Airlines. Even with the 25 CRJ701s at American Eagle, Bombardier will be at a disadvantage in trying to place its aircraft.

America West remains a customer for the A318, with 15 on order. With Canadair CRJ900s at the lower end and A318s at the upper end, there is probably little scope for large RJs at America West.

Given the existing 59-seat scope clause limit, Continental could definitely be a candidate for mainline operation of larger RJs. Given the strong tie with Embraer for the existing RJ fleet, the ERJ-170/190 probably stand a good chance of entering service with Continental mainline initially to fill the gap between the ERJ-145s and 737-500s.

Delta Airlines, Northwest and United are all large CRJ operators. Delta has a large fleet of 737-200s and Northwest a larger fleet of elderly DC-9s to replace.

United has both A319s and A320s in service. The gap between the United Express scope clause of 70 seats and A319's 120 seats is arguably best filled with CRJ900s and A318s. Since the CRJ900s would have to be operated by the mainline, the A318 may have better prospects.

US Airways' scope clause already allows a substantial fleet of ERJ-170/175s, but the larger ERJ-190/195 would have to be operated by the mainline.

Given that US Airways has committed to the A320 family as the basis of its narrowbody fleet, it is going to be a battle between the ERJ-190/195 and the A318 for mainline orders. Commonality savings are driven more by pilot savings than anything else, so regional ERJ-

170/175 pilots would not be allowed to fly mainline ERJ-190/195s, thereby giving the A318 an advantage.

Low cost carriers

Jetblue's commitment to a fleet of ERJ-190s set a new precedent for the operation of 100 seaters by low-cost carriers, but will the others follow? Air Wisconsin is currently flying CRJ200s for low cost carrier Air Tran, but given Air Tran's commitment to the 717 there is probably little opportunity for the larger regional jets. The third and largest 'low-cost' operator, Southwest Airlines, has so far failed to move from its single type fleet of the 737. Even the USA's latest low-cost carrier, ACA's Independence Air, will be operating A320s rather than large RJs. Given the regional background of its owner, it might have been expected to have given more consideration to the larger RJs.

Swiss and US Airways

While Bombardier and Embraer continue to pursue new prospects for their RJs, at least two of their existing customers are far from solid. Swiss now only accounts for 30 ERJ-170s and -195s, and in November 2003, amid much speculation, Embraer announced that Swiss had requested a postponement of its order.

US Airways, with the support of GECAS, has managed to extract itself from Chapter 11, but there is still a significant risk that it will not survive.

The two carriers account for 140 of the outstanding backlog of 347 70-100 seat RJs.

Following negotiations while in Chapter 11, USAirways managed to get its scope clause widened to allow up to 315 45 to 70 seat regional jets. It subsequently ordered 85 ERJ-170s.

Conclusions

There is no doubt that demand exists for the new generation of 70-100 seat RJs, but the scope clauses artificially constrain passenger demand. The past 12 months have seen all the mainline airlines trying to achieve major cost concessions from their pilots in order to avoid Chapter 11 or emerge from it.

Scope clause revisions have been used in the bargaining process with the result that limitations on the number of smaller RJs (less than 51 seats) have been eased or lifted completely. At the same time, most of the major airlines have seen increasing limitations applied on their operation of larger RJs (70 seats and more). American's mainline pilots have regained the operation of RJs with more than 50 seats and America West now a scope clause for the first time.

Delta Connection is limited to 50 seaters, except for 57 'grandfathered' CRJ700s. Only United and US Airways, both of which had to re-organise under Chapter 11, have seen their scope clauses modified to increase their regional carriers' ability to operate 70 seaters.

For airlines that have managed to avoid Chapter 11, further progress to renegotiate scope clauses to allow the widespread operation of 70-100 seat RJs is unlikely to be any less traumatic than it has been for the 50-seat RJ generation. If anything, it is likely to be even more bitter as the mainline pilots see the larger aircraft as even closer to their own turf. Clearly the pilot unions, while in a poor negotiating position, are not going to sacrifice the operation of RJs with more than 70 seats.

The obvious alternative is for the larger RJs to be operated by the mainline carriers, but the only carrier to have chosen this path is American. Embraer is going to have an advantage over Bombardier where larger RJs are going to be operated by the mainline operators, but both will face substantial competition from the A318 and the 717. The mainline carriers with the lowest seating limit in their scope clauses are probably the most likely to entertain the operation of large RJs, since they have the largest capacity gap to bridge. This points to American and Continental, both large Embraer customers, as the best prospects for mainline RJ operation. **AC**