AIRLINE MERGERS IN THE 1970's

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Recently, a number of airlines have sought to increase their share in the market and improve their financial position through mergers. In the following article Mr. John Crooker examines the position that the Civil Aeronautics Board has taken concerning mergers involving both the failing carrier and the healthy, certificate carrier. His analysis includes predictions of future Board responses to similar situations and predictions of other types of mergers that may possibly be proposed.

THE designation of a new CAB Chairman is sometimes followed by speculation as to whether his “philosophy” (concerning routes, rates, subsidy or mergers) will provide new leadership in crystallizing the views of other Board members on those topics. With the designation of Robert Timm as Chairman,1 it is of particular interest at this time to consider the position the Board may take regarding mergers or acquisitions that may be proposed in the years just ahead. Therefore, a review of recent merger and acquisition cases seems timely. Two factors might be kept in mind, however, in looking at these recent decisions: first, it appears that two new members will come to the Board, one to succeed former Chairman Secor Browne1 and the other to succeed Member Robert Murphy;2 secondly, Mr. Timm, prior to becoming Chairman, set

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2 Resignation noted in 9 WEEKLY COMPILATION OF PRESIDENTIAL DOCUMENTS 192 (1973).

3 The President sent to the Senate on March 12, 1973, the name of Judge Lee R. West of Oklahoma to succeed Mr. Murphy. 9 WEEKLY COMPILATION OF PRESIDENTIAL DOCUMENTS 251 (1973).
forth his interpretation of Section 408 in his vigorous and articulate dissent in the *American-Western Merger Case.* Hence, the welding of some “new majority” in the area of proposed future mergers may be likely. Happily, from the standpoint of a person commenting on the Board’s position in recent merger cases, there are no major cases in this area pending, so that any thoughts expressed clearly do not relate to any pending proceeding.

I. THE FAILING CARRIER CASES

During the early part of the 1970’s, the Board handed down decisions in Section 408 cases pertaining to four air carriers that had sustained significant financial losses,—Trans Caribbean, Caribair, Mohawk and Northeast. In each instance except Caribair, the majority followed a course of action to “prevent the demise” of an ailing carrier. A quick look at the *American-Trans Caribbean Merger Case,* decided in December, 1970, is helpful as background to the steps taken in the *Eastern-Caribair* case. The Board (with only Member Murphy dissenting on the question of “tacking” of route authority of the two carriers) unanimously approved the merger, following largely the reasoning of the Examiner in his recommended opinion, concluding that “the merger will prevent

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* CAB Docket No. 22916; CAB Orders Nos. 72-7-91 (June 13, 1972), 72-7-92 (June 13, 1972) (approved by the President, June 26, 1972).

* The proposed Eastern acquisition of Caribair had not, as of the time of initial preparation of this article (late March, 1973) been finally decided. However, on April 11, 1973, a final decision was reached in which the President directed the Board to approve the merger in accordance with the view of the dissenting Board members. See note 87 infra, and text accompanying.


* CAB Docket No. 21828, CAB Order No. 70-12-161 (December 18, 1970) (approved by the President, December 31, 1970).

* Effective August 17, 1972, the title “Examiner” was changed to “Administrative Law Judge.” 37 Fed. Reg. 16,787 (1972). Most of the decisions treated in this article referred to hearings before “Examiners,” and it should be understood that the two titles are used interchangeably.
the demise of Trans Caribbean. A discussion of beneficial results which spring from most mergers followed: *i.e.*, traffic integration; improved use of flight equipment and personnel; cost savings from superior aircraft maintenance and traffic service operations; and the elimination of duplicate terminal and other facilities.\[10\]

In its opinion, the Board fully treated the matter of estimated diversion from other carriers, especially as a result of "tacking." Two policies were reiterated:

(i) A merged carrier's ability to "tack" routes is a "natural, inherent concomitant of the transaction;" and the public should not be denied the benefits therefrom "absent a strong showing that a restriction is needed in order to protect other carriers."

(ii) The Board may stay a merged carrier's authorization to operate any transferred route, pending completion of 401 (g) proceedings instituted to consider whether the authorization should be deleted from the transferred certificate, but that power should be exercised only in "unusual circumstances."

In rejecting the contentions (principally by Pan American but also by Eastern) with respect to probable diversion, the Board pointed out that recent route awards to Trans Caribbean had been made not solely with the view of carrier strengthening but also because the incumbent carriers in the Caribbean area had not aggressively exploited their certificate rights.

In this case, the Board passed on one collateral issue on its own initiative, making its approval subject to one rather interesting "non-route" condition—the elimination of agreements requiring American to employ Mr. Roy Chalk (Trans Caribbean's largest shareholder) and seven other Trans Caribbean officers. Mr. Chalk's agreement provided that he be paid an annual salary of $40,000 for eighty days of work per year for seven years; and if American requested that he render additional consulting services, he would receive an additional $500 per day. The evidence reflected that American had never before entered into similar employment contracts at comparable salaries for "consulting services;"\[18\] and it was

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\[10\] See CAB Order No. 70-12-161, *supra* note 8, at 2.

\[11\] *Id.* at 2, 3.

\[18\] *Id.* at 10.
apparently undisputed that no specific task or position had been earmarked for any of the Trans Caribbean officers. The Board observed that employment contracts may provide a means for majority shareholders to enjoy a special financial advantage to the detriment of minority shareholders. As the applicants failed to establish that the employment contracts were necessary or advantageous to the surviving carrier, it was concluded that the public interest required that the contracts not be tied to the merger agreement. American was not prohibited from engaging the services of Mr. Chalk or any of the others; the decision simply left American free to negotiate any such employment, outside the ambit of the merger agreement.

About three weeks before the Board’s decision in American-Trans Caribbean, the Board approved the Interim Management Arrangement applied for jointly by Eastern and Caribair in connection with their proposed merger. Within the first half of calendar 1971, the Examiner’s recommended decision, favoring the acquisition of Caribair by Eastern, was handed down; and oral argument was held before the Board. Thereafter, although Eastern pumped financial support into Caribair, matters did not move quickly. More than a year passed; and the continuing losses of Pan American had become a matter of great concern. The plight of Caribair was probably worse in mid-1972 than had been true of Trans Caribbean in late 1970, even though Eastern’s financial assistance to it had been some five times as great as the amount originally committed. But the Board majority, in its August 3, 1972, opinion sent to the White House cited two basic reasons for coming to a conclusion (contrary to that reached by the Examiner) that (i) approval would overturn nearly 30 years of “historical

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10 CAB Order No. 70-11-142 (November 27, 1970). The agreement was subsequently extended for three months by CAB Order No. 71-6-145 (June 29, 1971), thereafter from month to month by a series of orders, e.g., CAB Order No. 71-12-5 (December 1, 1971); CAB Order No. 72-3-115 (March 31, 1972).

14 Caribbean-Atlantic Airlines, Inc.-Eastern Air Lines, Inc. Acquisition Case, CAB Docket No. 22690, CAB Order No. 73-4-80 (April 11, 1973) (dissenting opinion of August 3, 1972 at 18). Eastern’s original commitment had been for $1,000,000. While the exact amount actually advanced to Caribair by its creditors is uncertain, it was said by Vice Chairman Gilliland and Member Minetti in their dissent that Caribair’s creditors “would be some millions of dollars better off if the Eastern acquisition agreement were approved. . . .” The Board majority did not disagree on this point.

15 Id. (opinion of August 3, 1972, was not signed by the President).
development in the Caribbean that has lead to the present U.S.-
Caribbean route structure;"18 and (ii) Eastern's acquisition of
Caribair "would divert substantial revenues from Pan American,
a particularly unfortunate circumstance in view of the disturbingly
high losses that Pan American has been suffering."17

In a thorough dissent, Vice Chairman Gillilland and Member
Minetti effectively answered the first point. They pointed out that
such a result would terminate "all U.S.-flag certificated service in
numerous intra-Caribbean markets—markets in which certificated
services [had] heretofore been found required by the public con-
venience and necessity." The dissenters also believed that the
adverse consequences to Pan American would not be severe, point-
ing out:

(i) If Eastern acquired Caribair's route and operated the service
as it then proposed to do, Pan American's 1972 traffic in
those markets would be greater than its actual 1969 traffic;
(ii) The bulk of the diversion feared by Pan American could
be averted by imposing suitable conditions on the transfer of
Caribair's route authority, without materially impairing East-
ern's plans for utilizing that authority;18 and
(iii) Some bit of "diversion" from Pan American existed because
of other decisions (e.g. the American-Trans Caribbean
matter) and not solely from approval of the proposed
Eastern-Caribair agreement.

The real crux of the difference of viewpoint between the ma-
majority view and the minority view related to the effect of the
anticipated traffic diversion on Pan American. In several cases
coming to the Board during the preceding few years, (e.g., the
merger of three local service carriers to form Air West,19 and the
Hughes acquisition of Air West20) much had been said about the
"failing business doctrine." Except in the Caribair situation, the
only entities deemed to be in dire financial straits were carriers

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18 Id. at 2 (opinion of August 3, 1972).
17 Id. at 3 (opinion of August 3, 1972).
19 Id. at 1 (dissenting opinion of August 3, 1972).
20 Id. at 3 (dissenting opinion of August 3, 1972).
19 Bonanza-Pacific-West Coast Merger Case, CAB Docket No. 18996, CAB
Order No. E-26625 (approved April 9, 1968).
20 Acquisition of Air West by Hughes Tool Co., CAB Docket No. 20665,
CAB Orders Nos. 69-7-102 (July 15, 1969), 69-7-103 (July 15, 1969) (approved
by the President).
proposed to be merged or acquired; but here there is a genuine concern for the ability of a third party carrier (and a very large one, at that) to survive, should the proposed acquisition be approved.

The Board majority in *Eastern-Caribair* found that: “For the three years ended December 31, 1971, Pan American suffered a system-wide loss of about $120,000,000,” and that for 1969 and 1970, “most of the loss” had occurred in the Caribbean. Further, it was deemed that “the net result could easily be a serious competitive disadvantage for Pan American that it could ill afford at this stage in its history;” and that “in all likelihood the disadvantage would be permanent and ever-increasing as the mainland interior traffic available to Eastern built up. . . .”

In the dissenting opinion, four pages were devoted to the affirmative public benefits of approval of the proposed agreement—factors such as those cited in the American-Trans Caribbean case. But both at the Board and at the White House, the focal question continued to be whether utilization of Caribair's route authority by Eastern would deal a staggering blow to Pan American.

The President returned the Board's August 3, 1972, opinion unsigned. In his letter, the President aptly summarized the two important foreign policy considerations involved in the case: that U.S.-flag carriers remain in a healthy financial condition; and that U.S.-flag certificated service to non-U.S. points in the Caribbean be maintained. He stated that he returned the opinion unsigned because it did not consider (as an alternative) “detailed restrictions to mitigate the diversionary impact on Pan American revenues if the acquisition were approved.” He urged the Board “to make the necessary studies to investigate such restrictions and to consider whether such restrictions could satisfy both the Board's objectives and the President's foreign policy concerns.”

By CAB Order 72-10-96, statements of views and replies thereto on the issues raised by the President's letter were invited and a

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22 Caribbean-Atlantic Airlines, Inc.-Eastern Airlines, Inc. Acquisition Case, CAB Docket No. 22690, CAB Order No. 73-4-80, at 12 (August 3, 1972) (not approved by the President).
23 *Id.* at 16.
24 *Id.* at 19-22 (dissenting opinion of August 3, 1972).
25 The President's disapproval of the Board's decision was announced in CAB Order 72-10-96 (October 30, 1972).
time frame was fixed for receipt of the same during the month of November 1972. Subsequently, there has been considerable speculation in the trade press that another decision has been reached and has been sent to the White House. Apparently, while Eastern terminated its financial support to Caribair, its management services continued; and necessary funds have been supplied (apparently largely from the Commonwealth of Puerto Rico) to prevent the death of Caribair.

As noted, the President’s action in Caribair (which in effect remanded the case to the Board) succinctly set forth the view that in such matters, a major part of the “diversionary impact” on a third carrier may be averted if the Board considers “detailed restrictions” on utilization of some of the route authority of the to-be-absorbed carrier. Favorable resolution of a merger application by imposing such restrictions was receiving attention at the Board at substantially the same time, in the Northwest-Northeast case.27

A merger agreement between Northeast and Northwest had been submitted for approval, approval was granted subject to one condition of great importance to Northwest—denying to the surviving carrier (Northwest) the Miami-Los Angeles authority granted to Northeast in the Southern Tier case.28 Northwest was unwilling to live with the proposed merger without gaining Miami-Los Angeles authority as part of the package, and Northeast sought another marriage. The position of Delta was somewhat different, since it had been utilizing Florida-California authority since the Southern Transcontinental case,29 decided more than a decade earlier. While it actively sought the Miami-Los Angeles route, Delta agreed to proceed with the merger should the Board stay the authority granted to Northeast in Southern Tier.30

The “failing business doctrine” (this time applied to Northeast) was in the forefront of the Board’s thoughts. On the second page of

29 Southern Tier Competitive Nonstop Investigation, CAB Docket No. 18257, CAB Order No. 69-7-135 (July 24, 1969).
31 See note 28 supra.
the opinion, the Board pointed out that the "proceeding represents the second time in a little more than a year in which the Board has been asked to consider a merger of Northeast Airlines with another air carrier." Comment was made at the time of the Northwest-Northeast proceeding that "while Northeast was not in extremis, and could reduce its losses through retrenchment, its financial condition was precarious, and its prospects for the future were bleak." The Board then set forth a series of financial statistics which unquestionably spelled bankruptcy for Northeast, if approval to merge was not forthcoming. The 1970 Northeast loss had been nearly eleven million dollars (despite windfall traffic picked up as a result of a strike of a competitor) and the 1971 loss appeared to be $13,922,000. The negative shareholder equity (excess of debts over assets) by the end of 1971 was approaching the $47 million mark. Revenues were falling far short of meeting operating expenses less depreciation and amortization. While Storer Broadcasting Company had, to that time, provided most of the needed cash, its Board of Directors had determined to end the financial assistance to Northeast (and thus to "get back to running" a broadcasting business, with which it was felt their corporate officers had reasonable familiarity and competence).

While the Board considered route strengthening as a solution to the carrier's dilemma, it was concluded that "Northeast simply does not have the financial wherewithal to mount the effective operation necessary to penetrate a new market and capture enough traffic to make such an enterprise profitable." And finally, viewing potential diversion in terms of growth offset, the Board agreed with the projection by the Bureau of Operating Rights that there would be "no diversion whatsoever." Objections had come from Eastern and National, to the effect that such merger would prevent them from obtaining the 12 percent rate of return goal established in Phase 8 of the Domestic Passenger Fare Investigation. The Board brushed aside this contention on both the facts and the proper interpretation of the Phase 8 decision—stating that the

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32 Id. at 2.
33 Id. at 7.
34 Id. at 19.
35 Id. See also CAB Order No. 71-4-58 (April 9, 1971).
record before it did not support the contention that over the long run, Eastern or National would be thus prevented from attaining that “rate of profit,” and also pointing out that the 12 percent figure is intended as an industry average over a period of years, and guarantees nothing to any particular carrier or industry-wide as to any particular year.\textsuperscript{38}

The Delta-Northeast merger was therefore approved. Procedurally, the authorization of Delta to operate segment 7 of Northeast's certificate for route 27\textsuperscript{7} was stayed “pending final decision in a proceeding instituted for the purpose of reexamination of such authorization.” The proceeding was to be instituted upon transfer of the certificate. It will be recalled that in the American-Trans Caribbean\textsuperscript{8} case, the Board had found that the recent grant of authority to Trans Caribbean had not been solely for the purpose of carrier strengthening; but in the Southern Tier case, it was indisputable that there could have been no justifiable reason for the award to Northeast except carrier strengthening. In the Delta-Northeast opinion, the Board expressed some displeasure at the actions of Northeast's officers in connection with the matter. It stated that “the [Miami-Los Angeles] award was based in part on Northeast's assurances to the Board that its management contemplated that the carrier would remain an independent entity. As it turned out, immediately after the award of the route, the carrier began its quest to merge with another carrier. The sole basis for the award was thus frustrated.”\textsuperscript{39}

On a final point with respect to this route, Delta urged that it should be allowed to operate the route pending the outcome of the 401(g) proceeding; the Department of Transportation supported the request. After careful review of the pros and cons, the Board concluded that “on balance” the reasons for ordering the 401(g) proceeding also required the Board to deny the request for pendente lite authority.\textsuperscript{40}

On one other point collateral to the main question of merger vel non, considerable concern was expressed about the intentions

\begin{itemize}
\item \textsuperscript{38} See note 31 supra at 20.
\item \textsuperscript{37} While this segment has been referred to as Miami-Los Angeles, technically it is Miami/Ft. Lauderdale, Florida—Los Angeles/Ontario/Long Beach, California.
\item \textsuperscript{38} See note 8 supra.
\item \textsuperscript{39} See note 31 supra.
\item \textsuperscript{40} Id. at 29-30.
\end{itemize}
of the surviving carrier to provide the type and extent of service which the Board had originally envisioned Northeast would provide to the New England area. Member Murphy dissented, principally because Delta had, some six weeks before the Board's decision, filed a "service proposal" proposing to delete from its post-merger certificate some two-thirds of the New England area cities certificated to Northeast. He favored reopening the record in the merger case to take evidence upon the service proposal.4 In arguing for remanding "the case to the Examiner to take evidence on Delta's proposal and to fully re-examine those proposals of other carriers, such as Eastern, who have indicated that they stand ready to serve this important area of the nation," Member Murphy commented that the Board "has had a long history of trying to compel unwilling carriers to serve markets that they do not wish to serve, and time and again has seen this unwillingness translated into marginal service grudgingly rendered." Member Minetti commented that he did "not regard it as essential or desirable to reopen the evidentiary record and remand the case to the Examiner," pointing out that such course "would defer final decision for many months or even years," but that he "would reopen oral argument (which could be done immediately) in order to permit the Board to question Delta's representative further concerning the carrier's intentions as to Northern New England service."5

By coincidence, within a week after the filing of Delta's "service proposal" affecting New England, the Board handed down its decision in another merger case—this one affecting two contiguous local service carriers whose route systems lay in the north-easterly quarter of the continental United States. All five of the Board members agreed that the merger of Allegheny and Mohawk should be approved.6 The reasons for the result were not complex: (i) the two carriers had 18 stations in common; (ii) the merger

42 See note 31 supra at 1 (dissenting opinion).
43 Id. at 3.
44 Id.
45 Id. at 1 (statement of Minetti).
46 CAB Orders Nos. 72-4-31 (1972), 72-4-32 (1972).
47 Id.

would result in discontinuance of competitive service in only two markets; (iii) no air carrier intervenor opposed approval; (iv) no air carrier intervenor submitted an estimate of diversion or contended that it would be jeopardized by approval of the merger; and (v) the Board affirmatively found no factual evidence of diversion from any other air carrier. Members Minetti and Murphy concurred in the principal result, but advocated changes in the labor protective provisions. Since these provisions constituted the only point of disagreement among the members in this case, a look at the suggestions made by the dissenters is warranted. Specifically, they advocated the institution of a new proceeding, in the nature of rulemaking, to consider for the future what if any substantive changes should be made in the labor protective provisions. In this writer's opinion, Members Minetti and Murphy had a valid point in observing that proposals for changes in labor protective provisions always come before the Board for consideration "as a peripheral issue in individual merger and route transfer cases, and tend to be overshadowed by the major issues of whether the merger or transfer shall be approved as being in the public interest." In the United-Capital case, careful consideration was given to the labor protective provisions; and for some years, the Board has more or less adopted these provisions by reference, unless some specific need existed to modify the conditions in a particular case. If a majority of the members of the Board, as it will exist in the latter part of 1973, should determine that substantial changes should now be made in the rather "standardized" labor protective provisions set out in United-Capital, then a proceeding might be instituted as proposed by Messrs. Minetti and Murphy. At all events, the Board should determine what labor protective provisions might now be considered as the "standardized" ones, so that ad hoc decisions on the labor points would not confront the Board in cases that are often laden with more pressing issues and when consideration is (as argued by the two dissenting members in the Allegheny-Mohawk case) "surrounded by an aura of urgency and haste." After all, certain phases of the Domestic Passenger-Fare

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48 Erie-Detroit and Islip-Bridgeport.
49 See note 46 supra at 5 (concurring opinion).
Investigation were approached in substantially the same procedural way.\(^{1}\)

Are there conclusions which may be easily summarized from the four “sick carrier” 408 cases of the early 1970's? Subject to broad generalities that neglect to pinpoint conditions, variations and exceptions, it appears that in future matters of this sort, the Board’s determinations will emphasize:

(i) That merger (even with modified service proposals) furnishes more protection to the public against loss of certificated services previously found to be needed, than does dismemberment of a carrier;

(ii) Careful examination of proposals for curtailed service after approval of a merger;

(iii) Assistance in the salvage of creditor (or even shareholder) interests; and preventing wholesale discharge of a company's employees;

(iv) Appraisal of affirmative benefits from traffic integration, elimination of duplicate services and facilities, etc.;

(v) Cancellation of “sweetheart contracts” with highly-paid executives for future “services” in merger agreements;

(vi) Possible standardization of the labor protective provisions;

(vii) Application of a “growth offset” rather than a “percent of market” yardstick to the potential diversion question;

(viii) Treatment of a merged carrier's ability to “tack” as natural and inherent, but remaining ready to review in a 401(g) proceeding the question of deleting specific authorization from the transferred certificate;

(ix) Determination on an ad hoc basis whether to permit pendente lite utilization of authority being considered in such a 401(g) proceeding; but probably “on balance” staying most of such questioned authority until a final determination.

In addition to the specifics set forth above, it is submitted that the Board will continue to be acutely aware of the fact that a decline in investor confidence in airline securities would attend the “de-

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\(^{1}\) See note 33 supra. The Phases of the Domestic Passenger Fare Investigation which were handled by rulemaking are as follows:


mise” of any certificated scheduled air carrier. Lest one conclude that this final factor pre-determines every merger case involving a debilitated scheduled carrier, it must be remembered that a careful review of the economics applicable to third party carriers must also be considered—and the larger and more prestigious the carrier in financial straits, the more the concern over its vitality will exist.

II. MERGER OF HEALTHY CARRIERS

The four cases discussed above were all considered in the light of the “failing business doctrine.” What about a proposed merger of two healthy carriers? American Airlines and Western Airlines presented such a situation. Scant attention was given in the four cases to the fact that the wording of Section 408 of the Act is cast differently than the wording of Section 401. But in the American-Western Merger Case, the Board majority felt constrained to discuss the “burden of proof” differences in the wording of Sections 401 and 408; and a principal thrust of the dissent by Chairman Timm involved this distinction.

The Examiner had recommended disapproval of the merger (and the attendant proposed transfer of Western’s certificates to American, as the surviving carrier) as inconsistent with the public interest upon findings that the merger would disrupt the size and balance relationship that must be maintained as between the large trunk carriers; that the merger would not result in any material public benefits or meet any serious transportation need; and that the merger would seriously disrupt the structure of the air transportation system, especially in the mainland-Hawaii markets.

The impact on other carriers in the mainland-Hawaii markets was a prominent factor in the decision in American-Western, just as the impact on Pan American was considered by the Board in Eastern-Caribair. Pages 4 through 16 of the Board’s decision were devoted almost in their entirety to arithmetic. The Board found that the mainland-Hawaii operations would account for about 52 percent of the total added revenues attributed to the merger;

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22 CAB Docket No. 22916, CAB Orders Nos. 72-7-91 (June 13, 1972), 72-7-92 (June 13, 1972) (approved by the President, July 26, 1972).

23 At the time of the decisions here referred to, Mr. Timm was a Member of the Board, but in view of his subsequent designation as Chairman, he is referred to in this article as Chairman Timm.
and that $65 million annually of diversion from other carriers would occur in those markets.\textsuperscript{54}

The Board took note of the fact that before 1969, only three U. S. carriers had mainland-Hawaii authority, and two of them (United and Pan American) carried nearly 95 percent of the traffic. Before 1969, the last major change in Transpacific authority (granting West Coast-Hawaii route authority to United) had occurred some two decades earlier,—a decade before the advent of the jet airliner. So in \textit{Transpac}, the Board had provided Western and Continental with significant mainland-Hawaii authority and had granted Braniff authority from five Southern cities, overflying the West Coast. These three carriers (and Northeast) were the trunk carriers not then having transcontinental authority. Further in \textit{Transpac}, both TWA and American had been awarded Hawaii authority with significant long-haul restrictions.

In its opinion in the \textit{American-Western} case, the Board noted:

\begin{quote}
[T]he possibility of disruption in mainland-Hawaii operations becomes particularly serious to us when we review the balance of carrier competition in these markets which the Board specifically patterned only three years ago in the \textit{Transpacific Route Investigation}. Because of the Board's action, these markets differ from other markets where the competitive relationships have arisen on a piecemeal basis, or where traffic growth is so great as to transcend the pattern established by previous Board route awards. In such other markets the alteration of the system by a merger might, therefore, be only one of many factors bearing on the resulting competitive route structure.\textsuperscript{55}

Again alluding to the delicate nature of the competitive balance sought to be established in \textit{Transpac}, it was said: "The resultant structure provided competitive Hawaiian service from all but one of the twenty-four mainland coterminals involved."\textsuperscript{56} Further it was said:

In implementing this balance the Board selected carriers and imposed restrictions, in a manner intended to provide a reasonable opportunity for profitable operations after an initial development period, to encourage nonstop operations from interior mainland points, and to strengthen weak carriers whose route systems re-

\textsuperscript{54} See note 52 \textit{supra} at 4-5 (majority opinion).
\textsuperscript{55} \textit{Id.} at 5.
\textsuperscript{56} New Orleans.
quired strengthening. Subsequent Presidential directives in the international phase of the case required deletion of an international Central Pacific route for American, and substitution of American for Continental in the international South Pacific route via Hawaii. The Board thereupon, in the domestic phase of the case, made corresponding alterations in its domestic route awards in order to maintain the competitive balance.57

The Board seriously considered whether the imposition of restrictions or nontransfer conditions could resolve the mainland-Hawaii market problem. As stated in the opinion: "In the first place, American has taken the position that it would not proceed with the merger in the event of the imposition of conditions or restrictions on transfer of California-Hawaii authority."58 The Board, having fresh in its mind the fulfillment of a similar statement of position by Northwest in its proposed merger with Northeast, was doubtless persuaded that American meant business. But the Board pursued the matter another step, and concluded that even if American would accept such a condition, there was no acceptable alternative to disapproval. American proposed a capacity limitation as had been approved in Order 71-8-91.59 The Board pointed out, however, that "such agreements have not generally been sanctioned under the Federal Aviation Act because of their anti-competitive nature."60 The August 1971 approval of one year capacity limitation agreements in four markets had been "a temporary expedient to resolve a financially ruinous but short-term problem of over-capacity."61 So the Board concluded that "[a] permanent problem cannot be solved permanently by a temporary expedient."62 Finally, in considering possible alternatives, the Board explored the possibility that the merged carrier's Hawaii operations might be re-

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57 See note 52 supra at 6.
58 CAB Order No. 72-7-91, at 21 (June 13, 1972).
59 In the Matter of the Application by Trans World Airlines, Inc. For Approval of Capacity Agreement, CAB Order No. 71-8-91 (August 19, 1971). The four East Coast-West Coast markets in which approval was given to engage in discussions as to limiting capacities were:
  New York/Newark—Los Angeles,
  New York/Newark—San Francisco,
  Chicago—San Francisco, and
  Washington/Baltimore—Los Angeles.
60 CAB Order No. 72-7-91, at 21 (June 13, 1972).
61 See note 52 supra at 21.
62 Id. at 21.
stricted to those which could have been performed separately by the two carriers under their existing route authority; but the Board rejected this solution because such a restriction would “create a series of cumbersome limitations within the merged carrier's route system, which is generally undesirable” and because such a restriction would not avoid giving to the merged carrier “a disruptive competitive advantage.”

In Chairman Timm's dissent, he expressed the view that “the majority rested its decision almost entirely on the competitive disruption an unconditional approval would cause in the mainland-Hawaii markets.” He then listed some of the identifiable benefits from most proposed mergers: e.g., the two systems would integrate well (which fact was not disputed); industry balance has nothing to do with size; efficiencies would be obtained in “aircraft utilization, reduction of personnel and staff, duplicate facility rentals, computer investment, advertising, reduced spares inventory, insurance savings and flight training savings.”

While the economic differences of viewpoint between Chairman Timm and the other members participating in the case are important, their significant difference in legal philosophy related to the proper interpretation to be given to the wording of Section 408(b). This statute requires any person seeking approval of a consolidation, merger, etc., to present an application to the Board, and that notice shall be given of the time and place of a public hearing. It then provides:

Unless, after such hearing, the Board finds that the consolidation, merger . . . will not be consistent with the public interest or that the conditions of this section will not be fulfilled, it shall by order approve such consolidation, merger . . . Provided that the Board shall not approve any consolidation, merger . . . which would result in creating a monopoly or monopolies and thereby restrain competition or jeopardize another air carrier not a party to the consolidation, merger . . .

Neither the majority in the American-Western case nor Chairman Timm felt that the decision turned on the question of whether

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63 Id. at 22.
64 Id. at 13 (dissenting opinion).
65 Id. at 16 (dissenting opinion).
66a Id. (emphasis added).
the merger "would result in creating a monopoly that would thereby restrain competition or jeopardize another air carrier, within the intent of Section 408(b). So the difference centered on the question of whether the Board must, by order, approve the merger unless there is a finding that such merger would be inconsistent with the public interest. In Chairman Timm's dissent, he noted that the phrase "consistent with the public interest" has raised a controversy over what happens when there is a proposed merger with no outstanding public benefits and no outstanding public detriments, i.e., an exactly even balance between pros and cons." A clear distinction was noted between the wording of Section 408(b) and Section 401(d). There is plainly an affirmative burden of proof to be borne by an applicant in order to obtain a certificate; but Chairman Timm persuasively asserts that in that hypothetical case in which the scales are tipped neither way, normal rules of statutory construction would compel the conclusion that:

Congress intended the Board to approve mergers between air carriers so long as the result would not be adverse to the public interest. A merger of two air carriers which did not promote the public interest would have to be approved by the Board under the Act unless the Board specifically found that the merger would be adverse to the public interest."

The proposed American-Western merger is a thing of the past. But in the realm of speculation as to future decisions in 408(b) cases, strict construction of the subsection may emerge, and the Board may conclude that its statutory charge is no more and no less than what the plain statutory language would imply as to what may be termed "burden of proof."

One additional point in Chairman Timm's dissent in American-Western is noteworthy. He enunciated a policy with which no other member disagreed that:

...bankruptcy is not a statutory condition precedent to merger. There is no prohibition in the Act against two healthy carriers merging. Economically sound carriers need not grow old, run down, and die before a Board-approved merger can be triggered. Carriers are statutorily entitled to the benefits of strengthening through

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67 See note 52 supra at 1 (dissenting opinion).
69 See note 52 supra at 2 (dissenting opinion).
merger while they are healthy. If Congress had not intended this to be the case, it would have so provided. ¹⁰

III. POSSIBLE FUTURE MERGERS NOT OF THE CONVENTIONAL TYPE

The five cases discussed above involved certificated scheduled carriers. The Allegheny-Mohawk case involved two subsidized carriers and each of the other cases involved two carriers not then receiving subsidy. There may be other fact situations that will reach the Board. Several such possibilities in alternative situations, which widely differ with each other, are now discussed very briefly.

(A) A proposal may be made involving one subsidized (local service) carrier and one non-subsidized (trunk) carrier. A trunk carrier (assuming that it would be the surviving entity) would probably find that the matter of Section 406” payments would be considered separately, after approval of a merger, just as was done in the Hughes-Air West proceeding. ²⁷ Realistically, no future subsidy payments could be expected. But several of the local service carriers now seem to be averting heavy losses, even in the absence of subsidy; ²⁸ and if a trunk carrier should want the certificate authority of one of the locals to mesh into its system, the loss of Section 406 payments currently being received by the smaller carrier would probably not offset the advantages the larger carrier would expect to realize. Surely, the acquirers of Trans Caribbean, Caribair and Northeast were faced with possible losses of much greater size than the 406 payments being made to many of the local service carriers.

(B) It is also possible that one of the certificated carriers would seek a merger with a carrier operating under some intra-state certificate issued by a State regulatory agency and not certificated by the CAB. It will be recalled that some four years ago, it appeared that Pacific Southwest Airlines might seek Board certification in

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¹⁰ Id. at 2-3.


²⁸ See note 21 supra.

²⁹ 1972 CAB ANNUAL REPORT 104. In “before subsidy” figures, Piedmont and Ozark showed an operating profit for FY 1972 and North Central showed a relatively small loss. Allegheny showed a profit of more than $7.4 million before the merger with Mohawk; and until a year’s statistics are available after the merger, it is not clear whether it will continue to show a “before subsidy” operating profit. Hence, of the remaining local service carriers, only Frontier, Hughes, Southern and Texas International showed heavy “before subsidy” losses.
order to commence operations into States other than California.

(C) Situations might arise similar to the TWA-Hilton situation, not necessarily as a merger, but in the realm of interlocking relationships or acquisitions of control. Particularly in connection with resort travel, potential airline passengers are desirous of having assurances that they will be well cared for at their destinations, and it is conceivable that other air carriers would seek to have some financial ties with companies in the public accommodations business. It is realized that (in an industry other than the airline industry) Boise Cascade has been less than pleased with its ventures into the resort business. Originally it had been thought that travel to choice resort areas would stimulate house building, which, in turn, would furnish a logical market for lumber. Despite the Boise Cascade experience, some air carrier’s affiliation with a hotel or resort chain is still a distinct possibility during the rest of the 1970’s.

(D) On another front, legislation was proposed in the Ninety-Second Congress which would have authorized the Board to permit an air carrier to hold both scheduled and supplemental certification. The bill, if passed, doubtless would have triggered some preliminary negotiations as to mergers between one or more of the scheduled carriers and one or more of the supplementals. That proposal did not move forward in the Ninety-Second Congress, but its sponsors indicate that the idea has not been abandoned. Probably the most compelling reason for careful scrutiny of such a proposal is that some foreign companies supposedly not affiliated with each other, but actually under the same control, offer both scheduled and charter services. The “get established” period for

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<table>
<thead>
<tr>
<th>FOREIGN SCHEDULED CARRIER</th>
<th>SUBSIDIARY</th>
<th>% OWNED BY SCHEDULED CARRIER</th>
</tr>
</thead>
<tbody>
<tr>
<td>Air France</td>
<td>Air Charter International</td>
<td>100%</td>
</tr>
<tr>
<td>Alitalia</td>
<td>Societa Aerea Mediterranea</td>
<td>100%</td>
</tr>
<tr>
<td>Austrian Airlines</td>
<td>Austrian Airtransport</td>
<td>40%</td>
</tr>
<tr>
<td>BEA</td>
<td>BEA Airtours Ltd.</td>
<td>100%</td>
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</tbody>
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5 S. 2548, 92d Cong., 1st Sess. (1971). As neither this bill nor S. 2549, 92d Cong., 1st Sess. (1971), had, at the time of preparation of this article, been introduced in the Ninety-Third Congress, the references are to such bills introduced by Senator Inouye, by request, on September 20, 1971.

55 Attached to statement presented on May 10, 1972, by Mr. Jerrold Scoutt, Jr., Counsel for, and Director of, World Airways, Inc., to the Aviation Subcommittee of the Senate Commerce Committee, was an Appendix listing “Charter Subsidiaries of Foreign Scheduled Carriers” as follows:
the supplementals should be deemed to be at an end. The service rendered by them to the public in focusing attention on what could be done in the way of lower fares when charter flights were well patronized is evident when the extensive bulk transportation business now undertaken by the scheduled carriers under their existing authority is examined.

If the Act were amended as proposed by S. 2548 the effect would be to delete the portion of paragraph (3) of Section 401(d)\(^\text{76}\) that states:

\[
(3) \text{In the case of an application for a certificate to engage in supplemental air transportation, the Board may issue a certificate, to any applicant not holding a certificate under paragraph (1) or (2) of this subsection . . . .}
\]

Under the proposed wording, the words "to any applicant not holding a certificate under paragraph (1) or (2) of this subsection" would be deleted. The proponents of this suggested change carefully point out that adoption of such a bill would not result in Congressional approval of relationships between scheduled and supplemental air carriers, but it would merely permit the possibility of such relationships, and leave the final determination to the CAB.

(E) One other bill was introduced by Senator Inouye in September 1971. This was S. 2549 which would have amended Section 408(b) of the Act. Comments on some of the provisions

<table>
<thead>
<tr>
<th>Airline Name</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Finnair</td>
<td>Kar-Air</td>
</tr>
<tr>
<td>Iberia</td>
<td>Aviaco</td>
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<tr>
<td>Yugoslav Air Transport</td>
<td>Air Jugoslavia</td>
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<tr>
<td>KLM</td>
<td>Martins Air Charter</td>
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<td>Lufthansa</td>
<td>Condor</td>
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<td>Sabena</td>
<td>Sobelair</td>
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<td>SAS</td>
<td>Scanair</td>
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<tr>
<td>Swissair</td>
<td>Balair</td>
</tr>
<tr>
<td>UTA</td>
<td>Compagnie Aeroinaritime d'Affretement</td>
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<tr>
<td>Air Trans Africa</td>
<td>Afro-Continental Airways</td>
</tr>
<tr>
<td>Balkan Bulgarian Transport</td>
<td>Bulair</td>
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<td>Luxair</td>
<td></td>
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<tr>
<td>Out Island Airways Ltd.</td>
<td>Island Flying Services</td>
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</tbody>
</table>

\(^{76}\)See note 68, supra.
of that subsection were made above, in connection with the discussion of the American-Western case. Currently, there is a "provided further" sentence in 408(b) reading:

Providing further, That if the applicant is a carrier other than an air carrier, or a person controlled by a carrier other than an air carrier or affiliated therewith within the meaning of section 5(8) of (the Interstate Commerce Act, as amended), such applicant shall for the purposes of this section be considered an air carrier and the Board shall not enter such an order of approval unless it finds that the transaction proposed will promote the public interest by enabling such carrier other than an air carrier to use aircraft to public advantage in its operation and will not restrain competition:

The purpose of S. 2549 was to delete from 408(b) the portion just quoted. It is interesting to note that some of the parties (from the ranks of the supplemental carriers) supporting S. 2548 also gave evidence in support of this bill." It is believed, however, that the proposal contained in S. 2549 has somewhat broader support at this time—including some support at the Board. The decision in the Long Haul Motor Carrier Control of Air Freight Forwarders Case\(^7\) was an opening wedge into the area of intermodal cooperation. Subsequently, the Joint DOT/NASA Civil Aviation Research and Policy Development Study stated (in regard to cargo) that:

The government should examine carefully its regulatory role in several areas to be certain that regulatory policies are not inhibiting innovation by industry. One example of such a problem is the current policy opposing multimodal mergers including air carriers. This policy was originally established to protect civil aviation from the then financially stronger ground modes, but today it represents a barrier to realizing the full potential of air cargo and impedes the incentive that R & D needed to improve intermodal cargo shipment.\(^9\)

Advocates of the S. 2549 proposal are rather modest in their statements as to how the Board would act on applications for:

\(^7\) Statement presented by World Airways, Inc., to the Aviation Subcommittee of the Senate Commerce Committee on May 10, 1972.

\(^8\) Long Haul Motor Carrier Control of Air Freight Forwarders Case, CAB Order No. 69-4100 (1969).

intermodal acquisitions. They foresee that the Board might proceed as it did in the *Freight Forwarder* case, permitting monitored entry into the field and retaining jurisdiction to keep a close tab on intermodal companies.

Relaxation of the existing virtual prohibition against common ownership of surface and air carriers would merely recognize the relative economic parity between these arms of the transportation industry today. In 1940, operating revenues for the air carriers amounted to less than 2½% of operating revenues for the railroads. In the very near future, the operating revenues should be about equal, because air carrier revenues have increased some 10,000 percent while railroad revenues have increased about 150 percent.

**IV. Conclusion**

In an industry in which growth and progress come swiftly, a "current" status report or analysis may become partially out-of-date before it is printed and read. To a certain extent, the same thing may be said with respect to an article pertaining to the regulatory agency having jurisdiction over such an industry. During the 1960’s, two excellent articles relating to CAB policies appeared in the *Journal of Air Law and Commerce.* In the earlier of the two articles, annual operating revenues of the trunk airlines were cited. For 1961, such revenues amounted to about $2 billion. By 1972, total operating revenues of the trunk airlines (excluding Pan American) had grown to more than $8,475,000,000. The

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86 See note 78, *supra.*
88 CAB QUARTERLY INTERIM FINANCIAL REPORT (PRELIMINARY) (Dec. 1972), prepared by the Bureau of Accounts and Statistics, Civil Aeronautics Board, shows the calendar year 1972 total system operating revenues of the certificated carriers to be:

<table>
<thead>
<tr>
<th>Category</th>
<th>Amount</th>
</tr>
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<tbody>
<tr>
<td>Trunk and Pan American</td>
<td>$9,781.1 million</td>
</tr>
<tr>
<td>All cargo</td>
<td>291.3 million</td>
</tr>
<tr>
<td>Local service carriers</td>
<td>934.9 million</td>
</tr>
<tr>
<td>Total</td>
<td>$11,007.3 million</td>
</tr>
</tbody>
</table>

subsidy article, published in 1968, preceded by a year or so, a reversal of the subsidy reduction trend of the late 1960's.

In connection with this article, three events have occurred subsequent to its preparation, which deserve further comment, so that the work will not be out-of-date from the inception. These three matters are discussed as something of a postscript.

On April 11, 1973, the President disapproved the Board's decision in the Eastern-Caribair case, and accepted the recommendations of the Board's minority decision. The President directed the Board to approve the acquisition subject to the restrictions on the merged carrier's operating authority, as stated in the minority opinion (with one exception). Therefore, of the four "sick carrier" merger and acquisition cases of the early 1970's, the only one in which the Board's majority did not approve the merger was overturned by the President for foreign policy reasons—and (subject to some restrictions on operating authority) merger was approved in all cases.

Secondly, Vice Chairman Gillilland delivered an address in Long Beach, California, on April 17, 1973, supporting the concepts embodied in S. 2548 and S. 2549, discussed above, stating:

Two statutory modifications would be helpful. One statute now in effect prohibits the merger of companies engaged in different modes of transportation. Another prohibits the merger of supplemental air carriers with scheduled air carriers. Each statute was intended to serve a worthy purpose and perhaps initially did so. The first may have saved an infant air transportation industry from strangling by the railroads. The second may have prevented a similar fate to air charter transportation from a different predator. Neither danger continues to exist. Neither restriction continues to serve a useful purpose. On the contrary, each serves as an impediment to the normal flow of commerce and to the maximization of sound economics in the use of the vehicles which transport it."

Finally, on the same day, Chairman Timm, in presenting the

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88 The President directed that the Mainland-Ponce award to Eastern should be deferred until April 1, 1975.
89 Remarks of Whitney Gilliland, Vice Chairman, Civil Aeronautics Board at Ceremonies Marking Deliveries of DC-10 Series 30 Convertible Freighter Aircraft to Overseas National Airways & Trans International Airlines, at 7-8, Long Beach, California (April 17, 1973).
Board's requests for fiscal 1974 appropriations to the Subcommittee for Department of Transportation and Related Agencies of the House Committee on Appropriations said:

The Board's number one priority, therefore, is to strengthen this system. This will be done by taking actions, sometimes bold and sometimes controversial, that will insure continuing progress. At the Civil Aeronautics Board, this means we are going to have to run to catch up with the people that we serve. We are going to have to change an attitude of mind and realize that the airline industry is no longer a growing child, but a mature adult. This maturity, in some cases, requires a more restrained set of regulatory reflexes and responses and in other cases, more flexibility than previously has been allowed.

What I am suggesting is that the airline industry should be afforded the same economic tools that other mature industries have, including a healthy and nondestructive competitive climate; responsible mergers, acquisitions, and diversification. *

Air carrier diversification will be another area in which new approaches will be considered during fiscal 1974. This is assured because of the Air Carrier Reorganization Investigation which is currently in process at the Board. This investigation is a comprehensive examination that has as its chief objective a determination as to what further regulations and/or legislation may be in the public interest to deal effectively with air carrier diversification. The Board is entering into this proceeding with an open mind. We have no preconceived notions of whether any particular type of diversification, including the holding-company approach, is either good or bad. Our intention is to rectify any deficiencies in aviation legislation or regulation, if indeed any exist, to prevent a reoccurrence of the Penn Central bankruptcy in the field of aviation.**

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**Statement of Chairman Robert D. Timm Before the Subcommittee for Department of Transportation and Related Agencies of the House Committee on Appropriations, April 17, 1973.