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REALIGNMENT OF THE DOMESTIC AIRLINE ROUTE PATTERN

By Louis E. Black, Jr.

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"To anyone familiar with all this background of history, 'ancient' as well as more recent, it is obvious that our failures have been due to administrative laxity rather than to ignorance of the constructive policies which have been plainly mapped out for our guidance."

I. INTRODUCTION

The commercial airline route pattern in the United States has been established, developed, and continuously regulated by the Federal Government. In 1918, the Post Office Department initiated air mail service using army planes and army personnel. By 1926, there were 8,252 miles of routes over which the Post Office Department was flying air mail. The Air Mail (Kelly) Act of 1925 provided that private carriers were to take over the transportation of air mail from the government. Air mail contracts and, later, air mail route certificates were awarded. Because of the necessity of obtaining air mail pay to support the cost of operation, the common carriage of passengers by air became an incident to the carriage of mail. For all practical purposes then, the Federal Government maintained effective control of the commercial air route pattern. From 1926 to 1938, through the award of air mail contracts and certificates for additional routes, the air carrier route mileage increased to 35,492 miles.

The Civil Aeronautics Act of 1938 provided that no air carrier could carry mail or participate in "air transportation" before obtaining a certificate of public convenience and necessity from the Civil Aeronautics Board. Section 401 (e) (1) of the Act, the "grandfather clause,"
authorized certification of all routes which had been in continuous operation from May 14, 1938, to August 22, 1938. By virtue of this provision, all the fallacies and mistakes in route structure in the former route pattern were perpetuated in the new route system. Since 1938, the Board has awarded certificates for additional routes so that there are now 135,575 miles of certificated interstate domestic routes. This figure indicates that there has been more than a 280% increase in route mileage during the period of CAB control of the route pattern. The commercial air routes, unlike the railroads and highways of the nation, were not laid out at random. Since 1926, with the exception of a few months in 1934, operation over the air routes has been by private enterprise, but throughout this entire period of development, the Federal Government, by naming and designating the routes to be flown, has maintained absolute control over the air route pattern.

It is generally recognized that there are many weaknesses in the present over-all route pattern. Because of technological development which has produced faster and more efficient aircraft, because of changes in population densities and relocation of industrial centers and marketing areas which have created new flows of commerce, and because of the general impetus to air transportation resulting from the development of air power during World War II, the airline route pattern should be adjustable to constant change and revision to meet these changing conditions. Routes once logically a part of one air carrier's network of operations now may be more properly integrated with another air carrier's system, or entirely discontinued. The Civil Aeronautics Act does not provide any explicit means by which either cancellation of route certificates or reallocation of routes for constructive purposes may take place. Some sections of the Act would permit such action indirectly. The transfer of route certificates among carriers as permitted by Sections 401 (i), 408, 412 (the Transfer Sections) of the Act affords one possible method of realigning routes.

In the following discussion, Board opinions in which certificate transfers have been considered will be examined and commented upon. Particular emphasis will be placed upon the legislative history of the Civil Aeronautics Act of 1938 as a background for proper interpreta-

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7 CAB, Mileage Book No. 1, Airport-to-Airport Mileages Over Interstate Routes of Certificated Air Carriers, 7th Rev., May 1, 1948.
8 This was the period during which the Army transported air mail. SMITH, AIRWAYS c. 20 (1944); Campbell, Procedural Due Process in the Cancellation of Air Mail Route Certificates, 21 Wash. L. Rev. 123 (1946).
9 United-Western, Acquisition of Air Carrier Property, 8 CAB 298 (1947) (majority and dissenting opinions); Statement of CAB before President's Air Policy Commission 203 (Oct. 27, 1947); Landis, Air Routes Under the Civil Aeronautics Act, 15 J. Air L. & C. 295 (1948).
10 A certificate may be revoked for continued wiful violation of the Act, a Board order, rule, or regulation, or condition of the certificate. §401(h), 52 Stat. 987, 49 USCA §481 (Supp. 1947). The Board has only approval powers over transfers under §401(i).
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In order to evaluate the problem which the Board faces in permitting a value to be placed upon an air carrier certificate of public convenience and necessity for the purpose of purchase and transfer, an examination will be made of administrative decisions permitting the transfer of certificates in other public utility fields under regulatory acts similar in form but differing in policy and purpose from the Civil Aeronautics Act. By this process, it is hoped that a conclusion can be reached concerning the plausibility of the Board's position regarding transfer of certificates and a suggestion made as to the maintenance of flexibility of the route pattern.

Statutory Scheme of Regulation

In many sections of the Act, the term "public interest" furnishes the standard for action on the part of the Board. Section 2 specifies the elements which the Board shall consider in its interpretation of "public interest" and treats the term as being synonymous with the expression "public convenience and necessity." For all domestic air carriers these words have a uniform, consistent meaning and application. Section 401 (d) (1) of the Act requires the CAB to issue a certificate to an applicant for transportation "required by the public convenience and necessity." (Emphasis supplied throughout.) Section 401 (i), regulating transfer of certificates provides: "No certificate may be transferred unless such transfer is approved by the Board as being consistent with the public interest."

Section 408 of the Act, under which the CAB must apply the test of "consistency with public interest," regulates the acquisition of air carrier property. Any contract or agreement relating to the transactions authorized in Sections 401 (i) and 408 must be filed with and approved by the Board under the provisions of Section 412. Here the CAB must disapprove any agreement it finds to be "adverse to the public interest."

Note that in all of these sections the Board is required to apply the same test, public interest, before it approves the acquisition and transfer of a certificate. Section 408 (b) contains an additional proviso that

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11 Practically every provision of §401 requires a direct reference to §2, the Policy Section of the Act, for a consideration of the terms "public convenience and necessity" and "public interest." 52 Stat. 980, 49 USCA §402 (Supp. 1947).
12 Ibid. "... in the public interest, and in accordance with the public convenience and necessity..."
13 The pattern of regulation set up under the Act affords a much more exemplary treatment of foreign air carriers. Their permits, in contrast to the U.S. air carrier's certificates, may be revoked by the Board "in the public interest." Compare §401, supra note 10, with §402 of the Act, 52 Stat. 991, 49 USCA §482 (Supp. 1947). But see, Waterman Steamship Co. v. CAB, 333 U.S. 103 (1948); Note, 61 Harv. L. Rev. 1053 (1948).
15 Ibid.
when the CAB approves transfer of a certificate a monopoly restraining competition or jeopardizing another air carrier must not be created. In compliance with these sections, when one carrier desires to obtain the certificate of another air carrier by purchase, merger, lease or acquisition of control, it must apply for approval of the transaction under Section 408. Similarly, the contract or agreement evidencing the terms of acquisition must be approved under Section 412. After a public hearing at which all interested parties may be heard, the transaction will be approved if “consistent with” and “not adverse to” the “public interest.” The actual transfer of the certificate will be approved under Section 401 (i) if “consistent with the public interest.”

Thus it makes no difference how a certificate is acquired from the original holder; whether by direct transfer, consolidation, or merger, or through acquisition of controlling interest in the holder, the test in any case will be the same. To construe the statute otherwise would violate established rules of construction to the effect that nothing can be permitted to be done indirectly which is prohibited from being done directly.

II. CAB Decisions

In the following discussion, an examination will be made of the problems confronting the Board in approving acquisition of one air carrier’s certificate by another air carrier. Only those cases affecting the domestic route pattern of the United States will be reviewed.18

The CAB was called upon to consider this problem at an early date.19 On July 7, 1939, United Air Lines applied to the Board for approval, under Section 408 (b) of the Act, of either (1) acquisition of control of and merger with Western Air Lines or (2) purchase by United of all of Western’s assets. A look at a map of the United States reveals the purpose of United’s application. United passengers desiring to reach Los Angeles from points east of Salt Lake City on United’s routes either had to fly to San Francisco and then down the coast to Los Angeles or disembark at Salt Lake City and then fly via Western to Los Angeles. Either method was inconvenient and time consuming. TWA and a minority group of share holders of Western intervened. The case was turned over to Hon. Roscoe Pound as a special trial exam-

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18 Any study of the international route pattern of U.S. air carriers would necessarily involve a discussion of the “Sea-Air” and “Chosen Instrument” controversies, which would enlarge discussion beyond reasonable limits. International and territorial route transfer cases containing important Board policy statements, unless otherwise noted, will be discussed in footnote.

19 Acquisition of Western A. E. by United A. L., 1 CAA 739 (1940). At that time United held certificates for routes from New York City to San Francisco, California, via Denver, Colorado, and Salt Lake City, Utah; from San Diego, California, to Seattle, Washington; from Seattle to Salt Lake City and from Denver to Cheyenne, Wyoming. Western held certificates for two routes: one from San Diego, California, via Los Angeles to Salt Lake City, the other from Salt Lake City to Great Falls, Montana.
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iner. After development of a complete record, Mr. Pound recom-
mended that acquisition be approved and that the Board proceed
to pass upon the acquisition plan to assure fairness to
intervening minority share holders of Western. After reargument, the
Board, in direct opposition to the examiner's finding, held the agree-
ment not to be in the "public interest" and therefore disapproved it.
The Board, in its opinion, quoted subsections (a) and (d) of Section 2
of the Act in full and stated:

> "Any merger or other form of acquisition, therefore, which, by
> stifling normal competition or by encouraging destructive competi-
> tion, would tend to retard or prevent the development of an air
> transportation system properly adapted to the present and future
> needs of the Nation must be deemed inconsistent with the public
> interest. We accordingly proceed to examine the effect of the pro-
> posed merger or purchase of assets in the light of the standards of
> public interest set forth in the above-quoted subsections." 20

The Board noted two reasons, both affecting competition, for not
approving the agreement. First, if the acquisition were approved,
United would obtain direct access to three main traffic generating cen-
ters on the West Coast, Los Angeles, San Francisco and Seattle, a
competitive position enjoyed by no other transcontinental carrier.
Furthermore, United would have more route mileage and serve a
greater population west of the Rockies than any other transcontinental
carrier, which would permit it to funnel an enviable share of the west-
est traffic into its transcontinental route. Second, by acquiring West-
ern's routes, United would monopolize traffic in the area west of the
Rockies. Since the agreement was disapproved, the Board did not con-
sider the plan of acquisition, valuation of assets, including the certifi-
cates of convenience and necessity, or mention Section 401 (i).

On the same date that the Board disapproved acquisition of West-
ern by United, it approved, as being in the public interest, an agree-
ment between United and Western for interchange of equipment at
Salt Lake City. 21 In this latter decision the Board discussed in detail
the meaning of "public interest" as contained in Sections 408 and 412.
The Board, after careful consideration, found that "public interest,"
whether preceded by "not consistent with" or "adverse to," had essen-
tially the same meaning and that the same factors must be evaluated in
a proceeding under either Section. From the Board's point of view,
two important problems were involved: "(1) whether or not any re-
straint of competition would prevent approval . . . ; (2) whether or not
jeopardy to another carrier would prevent such approval without re-
gard to the existence of a monopoly." 22 The Board found that the an-

20 Id. at 745.
21 United A. L.-Western A. E., Interchange of Equipment, 1 CAA 723 (1940).-
22 Id. at 732.
swers to these problems depended upon the meaning and application of the provisos in Section 408 (b). In the interpretation of them the Board stated:

"It follows that restraint of competition is a factor... only if it results from that degree of control which the Authority decides constitutes a monopoly of air transportation... In deciding upon the application of the proviso in Section 408 (b) to the agreement, therefore, it is necessary to determine whether it will result in giving one of the parties the degree of control of air transportation, or some phase thereof, within a particular section of the country, necessary to constitute a monopoly therein."23

These two decisions considered together lead to the conclusion that at this stage of air transport development, the Board, in determining "public interest" in sections of the Act being discussed here, placed primary emphasis on competition in fostering a reasonably balanced system of air transportation in every section of the country and on prevention of monopoly in any area.

Only a few weeks after the Western-United opinions the Board handed down another decision in which it was necessary to consider at length the public interest aspects of acquisition of the certificate of one air carrier by another. In this case, Acquisition of Marquette by TWA.24 TWA sought CAB approval of a contract by terms of which TWA would acquire all outstanding stock, business and assets of Marquette Airlines. The only intervenor was the Air Line Pilots Association. The application for approval was filed under the Transfer Sections. Marquette was operating under authority of a grandfather certificate granted in a proceeding which had been reopened and was at that time under investigation by the Board.25

The Board found that so far as the route itself was concerned, operation by TWA would promote an improved service and develop traffic potentialities along the route. Acquisition on this basis would be consistent with the public interest. The Board reiterated its holding in the Western-United Interchange case, and turned to a consideration of the terms of acquisition. The Board found that in return for the payment of approximately $500,000.00, TWA would receive assets of Marquette valued at the most at $30,000. It was therefore apparent that the bulk

23 Id. at 734.
24 2 CAB 1 (1940).
25 It was alleged that Marquette had fraudulently obtained its certificate because a part of Marquette stock had been held by Canadian nationals, thus leaving in doubt the question of United States citizenship, a sine qua non of certification. (§§ 1(2) and 401 (a) of Act.) Marquette's route extended from Detroit to St. Louis with intermediate stops at Toledo, Dayton and Cincinnati, Ohio. Marquette's operation over this route of heavy traffic potential had been far from spectacular. Marquette was operating old, out-moded and inefficient equipment one round trip per day, four days per week. During 1939 it had flown 81.57 per cent of its scheduled mileage and had an average load of only 2.03 revenue passengers. Operations from May 4, 1938 to January 31, 1940 had resulted in a deficit of $208,281.04.
of consideration to be paid was for items of an intangible nature. TWA cited as justification for the purchase price amounts paid by United and Eastern for transfers of air mail contracts under the Air Mail Act of 1934. The Board refuted this line of reasoning by making a clean break with this alleged precedent and refused to give evidential value to proceedings which did not involve transfer of operating rights under the Act.

TWA's assertion that the price was reasonable, since profit to one McKelvy was not excessive, was similarly turned down by the Board as there was no showing that investment lost in operating deficits had in any way enhanced the value of Marquette as a going concern or increased the value of any of its assets. TWA argued that the price was justified in light of potential earning capacity of the route as a part of TWA's system. To this argument the Board replied that this fact alone is not sufficient to determine reasonableness of a proposed price, especially when the amount to be paid is 15 times the value of tangible property to be transferred and there is little going concern or good will value inherent in the property. The Board then summarized into one question the gist of the finding which must be made in approving valuation in a route transfer case:

"The question which confronts us, therefore, is whether the expenditure by a carrier under our own jurisdiction of a large sum of money from its corporate funds is warranted in the acquisition of what amounts to little more than a bare certificate of public convenience and necessity."

"A certificate of convenience and necessity given to an air carrier conveys the privilege of operating as a common carrier between certain points. The privilege is one granted by Government in the interest of an orderly and sound economic development of air transportation. Persons enjoying such a privilege may use it to build up a valuable property, possessed not only of physical assets but also of substantial going concern value, representing the experience, the goodwill, and the collective competence developed by the operating organization. Individuals cannot create the privilege that the certificate conveys; they do not exercise that privilege without restriction; and they cannot transfer it except under terms imposed by law.

"It would be clearly adverse to the public interest, as defined in the Civil Aeronautics Act, to allow a certificate of convenience and necessity to be treated as if it were a speculative security, to be sold by the holder to the highest bidder, or as if it were possessed of a

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26 From the sum over and above value of assets transferred, one McKelvy, promoter and principal owner of Marquette, would realize more than a 20 per cent profit on his total cash investment in Marquette, and a third party would receive $35,000.00 for merely bringing the contracting parties together.

26 See note 26, supra.

27 "These transactions involved the transfer of air mail contracts granted under the provisions of the Air Mail Act of 1934, as amended, which did not impose a jurisdiction over transfers of air transport operations such as is provided by the Civil Aeronautics Act. They, therefore, have little probative value in the present proceeding." 2 CAB 1, 12 (1940).
value of its own, distinct from the legitimate expenses of initially securing a certificate, and from the values developed by the conduct of operations under the certificate. The transfer of certificates at inflated or speculative prices would not foster sound economic conditions in air transportation, as required by the provisions of Section 2 of the Act. It would not promote economical and efficient service at reasonable charges. It would not avert unfair or destructive competitive practices, but would serve rather to encourage the appearance of such practices. We conclude that payments for the sole purpose of effecting a transfer of a privilege conveyed by public authority, with the expectation that they will at sometime be recovered by the purchaser from the users of the service or from air mail compensation paid by the Government are not in the public interest.

"We find that the price provided by the terms of the contract which is before us is excessive."\(^{28}\)

The Board therefore held that acquisition of Marquette by TWA under terms and conditions of the contract before the Board must be denied as not being consistent with the public interest.

In a supplemental opinion the Board recanted from this position. The First Marquette case was decided on July 3, 1940. Subsequently, the parties modified the terms of the transfer agreement and TWA was given permission by the Board to operate under Marquette's certificate of convenience and necessity and Marquette was relieved of all responsibilities thereunder. TWA and Marquette then petitioned the Board for reconsideration of its order of July 3. The Board now had before it a new agreement and traffic data compiled by TWA from its operation of the Marquette route. Up to this point, Board decisions regarding acquisition and transfer of certificates had been unanimous, but with the Second Marquette case unanimity was dispelled.\(^{29}\)

By the terms of the modified agreement the purchase price to be paid by TWA was reduced by one-third, payment to the third party intermediary was eliminated, and TWA was to take Marquette's certificate clear of any infirmities due to reopening of the Marquette Grandfather case.\(^{30}\) The majority, citing Supreme Court cases\(^{31}\) noted the distinction between transfer value of a certificate and valuation of property to determine rate base value of a public utility. After citing the parallel between the Civil Aeronautics Act and the Motor Carrier Act and decisions of the Interstate Commerce Commission approving transfers where operating rights were given independent value, they held that acquisition would now be approved. Inasmuch as other airlines

\(^{28}\) 2 CAB 1, 14 (1940).

\(^{29}\) Acquisition of Marquette by TWA, Supplemental Opinion, 2 CAB 409 (1940). Board Member Branch, who had not participated in the original decision, now sided with Mr. Oswald Ryan in a majority opinion. Board Member Baker wrote a separate concurring opinion. Member Warner dissented.

\(^{30}\) Marquette Air., Grandfather Certificate, 1 CAA 301 (1939).

did not intervene, the Board merely affirmed its former finding that the acquisition would not result in a monopoly, restrain competition or jeopardize another air carrier. Considerable evidence was introduced concerning the successful operation by TWA of the Marquette route. Considering these facts as related to the purchase price the majority stated:

"The public interest in the purchase price involved in a transfer such as that here before us, rests upon the fact that an extravagant and unreasonable price may result in a depletion and waste of the purchaser's assets, with the resultant imposition of additional obligations upon the public or an impairment of the service now being rendered to the public by TWA. No such conclusion is justified by the facts presented in this proceeding. On the contrary, TWA anticipates, and the anticipation does not appear unduly optimistic in the light of the supplemental evidence, that the operation of the Marquette route will result in the strengthening of TWA's financial and operating position over the period of a few years. It is obvious that the purchase price can properly be regarded as only one element of the public interest in a case of this nature and that it must be carefully weighed in connection with all other applicable factors. Certainly the improvement and expansion of existing service to the public and the financial strengthening of an existing carrier, both of which are found to be reasonably expected results of the present acquisition, are consistent with and will advance the public interest. The public interest has direct relation to the adequacy of transportation service, to its essential conditions of economy and efficiency, and to appropriate provisions and best uses of transportation facilities." 32

Thus the Board merely reiterated its finding in the earlier decision that the Marquette route was more properly an integrated part of the TWA system than an independent route and added that in this particular case such a factor coupled with anticipated financial earnings from the route would outweigh objection to price paid for the route certificate. The Board made no effort to explain from what source the sum of approximately $200,000 which TWA would pay Marquette for the certificate would ultimately be derived. The question of payment of any sum to a corporation unable to prove lawful ownership of a privilege originally granted to it gratuitously and to which it had contributed nothing, also goes begging. The Board placed a condition upon approval to the effect that value permitted a certificate for transfer purposes was neither binding upon the Board nor determinative of value for rate making or other purposes. 33

In a concurring opinion Mr. Baker stated that he felt that it was in the public interest to allow management to determine the price to be

32 Marquette Air., supra note 30 at 415.
33 Thwarted at every turn in its effort to obtain complete information concerning citizenship of Marquette during the grandfather period, and faced with the prospect of prolonged judicial proceedings in Canada, the Board in a second supplemental opinion closed the Marquette Grandfather case and perfected transfer of Marquette's certificate to TWA. Marquette Air.—Grandfather Certif.—Acquisition by TWA, Supplemental Opinion, 3 CAB 111 (1940).
placed on a certificate and that the proper realm for administrative control was in a revised rate-making procedure which included franchise value. A majority of the Board therefore completely reversed the position taken in the First Marquette case on the issue of the advisability of allowing a price to be placed on a certificate to be transferred.

Mr. Warner, however, wrote an emphatic dissent in which he affirmed the Board's former holding and, after a discussion of the purpose of a certificate as issued under the Act, stated:

"Any sale by one party to another at a price including allowance for a value of the certificate necessarily connotes an expectation on the part of the purchaser that there will be received in some fashion, either from the public through air mail compensation or from the traveling public through the payment of commercial charges, enough income to justify the payment made for the certificate. To sanction such a sale would be to sanction the ultimate placing of an additional burden upon the public, through the allowance of speculative transactions in an exceptional right which had been created only to the end that the public interest might be better served."

Mr. Warner then added that in allowing transfer value to be placed on a certificate, the Board was violating mandates of the policy section of the Act, especially those parts requiring the fostering of sound economic conditions in air transportation and promotion of service by air carriers at reasonable charges.

Mr. Warner also discussed the question of value. He felt that public interest required that a valuation of an airline enterprise should be determined by what owners had in fact contributed by their effort and should exclude any pricing of privileges conveyed by the government issued franchise. He particularly deplored the practice condoned by the majority of permitting losses incurred without benefitting service rendered or physical and economic status at time of sale, to be capitalized into purchase price. Going concern or goodwill value could easily be separated from certificate value according to valuation methods offered by Mr. Warner.34

In Western A. L., Acquisition of Inland A. L.,35 the Board was called upon to approve acquisition of control, purchase of assets and certificate of convenience and necessity of Inland Air Lines by Western Air Lines. The Air Line Pilots Association intervened but, upon being assured that seniority rights of pilots would be maintained, withdrew. Although the CAB approved transfer of Inland's certificate to Western, at no place in the opinion does the Board so much as mention Section 401 (i). It is difficult to determine whether or not this omission was an

34 "... public interest would justify only the placing upon that enterprise of a valuation representing the reasonable commercial value of what the initial owners had in fact contributed by their effort, and excluding the value of the rights and privileges created by a public agency through the certificate of public convenience and necessity." Id. at 420.

35 4 CAB 654 (1944).
oversight or whether the Board believes that a finding of "public interest" under Section 408 satisfies the requirements of other sections involved in an acquisition and transfer case, and that they therefore do not have to be mentioned or discussed. Clarification would seem to be desirable.

By terms of the acquisition agreement, certain officials of Inland were to be retained in the employment of Western, and Western was to pay $415,271.76 for Inland’s assets which had a book value computed variously from $122,560 to $296,002. Western asserted that the difference between purchase price and book value represented the fair market value of Inland’s equipment and leases, and therefore no part of the purchase price needed to be allocated to goodwill, going concern or franchise value. Western did admit, however, that inasmuch as Inland had been engaged in operations over the same route for nearly 14 years, it very definitely had going concern, goodwill and franchise value. The Board found that the financial status of Western would not be impaired by the acquisition and that the monopoly and competition factors of Section 408 were satisfied, since the two systems were in no way parallel, each serving a different area. The Board quoted from directives contained in Section 2 of the Act and then, surprisingly, stated:

"Examination of the past flow of traffic over the routes of Western and Inland, the existing community relations along the route, as well as the geographical situation, reveals that the proposed union of the two carriers will offer nothing in the development of an integrated and coordinated transportation system... Figures indicate that the chief community of interest of the cities on Inland’s route is with the market centers east of the Rocky Mountains and reflect a lack of community of interest between the Western and Inland systems. These facts lead to the conclusion that the proposed acquisition will not create an integrated pattern of air transportation and will result in little new through service but will simply put under one management two presently independent operating routes, serving different territories and different needs and having a single common point." 36

The Board held, however, that this complete lack of integration was offset by the desirability of substituting Western management for that of Inland, even though the two principal owners and officers of Inland were to remain on Western’s payroll for a term of two and one-half years.

As stated previously, the Board approved the acquisition and transfer of Inland’s certificate. Board Members Warner and Branch dissented from that part of the opinion which approved payment of salaries to former officers of Inland. They felt that viewed in its most favorable light, this employment contract was void for lack of mutuality and amounted to nothing more than a hidden commission or bonus for negotiating and consummating the acquisition.

36 Id. at .660.
Board Member Lee dissented. Mr. Lee struck at what he felt was the basic fallacy of the majority decision, namely a complete disregard of mandates of Section 2 of the Act requiring the Board to take a long range planner's view of fostering an airline route pattern which would promote and develop an integrated system of air transportation. He quoted in detail definitions of the word "system" and added — "The implication of the word goes further and includes the idea not only of a large overall pattern, but also of a pattern based on principle, a design into which the parts are fitted and not thrown haphazardly."  

Mr. Lee felt, in addition, that inasmuch as it had been the declared policy of the Board since the United-Western Merger case to strengthen Western as a regional carrier, public interest would be unfavorably affected by the financial burden imposed on Western by acquisition of Inland. Thus, in Mr. Lee's dissent, for the first time the relationship of acquisition cases to the airline route pattern is stressed.  

37 Id. at 665 (Lee, Member, dissenting). Following are additional quotations from Mr. Lee's dissent: "The air pattern of each individual carrier's route system is the foundation of the overall national system. Therefore, the Board in taking a long-range view of air transportation, which is contemplated by the language of the Act, must concern itself with the creation of a properly integrated route system for each individual carrier..."

"The approval of a merger is as permanent as the granting of a new route, and should be approached with the same concern for a properly integrated air system, because once it is done it cannot be undone..."

"It is the function of the Board to plan in advance the formulation of sound route patterns for the individual carriers. In effectuating this result the Board may use the veto power with respect to acquisition and mergers. Although the exercise of this power makes no change in the national air map, it can prevent the formation of an unsound route system for individual carriers."

38 In United A. L., Acquisition of Lamsa, S. A., 4 CAB 409 (1943) the Board approved under Section 408, United's acquisition of an airline whose routes were wholly within Mexico. Even though this acquisition in no way affected the domestic airline route pattern, the Board's opinion is noteworthy. The physical assets of Lamsa were valued at $32,000, for which United proposed to pay $145,750. United's president testified that Lamsa enjoyed "goodwill" which he felt was permanent and well worth $113,750, part of the purchase price allocable to intangibles, franchises and goodwill. United intended to spend approximately $1,000,000 in the future to improve Lamsa's service, but for the present proposed to use all Lamsa equipment and add only a few supervisory personnel. On these facts, the Board found that the purchase price was not disproportionate to the value of the property and business of Lamsa, including operating rights, that there were no go-betweens, finders' fees or commissions to be paid, that there would be no harmful effects on United's financial position and therefore the acquisition would be approved as not being inconsistent with the public interest. Although American intervened, the Board did not discuss the monopoly and competition provision of Section 408. Note that in this case where a complete airline, an operating unit, was purchased and its business name continued, its personnel and operations remaining the same, the Board tacitly recognized and approved the valuation of franchises and goodwill. (The Board very easily could have made an exception in approving the Lamsa acquisition without discussing valuation problems because of the national defense aspects of public interest involved. Several foreign airlines, including those controlled by fascist governments, were interested in obtaining Lamsa. Id. at 413.)

From time to time, Pan American Airways has transferred its certificates to subsidiaries and vice versa. In cases involving transfer of certificates within a corporate family, there are very few factors that the Board can consider as being in the public interest since status quo, for all practical purposes, remains the same. See, e.g., United, Medellin, Cent. Airways—Canal Zone—Columbia Op., 2 CAB 334 (1940); Pan Am. Airways Merger, 2 CAB 503 (1940); Acquisition of Pan Am. Airways—Africa, Ltd., 3 CAB 32 (1941).

In Wein Alaska Air—Acquisition—Mirow Air Service, 3 CAB 207 (1941),
In Acquisition of Mayflower Air by Northeast Air, the Board found that Mayflower's certificate was of doubtful value and that sale of certificates at inflated values was not conducive to development of an economically sound air transportation system. The Board therefore refused to approve acquisition of Mayflower's certificate by Northeast unless the sale price was reduced from $17,500 to $10,000. Later, in a supplemental opinion, the Board approved acquisition and transfer at the original price. This it did without commenting upon the fact that regardless of who offered to buy Mayflower's certificate at any price, the transfer would in all cases have to be approved by the Board as being in the public interest.

In the National-Caribbean-Atlantic Control, a case complicated by the fact that without Board approval National had acquired control of Caribbean-Atlantic prior to the proceeding, the CAB disapproved an acquisition agreement on facts directly paralleling those of the Western-Inland case. Here National, which held certificates for routes in the southeastern part of the U.S., sought approval of acquisition through a stock exchange agreement of Caribbean-Atlantic, which, some 1000 miles away from National's region, operated over routes in and between Puerto Rico and the Virgin Islands. The Board denied the application on several counts. It was obvious that the acquisition would offer nothing toward the development of an integrated and coordinated air transportation system.

Concerning approval of purchase price in acquisition cases, the Board said:

"There are several factors to be considered in determining whether the purchase price is such as to render the acquisition..."
inconsistent with the public interest. The reasonableness of the acquisition price may not be judged solely whether the purchaser can pay that price. The investment might exceed the reasonable and fair value of the property used and useful in the operations of the acquired carrier and the purchase of such assets might impose such obligations as to weaken the purchaser's financial structure or necessitate higher rates and the ultimate payment of greater mail subsidies, particularly where there is no integration of operations." 43

The Board then reviewed in detail the proposed transaction and held:

"We are convinced that an excessive price paid for an air carrier, in one form or another and in the long run, comes out of the pockets of the traveling and investing public, and the willingness of a larger carrier to acquire control of a small, isolated carrier at a price beyond a reasonable value would be of grave concern to us. The air map of this country could be changed as drastically by acquisition of control as by obtaining certificates of public convenience and necessity for new routes. In building up well-balanced route systems, acquisitions of control sometimes contribute to progress in the industry. However, the test is the public interest and not the acquisitiveness of private managements whose ambition might lead to the formation of systems that are too large for effective operation, to trafficking in certificates, or to other questionable maneuvers, which might result in destroying a balance which has been carefully built up. The acquisition of control probably would result in some improvements in the service rendered by Caribbean because of National's greater financial resources and technical skill. We find however that the lack of integration of operations and the consideration called for by the acquisition agreement compel the conclusion that the acquisition is inconsistent with the public interest and the application should be denied." 44

Thus, although lack of integration of operations and valuation were given secondary importance in the Western-Inland decision, the Board here seems to accord these same factors controlling consideration. Since the acquisition was not approved, the Board did not discuss the applicability of Section 401 (i) but treated the application as involving only Sections 408 and 412.

United A. L., Operation of Catalina Air Transport 45 is a typical example of the type of CAB opinion which makes difficult the task of reconciling the acquisition cases. Catalina held a grandfather certificate authorizing air transportation of persons and property from the Los Angeles area to Santa Catalina Island, a distance of roughly 35 miles.46 By terms of the agreement before the Board for approval, United would take over all operating rights for the period of one year,

43 Id. at 677.
44 Id. at 682.
45 6 CAB 1041 (1946).
46 All of Catalina's aircraft were requisitioned during the war and at the time of application, operations had been suspended for almost four years. Catalina estimated that a capital outlay of over $200,000 would be necessary before it could commence operations. As a result, Catalina preferred not to re-enter the business of air transportation if United could furnish adequate service.
with the right of renewal of the agreement from year to year, in return for a flat rate payment to Catalina per revenue passenger transported, subject to minimum and maximum annual totals of $15-25,000 respectively. This sum was to be treated as rental for the exclusive use of the airport on Catalina Island. All Catalina had to do was keep the airport in repair and receive payment from United. It is difficult to see how this transaction could be treated as anything other than a transfer of Catalina’s certificate to United for a renewable term, yet the Board does not mention Section 401 (i) or even note that the section in any way applies. The Board also found that the Catalina service, essentially a local, seasonal, feeder and shuttle operation would be properly integrated with that of a transcontinental, long haul carrier, United, when less than two weeks prior to its decision it had awarded a certificate for local and feeder operations, in the Los Angeles area to Southwest Airlines.Granted that no feeder airline intervened and conceding that it was desirable for United to utilize equipment and personnel during turn around at Los Angeles, the fact remains that the Board relegated a consideration of a beneficial airline route pattern to a very minor role. The Board approved the agreement as not resulting in a monopoly, restraining competition or jeopardizing another air carrier.

In a case decided September 27, 1946, the Board ruled upon the acquisition of Mid-Continent Airlines by American Airlines under a proposed stock transfer agreement with the holder of a controlling block of Mid-Continent stock. Labor unions, airport commissioners, and ten airlines intervened. American is the largest transcontinental carrier, while Mid-Continent operates over a north-south route in the center of the nation from Minot, North Dakota to New Orleans. The Board reviewed the history of Mid-Continent and of negotiations leading to the present petition. The Board noted that the term “public interest” as found in Section 408 (b) must be determined by the statutory objectives set forth in Section 2 of the Act and then stated what it thought to be the correct formula for proceeding upon such a determination:

“The ultimate question to be decided in this proceeding is whether the proposed acquisition is not consistent with the public interest. Adjudication of this issue is a balancing process. No single factor is controlling; rather, we must weigh all the considerations disclosed by the evidence relating to the high purposes enumerated in section 2 of the Act, in order to calculate, as near as may be determined, the probable net effect of the proposed transaction upon the public interest.”

Quoting from the National – Caribbean-Atlantic Control case, the Board thought its first inquiry should be directed to the question of

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47 West Coast Case, 8 CAB 961 (1946).
48 Am. Air., Control of Mid-Continent Air., 7 CAB 365 (1946); Note, 14 J. Air L. & C. 391 (1947).
49 Id. at 372.
whether or not the proposed transaction would promote development of a well-integrated, internally coordinated pattern of air transportation. They found the systems to be entirely uncomplementary as to flow of traffic and development of traffic potential. Furthermore, the Board found that many of the intervening carriers would be injured by the acquisition through loss of traffic and that American would enjoy a superior competitive advantage through its control of originating and terminating points to which other carriers had no access. The Board then turned to an evaluation of the economic arguments of American, such as the weak financial position of Mid-Continent, and benefits which would result from acquisition, such as fare reductions, reduced mail pay, lower operating costs etc., and found them to lack convincing proof. For these reasons the agreement was not approved. Therefore the Board did not discuss valuation and purchase price, or mention the applicability of Section 401 (i).

In Orlando Airlines, Transfer of Certificate, the Board was confronted with an acquisition involving a factual situation very similar to the TWA-Marquette case. The only distinction is that whereas TWA was a going concern, the acquiring air carrier here would have to inaugurate operations under a temporary feeder certificate. Assuming that underlying legal and economic principles remain the same, it is difficult to see how this distinction could in any way affect the Board's reasoning.

By terms of the agreement, Orlando Airlines, the private enterprise of one Gordon, proposed to transfer its assets and certificate to Florida Airways, a corporation organized and controlled by the same Gordon, in exchange for assumption of Orlando's liabilities and issuance of Florida stock to Gordon. Florida would carry on its books at $268,677.76 the assets and cost of the certificates of convenience and necessity acquired from Orlando, would assume liabilities of Orlando amounting to $138,517.82 and issue shares to Gordon in the face amount of $130,130.00. This latter amount approximately equaled the operating losses of Orlando which it had capitalized in order to transfer as an asset. The Board noted without comment the value of $12,437.36 assigned to the certificate which amount represented the cost of securing it. The Board stated what it considered to be primary considerations of public interest in a transfer proceeding involving a feeder line under Sections 401 (i) and 408 (a): (1) Effect of such arrangements on air transportation; (2) Effect on experimental feeder program; (3) Effect on ability of feeder air carriers to attract capital; (4) Effect on requirements for increased mail pay. The Board, citing a Brandeis opinion, stated it knew of no theory by

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50 7 CAB 429 (1946).
51 This practice is permitted under §§1910-1920 of CAB, Uniform System of Accounts for Air Carriers, CAB Form 41 Manual 1-1-47.
which past operating losses could be capitalized as an asset on the books of a regulated enterprise and unanimously held that the transaction would unduly burden Florida by being saddled with Gordon's past losses and that the transfer should be denied as not being consistent with the public interest. One fact concerning the Orlando case should be noted. The Board nowhere mentions or so much as cites any of its prior holdings in acquisition cases.

In *Transcontinental & W. A., Route No. 38 Transfer*, the Board deferred until after the outcome of the Arizona-New Mexico feeder-line proceeding a determination of whether or not the transfer of TWA's Route 38 to Arizona Air would be approved. Contrary to the Catalina decision, the Board here found that Route 38, which extended from Phoenix, Arizona, to Las Vegas, Nevada via intermediate points, in contrast to its present operation by a long haul carrier, could be profitably integrated with a local system. The Board also noted that the proposed purchase price of $100,000 almost equaled the loss of $103,000 which TWA had suffered in operating the route. In return, TWA was to receive stock holdings enabling it to maintain a 20 per cent interest in Arizona Air. The Board noted that Arizona Air, as a "need" carrier would require breakeven mail pay based on a reasonable return on investment and "thus if Arizona Air showed profits because of this mail pay, TWA would receive 20 per cent of these profits as against certain losses if it flew the route itself. For that privilege TWA seeks to receive $100,000!" The public interest in preventing such a transfer is obvious.

The case is unique in that the Board recognized that TWA received air mail pay on an overall, systemwide service-rate basis, but at the same time the Board broke down operation expenses, mail pay and costs to evaluate the worth of Route 38. If any progress is to be made toward reorganizing the whole airline route pattern of the United States, this sort of individual route appraisal would seem to be most desirable.

The case is noteworthy for another reason. It will be recalled that most of the air carriers operating west of the Mississippi intervened in the *American-Mid Continent* case. Similarly, all the air carriers operating in the Route 38 region intervened in the present proceeding, indicating that the airlines have begun to realize the significance of acquisition cases as a whole. Participation of a large number of interveners in an administrative proceeding would seem to be the only method of assuring judicial review in case of administrative error.

To form a basis for understanding the most significant acquisition case yet decided by the Board, *United-Western Acquisition Air Carrier...*
the historical setting should be furnished. It will be recalled that in the Western-United Acquisition and Interchange cases the Board, overruling the examiner’s finding, decided that the public convenience in through service by United from points on its system to Los Angeles, was overridden by public interest in maintaining Western as a strong independent carrier and also by the superior competitive position which United would have if the acquisition were approved.

On November 11, 1944, the Board awarded the certificate for Route 68 between Denver and Los Angeles to Western Air Lines. The examiner in this proceeding recommended that United’s application should be granted and that all others should be denied. After narrowing the field of applicants to United and Western, the Board again contrary to an examiner’s recommendation, awarded the route to Western. It felt that if the route were awarded to United, traffic would be diverted from Western’s Los Angeles-Salt Lake City route with the result that Western would be financially weakened. This would be contrary to the Board’s policy for the development of Western as set forth in the Western-United Acquisition and Interchange cases. Because of the spirited competition for Los Angeles traffic, the Board thought that United and Western could work out a successful interchange agreement. Thus the Board, at the expense of public convenience, reiterated its policy of maintaining Western as a strong independent carrier, economically sound because of ownership of a route dangling parasitically from United’s transcontinental system and affording United traffic the only direct entry into Los Angeles.

In light of subsequent events, one paragraph of Member Warner’s concurring opinion in the Route 68 case is interesting. Mr. Warner

Appeal Under §1008(e) of the Civil Aeronautics Act, 15 J. Air L. & C. 365 (1948).

In Northern Consolidated Air., et al., Consolidation, 8 CAB 110 (1947), the CAB recognized that the finding made under either §408 or 401(i) in an acquisition case is the same since public interest is the controlling factor of either of them and approved a consolidation agreement which contained valuation of goodwill and franchises at approximately 25% of total assets involved. Member Young dissented on the basis that the Board should not approve self-determined valuations of franchises, assets, and going-concern value.

Shortly thereafter, the Board approved transfer under Section 401(i) of the certificate of Woodley Air way, a partnership, to Pacific Northern Airlines, a corporation formed to take over partnership assets. The Board found that the value of stock to be issued to the partners was not disproportionate to the value of property received by the corporation from the partnership. Pacific Northern Air., Certificate Transfer, 8 CAB 217 (1947).

8 CAB 298 (1947).

Supra notes 19 and 21.

Western A. L., Denver-Los Angeles Service, 6 CAB 199 (1944).

United was granted judicial review of the Board’s opinion. United A. L. v. CAB, 155 F.(2d) 169 (App. D.C. 1946). The court held that it was for the Board to interpret the policy section of the Act and to determine what was in the public interest, convenience and necessity; found that the Board had not violated any legal requirements in its proceeding; and that the Board had merely determined in the public interest to maintain the strong competitive and economic position of Western in national air transportation as well as in the western part of the country.
favored award of the route to Western, but tempered his opinion with the following remarks:

"It must, of course, be taken into account that continued technical development of transport aircraft may in the future make it economically desirable to conduct nonstop operations between Mississippi Valley and the Pacific coast. When that point is reached the question of United's access to Los Angeles from the east, for the purpose of conducting such flights, may be expected to arise once more; but at the moment it is only necessary to recognize the prospect of its resurgence, and to anticipate that it will then be dealt with in the light of the traffic flow and the state of the aeronautical art as then existing." 60

One would think from Mr. Warner's statement that the Board, after twice refusing to grant United a route from Los Angeles to a point on its transcontinental system, had finally realized that Route 68 at some future date might more properly be an integrated part of United's operations and would have conditioned the certificate issued accordingly.61

Western began operations over Route 68 on April 1, 1946. Only a year later United and Western filed joint application with the Board under the Transfer Sections for approval of an agreement providing for transfer by Western to United of certain equipment, four DC-4's, engines and spare parts, leaseholds and property.62 One day prior to the day set for hearing in the proceeding, the Board issued an order, the effect of which was to permit United, American and TWA direct non-stop privileges between Chicago and the Pacific coast.63 Interest in the transfer proceeding was manifested by the intervention of the Air Line Pilots Association, civic groups and the principal airlines operating in the area.

It appears from the opinion that after consummation of negotiations in March, 1947, and the signing of the agreement, United advanced to Western $1,000,000 which amount was to be assigned either to the purchase price or to commence bearing interest on September 1, 1947, depending upon the approval by the Board of the whole agreement. Additional terms of the agreement provided that United was to pay Western $3,750,000 for the Route 68 certificate and property valued variously from $1,700,000 to $2,200,000. After being taken

60 Western A. L., supra note 58, at 215.
61 The Board granted to Western a permanent certificate for Route 68, containing, however, the following provision couched in the language of Section 401(f) of the Act: "The exercise of the privileges granted by this certificate shall be subject to such reasonable terms, conditions, and limitations required by the public interest as may from time to time be prescribed by the Board." Western A. L., supra note 58, at 216.
62 United-Western, Acquisition Air Carrier Property, supra note 56; Notes, 48 Col. L. Rev. 89 (1948); 61 Harv. L. Rev. 523 (1948); 15 U. of Chi. L. Rev. 343 (1948).
63 TWA, et al., Route Consolidations, 8 CAB 28 (1947).
over by United, the certificate would be amended to contain a restriction against transportation of any traffic between Las Vegas, Nevada, and Los Angeles.

It developed during the proceeding that Western was in bad financial straits, brought on in part by the fact that it had had to purchase for use on Route 68 four-engined equipment that it did not need elsewhere, that even though Western had made a profit on the route during the previous year, in the future, it would not, since United had non-stop privileges from the East to Los Angeles. By carrying on direct, arms-length, personal negotiations from the outset, the contracting parties avoided a pitfall noted in the *First Marquette* case.

The presidents of the respective airlines emphasized that they were voluntarily taking constructive steps to arrange the domestic route pattern into a "more sensible system." The applicants urged that the route be transferred for the following reasons:

1. Route 68 was fundamentally a segment of United's transcontinental route.
2. That it is in the public interest to encourage voluntary and cooperative route adjustments by air carriers.
3. That Route 68 cannot support two services.
4. That Western would benefit financially.
5. That the transfer would not create a monopoly, restrain competition or jeopardize another carrier.

Public Counsel argued that the transaction should be disapproved for these reasons:

1. Applicants have taken on themselves a function of the Board in remaking the airline route map.
2. Approval of this agreement would encourage similar actions.
3. Western seeks to profit by what it now contends to be a mistake of the Board.
4. If the proposed sale should be approved the following harmful results would occur:
   a. Criterion would be established for selection of carriers based on ability to out-bid competitors rather than fitness and ability.
   b. Peddling of certificates would be encouraged.
   c. United would be required to expend funds for a certificate which in the public interest it should have been awarded in the first place.

In considering the facts of the case the Board said:

"Adjudication of this issue is a balancing process with no single factor controlling the determination . . . ."  
"In considering acquisitions of control and transfers of routes, the Board has ever borne in mind the fact that the air map of the
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country can be changed as drastically by such transactions as by obtaining certificates of public convenience and necessity and, where such transactions might result in destroying a balanced route system, approval of the proposal has been withheld... This transaction, as all such proposals, must be examined to determine whether it will facilitate an economically sound and efficient operation and at the same time satisfy the standard of public convenience and necessity. To serve this purpose it is necessary that the route to be transferred should bear an integrated relation to United's system and be adapted to its normal flow of air traffic."

Since the Board had previously found the route to be an integrated part of United's system and since the economic reasons for awarding the route to Western instead of United had been neutralized by United's non-stop privileges to Los Angeles, the Board found acquisition on the basis of route pattern to be in the public interest. In addition, the Board did not think it was necessary to place a condition in the agreement that all Western personnel must be retained, since the President of Western had testified that all personnel would be used on other Western routes.

The Board then turned to what it considered to be the principal issue in the case, namely the approval of the acquisition price. Here the Board recognized that approximately $1,500,000 was for "intangibles." The Board cited the distinction between "rate base value" and "acquisition value" made in other public utility fields and stated that so long as value for intangibles could be insulated from rate base value, the acquisition should be approved. The Board noted that the ICC had approved acquisitions where value of intangibles had exceeded by four or five times the value of the physical property transferred. Since the purchase price had been honestly arrived at by direct negotiations of the presidents of the respective airlines, the Board found "no justification for a decision which would outlaw the profit incentive from business transactions like that before us." The Board concluded its opinion by stating:

"The essence of the rule to which we adhere in the present case is that in transactions involving the transfer of air carrier property the effect of price upon the public interest must be determined by the facts of the particular case. No inflexible rule outlawing intangibles from exchange price can act as a substitute for sound judgment based upon careful analysis of the evidence of record of the particular case. The Board in such cases cannot consistently and should not renounce its responsibility and duty to undertake such a judgment by proclaiming a doctrine which would be, in effect, a le-

66 Ibid.
67 It can only be presumed that airline-interveners lost interest in the proceeding once non-stop privileges to the West Coast had been granted to TWA, American, and United, note 63 supra.
68 United-Western, supra note 56, at 311. This aspect of the case is still unsettled. By Order Serial E-1894, the Board on Aug. 25, 1948 reopened the case to have further hearing on the rights of Western employees allegedly adversely affected by transfer of Route 68.
69 United-Western, supra note 56, at 323.
gal presumption that any exchange price in excess of the prudent investment in the tangible assets being sold is regardless of the facts and circumstances of the case, per se adverse to the public interest.

"The Board will, in the future as in the past, scrutinize with care the prices agreed upon in such transfers to be certain that they are not unreasonable in terms of sound commercial values, and that they will not have a detrimental effect upon the air carriers involved or in any other way adversely affect the public interest. Our established policy to exclude from rates any element of intangible value which may appear in the prices agreed upon in any such transactions and our determination to disapprove transactions involving excessive and unreasonable prices are certain to act as deterrents to the negotiation of such prices." 70

A majority of the Board approved the transfer and acquisition as being consistent with the public interest, subject to the condition that the investment value for rate making purposes of the properties acquired should remain the same on United's books and that the sum of $2,106,209 representing the excess of purchase price over investment value for rate-making be charged to surplus.71 The majority opinion carried an appendix containing cases stating the position of the ICC and the Federal Power Commission with respect to prices in acquisitions. Thus, the Board, affirming the decision of the Second Marquette case, established what might be called an arms-length-bargaining, reasonable commercial value test for approving valuation of a certificate for transfer purposes.

Chairman Landis dissented. He felt that for two reasons the majority doctrine was deleterious to the public interest in developing air transportation. First, there could never be a voluntary realignment of the airline route pattern through acquisition or merger because of the high cost placed upon such transactions by the majority, and second, the opinion was an "open-sesame" to false valuations which would eventually lead to disastrous inflation in an industry which to date had been kept financially sound. Mr. Landis noted the difficulties that the ICC met in dealing with valuation and stated that the CAB had an ideal opportunity to prevent market speculation upon the inefficiency of government to regulate fair return. He then analyzed the valuation of each item to be transferred and whereas the majority glibly assessed to intangibles, without defining the term, the amount of purchase price

70 Id. at 324.
71 The Board was properly embarrassed when it discovered that United did not have an earned surplus sufficient to cover the intangibles. In Order Serial E-786, Sept. 10, 1947, the Board modified its earlier order to permit United to charge off the intangibles to surplus over a 5 year period. United carries on its books as an asset $2,106,209 noted as follows: "Excess of purchase price of Denver-Los Angeles route and related properties over original cost less depreciation, being amortized (By condition attached to Civil Aeronautics Board approval of the purchase by United of the Denver-Los Angeles route—No. 68—and by stipulation filed with the Board by United, this item may not be claimed as investment for rate-making purposes)." Annual Report to Stockholders 1947, United Airlines Inc.
over valuation of equipment transferred, he enumerated and evaluated the factors which could be considered intangibles. "Going concern" or "goodwill" value, in his opinion, merely represented the ability of a business to earn more than a fair return and to allow such a value to find its way into the rate base of an industry so closely regulated as air transportation would be to pyramid against the public the government's ineffectiveness and failure to limit earnings to a fair return.

Concerning "franchise value," Mr. Landis said that the decision in the Second Marquette case should be overruled as, in his opinion, a certificate was a privilege held in trust from the government and to permit the certificate to be sold at a price was "literally sinful." Market value, to his way of thinking, was merely another manifestation of the ineffectiveness of government regulation, since it too represented the ability of the utility to earn more than a fair return. Mr. Landis felt that it was impossible by the mere use of a bookkeeping process to quarantine these intangible values from finding their way into an inflated rate-base valuation. In addition, he pointed out that the inconsistency of the Board's position in approving, as a prudent move by management, a valuation which later in a rate proceeding must be excluded from the rate base as not being a prudent investment.

Not all of Chairman Landis' opinion concerns a criticism of the majority opinion. He specifically sets forth his formula, based upon the use of air mail subsidy, for realigning the airline route pattern:

"The doctrine I advocate would relate allowable sales and purchase prices to a criterion of investment and would furnish standards against which the efficiency and economy of management could be measured and subsidy granted or denied management dependent upon its conformance to these standards. For with such a standard in existence the unwillingness of management to dispose of an uneconomic route at a price that is fair because it is bottomed on investment would be the basis of a charge of lack of economy that would justify reduction in subsidy. In this way government could both correct the inertia of management and restrain its greed."

Mr. Landis noted the necessity for reordering the route pattern to utilize new equipment and further stated that Western in this proceeding had suggested a method by which this might be done in a practical manner consistent with the public interest.

"Western intimated that in the event the sale of Route 68 was approved, Inland would prove to be of little value to its system and Western would therefore place Inland on the block before the Board to be disposed of to such purchasers and at such prices as the Board might deem best. This was an eminently wise, just and practical

72 United-Western, supra note 56 at 342 (Landis, Chairman, dissenting). In Mr. Landis' mind, the stumbling block to such action was price: 'Would-be acquirers hesitate to pay the inflated prices that are asked for fear that they will not of a certainty pass that inflation on to the public.' And meanwhile the administration of subsidy upholds the hands of potential sellers in their inflationary demands. And inaction results."
approach. But such an approval naturally follows when by holding price to investment, competition in terms of price is eliminated between potential buyers. The sole criterion remaining is then that of the public interest in the most efficient integration of the airlines.\textsuperscript{73}

Thus, while the Chairman criticized the majority opinion because of its abandonment of the ideal theory of government control of the air transportation system, he offered concrete and practical suggestions as to how this ideal might be reached. The rationale of the Lee and Warner dissents are effectively combined in the Landis opinion.\textsuperscript{74}

There are several aspects of the majority opinion which would seem to warrant discussion. One cannot help but feel that because of the terms of the agreement, the financial position of Western, and the absence of an earned surplus to which United could write off the intangibles, the Board arrived at its decision without sufficient consideration of all the facts. Had the full consequences of approval been reasoned through the holding might have been different. One is further impressed by the fact that the majority seems to ignore its promotional responsibilities and prefers to sit as a mere judge of valuation. As pointed out in the dissent, the practice fostered by the majority of permitting transfer value to be determined by arms-length bargaining of experienced capable men familiar with the industry, would seem to have no bounds. The majority's view that the mere exclusion of franchise value from the rate base value will be a sufficient deterrent to the inflationary valuation of the commercial value of a certificate would seem to be most optimistic and lacking in realism. There was complete unanimity as to what the correct rate-base value should be, but the main point of dissention was over the question of whether or not the value of intangibles could be effectively insulated from this base by a mere bookkeeping process. The result of future proceedings concerning rates and mail pay and the dividend record of United stock should indicate which position was correct.\textsuperscript{75}

Since United was to operate over the route in its own name using its own equipment and personnel, it is difficult to see how the route could be said to have going concern value. Furthermore, since the route by virtue of its connection with United made money for Western from the outset, any goodwill which the route may have enjoyed was the result of its being an integral part of United's system, and not Western's. In addition, if one were to allocate goodwill and going concern value to Western's entire system in proportion to that here allocated by

\textsuperscript{73} Id. at 343.

\textsuperscript{74} Mr. Lee objected to the Board's failure to devise an integrated route pattern in its approval of transfer applications, note 39 \textit{supra}. Mr. Warner pointed out that by placing a value on a certificate, the Board was imposing a direct burden on the public either through air mail payments or commercial charges which would permit the purchaser to recoup certificate cost, note 32 \textit{supra}.

\textsuperscript{75} $2,500,000 was transferred from depreciation reserve for retirement of C-54 type airiraft to surplus by United at the end of 1947. \textit{Annual Report to Stockholders 1947}, United Airlines Inc.
the majority to Route 68, Western would enjoy a goodwill or going concern value of roughly $5-6,000,000. This is a rather startling figure in view of the fact that Western's president testified in this proceeding that Western was on the verge of bankruptcy. Why United should pay for something, which, if it exists at all, is the result of United's own efforts, does not seem to be either reasonable, ethical or logical. It would therefore seem to be apparent that even though certain leases and materiel were included in the transfer, the only intangible value transferred must be allocated to the naked certificate. But if this is admitted, an anomaly is created by the fact that the Board, before touching upon the question of valuation, found that acquisition by United was in the public interest. It will be remembered that Western's original certificate was "subject to such reasonable terms, conditions, and limitations required by the public interest as may from time to time be prescribed by the Board." Since Section 2 of the Act sets forth the magic equation which uniformly defines the term "public interest," it is difficult to see how the Board could permit Western to place a value on a condition to its own certificate. 7

(To be continued)

7 In its most recent acquisition and transfer decision the Board seems to belabor the question of valuation of certificates for transfer purposes, Acquisition of Petersburg Air Service by Alaska Island Air., 8 CAB ..., (Serial E-1136, Dec. 31, 1947). The holdings in future acquisition cases will determine whether this decision was the beginning of a policy trend away from the United-Western formula toward a valuation policy founded upon its earlier decisions or was merely another stage in policy vacillation.