

KIRKLAND ALERT

November 2013

The DOJ Settles Airline Challenge, Clears Path for AMR/US Airways Merger

On November 12, 2013, the U.S. Department of Justice announced a proposed settlement of its challenge to the US Airways/American Airlines merger. The settlement, which requires extensive divestitures, clears the way for the carriers to close the \$11 billion deal they announced on February 14, 2013. Consummation of this deal brings to a close a period of significant industry consolidation that has reduced the number of major U.S. airlines from nine to five since 2008. Although some of these other transactions required remedies, the scope of the proposed settlement is far larger. Specifically, the merging parties have agreed to divest 104 takeoff/landing slots at Washington's Reagan National Airport, 34 takeoff/landing slots at New York's LaGuardia Airport, and airport assets at Boston's Logan Airport, Dallas's Love Field, and American's hubs at LAX, O'Hare, and Miami.

The extensive nature of the settlement is not surprising, given the dire picture of consumer harm that the DOJ painted in its complaint. The challenge to the merger filed by the DOJ on August 13, 2013, identified three potential sources of consumer harm: increased concentration in slot holdings at Reagan National, diminished competition on roughly 1,000 routes currently served by both merging parties, and an increased likelihood of tacit coordination among the remaining three legacy carriers following the elimination of pricing maverick US Airways. The complaint gave short shrift to the competitive significance of low-cost carriers like Southwest and JetBlue, and portrayed previous airline deals (including Delta/Northwest and United/Continental) as failing to deliver on promised benefits.

Given the emphasis of the DOJ complaint on slot concentration at Reagan National, remedies at that airport have been widely viewed as necessary (but not sufficient) to resolve the various competitive concerns raised by the transaction. The required Reagan divestitures are significant and exceed the 68 Reagan slots that US Airways acquired from Delta in 2011. Note, though, that although the slot and gate divestitures at Reagan may resolve concerns on some of the affected routes, without commitments from the acquirers of the slots and gates to fly to the many affected cities, it is unlikely that the new owners will use those assets to replicate the competition otherwise lost between American and US Airways.

The other divestitures in the settlement package are not as clearly tied to the remaining harms alleged in the DOJ complaint. For example, although the settlement requires the divestiture of LaGuardia slots, the DOJ did not identify LaGuardia as an airport of concern in its complaint (although New York City routes were flagged as issues). Moreover, the harm the DOJ sought to address with the Miami divestiture is unclear; even the DOJ acknowledged in its Competitive Impact Statement that access to Miami's facilities is not currently constrained. Finally, some of the slots being divested by US Airways and American are already leased to and used by Southwest and JetBlue, not the merging carriers. Nearly a third of the divested LaGuardia slots, for example, are currently leased to Southwest.

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Given the mismatch between harms alleged and remedies extracted, it is clear that the DOJ chose to exercise its prosecutorial discretion to permit the balancing of competitive harms in some markets against increased competition in others. At bottom, the settlement creates relatively small benefits designed to offset the arguably small costs the merger would have imposed on consumers.

The DOJ had been under significant pressure in recent weeks to settle its challenge to the merger, as evidenced by Attorney General Holder's public acknowledgement last week regarding the possibility of a settlement. One of the states that originally joined the DOJ in challenging the merger, Texas, withdrew from the suit following Texas-specific commitments by the merging parties, and the Oklahoma Attorney General announced his intent to intervene in the suit on behalf of the airlines. Members of Congress, labor unions and local politicians also supported the merger and pushed the DOJ to drop the suit.

The settlement remains subject to court approval under the Tunney Act. The court must find that the settlement is in the public interest. The public will be permitted to comment on the proposed settlement as part of the court's review; even in the face of significant opposition, though, it would be quite unusual for the court to overturn the settlement. The airlines may close the transaction while the Tunney Act process is ongoing.

Although the settlement resolves the DOJ suit, the airlines still face a private suit by airline passengers seeking to block the merger. This suit, which was stayed during the pendency of the DOJ's challenge, is likely to be revived. The same attorney (Joe Alioto) seeking to block the proposed US Airways/American Airlines merger also filed suit challenging the mergers of Delta and Northwest, United and Continental, and Southwest and AirTran. Delta and Northwest settled their suit. United and Continental proceeded to trial and prevailed. The challenge to Southwest/AirTran was filed following consummation of the merger; the U.S. Court of Appeals for the Ninth Circuit subsequently sanctioned Alioto for filing the suit. It is unlikely that Alioto will be dissuaded by the settlement with the DOJ, as he pursued private challenges to InBev's acquisitions of Anheuser-Busch and Modelo following the DOJ settlements with the parties in both instances. The current suit, like its predecessors, is weak; depending upon the time available to them, the merging carriers may choose either to settle the suit for nuisance value or proceed to trial, which defendants almost certainly will win.

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