

2014

Searching for the Sweet Spot: An Analysis of the American-US Airways Merger

Mathew Drocton

Follow this and additional works at: <https://scholarlycommons.law.case.edu/caselrev>

 Part of the [Law Commons](#)

Recommended Citation

Mathew Drocton, *Searching for the Sweet Spot: An Analysis of the American-US Airways Merger*, 65 Case W. Rsrv. L. Rev. 487 (2014)

Available at: <https://scholarlycommons.law.case.edu/caselrev/vol65/iss2/9>

This Comments is brought to you for free and open access by the Student Journals at Case Western Reserve University School of Law Scholarly Commons. It has been accepted for inclusion in Case Western Reserve Law Review by an authorized administrator of Case Western Reserve University School of Law Scholarly Commons.

— Comment —

SEARCHING FOR THE SWEET SPOT:
AN ANALYSIS OF THE AMERICAN—
US AIRWAYS MERGER

CONTENTS

INTRODUCTION 487

I. EXPECT DELAYS: THE DOJ COMPLAINT 489

A. Increased Concentration 490

B. Coordinated Behavior 491

C. Elimination of Competition 494

D. Procompetitive Effects 494

II. CLEARED FOR TAKE-OFF: THE SETTLEMENT 495

A. Previous Mergers 495

B. Current Settlement 497

III. POSSIBLE TURBULENCE: AN ANALYSIS OF THE SETTLEMENT 500

A. Adequacy of the Settlement 500

B. Impact on Market Efficiency 503

CONCLUSION 504

INTRODUCTION

After the passage of the Airline Deregulation Act of 1978,¹ the airline market moved toward consolidation with the Department of Justice remaining relatively taciturn.² Since the deregulation, there

-
1. Airline Deregulation Act of 1978, Pub. L. No. 95-504 (codified at 49 U.S.C. § 40101 (2012)).
 2. *But see*, Press Release, Dep’t of Justice, Department of Justice and Several States Will Sue to Stop United Airlines from Acquiring US Airways (Jul. 27, 2001), http://www.justice.gov/atr/public/press_releases/2001/8701.pdf (moving to block the proposed US Airways and United merger because “[t]he proposal did not assure competition for those adversely affected by the acquisition, such as passengers in east coast connect markets, and instead substituted regulation for competition on some key routes and created competitive harms through United’s and American’s agreement to jointly fly and price the New York, Washington and Boston shuttle routes”) (quoting R. Hewitt Pate, Deputy Assistant Attorney General for the Department of Justice).

have been more than 160 airline bankruptcies³ and approximately \$15 billion in operative losses over the past decade.⁴

Following the consummation of the United-Continental merger in 2010, US Airways expressed interest in securing a merger of its own.⁵ On November 29, 2011, American Airlines and its parent, AMR Corporation, filed for bankruptcy.⁶ American's bankruptcy filing came after years of financial struggles ending with a \$1.06 billion loss during the 2011 fiscal year.⁷ American sought a merger with US Airways to escape bankruptcy and regain profitability. The two airlines agreed to a stock swap valued at \$18 billion.⁸ Citing concerns of market enervation, the DOJ initially moved to block the prospective American-US Airways amalgamation.⁹ The newly formed airline would utilize American's brand while operating under US Airways' management. Critics argued that the DOJ's suit illustrated disparate treatment with regard to prior airline mergers and possibly signified a new antitrust policy.¹⁰

The Airline Deregulation Act seemingly left the airline industry in a state of economic turmoil. The DOJ, primarily concerned with competition and consumer protection, now faces the additional task of market preservation, which inadvertently factors into their antitrust calculus. In order to achieve economies of scale in the current climate, market consolidation is arguably a necessary evil. If an airline fails, the market suffers loss of competition with an already concentrated market. Alas, the DOJ is left with the task of reaching a sustainable level of profitability for airlines while maintaining competition.

-
3. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-10-778T, AIRLINE MERGERS: ISSUES RAISED BY THE PROPOSED MERGER OF UNITED AND CONTINENTAL AIRLINES 4-5 (2010) ("While most of these bankruptcies affected small airlines that were eventually liquidated, 4 of the more recent bankruptcies (Delta, Northwest, United, and US Airways) are among the largest corporate bankruptcies ever . . .").
 4. *Id.*
 5. See Holman W. Jenkins Jr., *Airlines vs. History*, WALL ST. J., May 5, 2010, at A19 ("We didn't need seven of them in 2005. We don't need four of them now. We need three.") (quoting US Airways' Doug Parker).
 6. *In re AMR Corp.*, 477 B.R. 384, 401 (Bankr. S.D.N.Y. 2012).
 7. *Id.* at 397.
 8. Susan Carey, *Fixing a "Fragile" Air Merger: US Airways CEO Kept the Faith During Antitrust Suit; New Challenges Await*, WALL ST. J., Dec. 2, 2013, at B1.
 9. See Complaint, United States v. US Airways Grp., Inc., No. 1:13-cv-01236, (D.D.C. Aug. 13, 2013) [hereinafter *Complaint*].
 10. See, e.g., James B. Stewart, *A Merger Too Far for U.S. and Airlines*, N.Y. TIMES, Aug. 17, 2013, at B1 ("The government 'abandoned the framework it used in approving the last three airline mergers,' said Paul T. Denis, a partner at Dechert L.L.P. . . .").

This Comment analyzes the approval of the American–US Airways merger and the economic impact on the airline industry. While many believe the DOJ’s treatment of the merger signals a shift in policy, this Comment will posit that the agency’s response is consistent with past practice. In fact, this Comment will suggest that the requirements the DOJ has imposed arguably do not do enough to remedy the potential anticompetitive issues produced by the combination. Part I outlines the complaints filed by the DOJ and explores the anticompetition concerns raised. Using the merger guideline’s framework, Part I discusses the alleged effects of the merger, as argued in the DOJ complaint. The already concentrated market conflated with the sizeable competition provided by two of the largest airlines proves the DOJ’s concerns to be legitimate.

Part II details the litigation surrounding the prospective merger and explores the antitrust settlement. Comparing recent approved airline mergers, Part II argues that the settlement did not depart in any meaningful way from previous antitrust policy in the airline industry. The American–US Airways merger posed greater anticompetition concerns than prior mergers causing the lawsuit. Ultimately, the economics and trial uncertainty resulted in larger scale divestments instead of an attempt to block the merger.

Part III analyzes the sufficiency of the settlement in light of the original issues raised in the DOJ complaint and discusses the impact on the airline market. By considering the economic implications of the divestitures and the competition generated by Low Cost Carriers (LCCs), Part III calls into doubt the settlement’s ability to redress the original anticompetition concerns. Additionally, the economic impact on the market appears to be a net positive, as it addresses the faltering profitability of the airlines.

I. EXPECT DELAYS: THE DOJ COMPLAINT

In evaluating a proposed merger, the DOJ defines the market; calculates the market concentration; considers the unilateral effects, such as elimination of competition; and lastly contemplates potential coordinated behavior.¹¹ Next, the DOJ balances the anticompetitive effects against possible procompetitive effects.¹² Following the DOJ’s examination, Bill Baer, head of the Antitrust Division at the DOJ made the position of the agency perfectly clear when he stated that “[w]e think the right solution here is a full-stop injunction.”¹³ At first glance,

11. U.S. DEP’T OF JUSTICE & FED. TRADE COMM’N, HORIZONTAL MERGER GUIDELINES §§ 4–7 (2010) [hereinafter *2010 Merger Guidelines*].

12. *Id.* at § 10.

13. David Ingram & Karen Jacobs, *U.S. Sues to Block AMR-US Airways Merger; Stocks Fall*, REUTERS, Aug. 13, 2013, <http://www.reuters.com/>

a DOJ suit to block the American–US Airways merger appears to be a stark change with regard to past antitrust policy.¹⁴

The State filed suit to block the American–US Airways deal, claiming the merger violated Section 7 of the Clayton Act.¹⁵ The DOJ complaint relied upon the three anticompetitive effects penned in the Merger Guidelines: (1) increased competition, (2) increased coordinated behavior, and (3) elimination of head-to-head competition.¹⁶

A. Increased Concentration

Looking to individual markets, the American–US Airways merger would cause a significant increase in market concentrations. When evaluating the effects on market concentration, the DOJ often calculates the Herfindahl-Hirschman Index (“HHI”) of market concentration by summing the squares of each firm’s market share.¹⁷ Generally, unconcentrated markets contain an HHI below 1,500, moderately concentrated markets contain an HHI between 1,500 and 2,500, and highly concentrated markets contain an HHI above 2,500.¹⁸ Additionally, if a merger creates a highly concentrated market and “involve[s] an increase in the HHI of more than 200 points[, the merger] will be presumed to be likely to enhance market power.”¹⁹ A post-merger American–US Airways would result in 1,000 city pairs, exceeding a 2,500-point HHI while also increasing the HHI by more than 200 points.²⁰ Also, of particular importance, the market would consist primarily of three legacies, the major airlines with interstate routes prior to the Deregulation Act of 1978 and the competitive Low Cost Carrier (“LCC”) Southwest.²¹ The post-merger result would be

article/2013/08/13/us-amr-usairways-lawsuit-idUSBRE97C0JF20130813.

14. Stewart, *supra* note 10, at B1.
15. *Complaint*, *supra* note 9, at 7. Section 7 of the Clayton Act outlaws acquisitions that substantially lessen competition or tend to create a monopoly. 15 U.S.C. § 18 (2012).
16. *Complaint*, *supra* note 9, at 12–32.
17. *2010 Merger Guidelines*, *supra* note 11, at § 5.3.
18. *Id.*
19. *Id.* If such a presumption is created, “[t]he presumption may be rebutted by persuasive evidence showing that the merger is unlikely to enhance market power.” *Id.*
20. Amended Complaint at 14, United States v. US Airways Grp., Inc., No. 1:13-cv-01236 (D.D.C. Sept. 5, 2013) [hereinafter *Amended Complaint*].
21. See Competition and Bankruptcy in the Airline Industry: The Proposed Merger of American Airlines and US Airways: Hearing Before the H. Comm. on the Judiciary, 113th Cong. 107 (2013) [hereinafter *Airline Hearings*] (statement of Christopher L. Sagers, James A. Thomas Distinguished Professor of Law, Cleveland State University) (“American

four airline carriers with control over 80 percent of the domestic airline market.²² Ultimately, the airline industry currently operates at abnormally high concentration throughout various markets, and if HHI receives credence, the merger will cause anticompetitive effects. However, market share statistics are not conclusive but merely a factor to be considered.²³

B. Coordinated Behavior

The oligopolistic nature and readily transparent pricing in the deregulation era of the airline industry makes coordinated pricing and decreased service relatively simple to implement. Coordinating behavior for an industry dominated by five firms is perhaps not as disconcerting as an industry dominated by four firms. The DOJ pointed to four post-merger results that would increase coordinated behavior: (1) elimination of US Airways' Advantage Fares program, (2) increased capacity discipline, (3) elimination of American's expansion plans, and (4) increased fares.²⁴

US Airways plays a pivotal role in airline competition through its Advantage Fares program, which offers discounted one-stop fares that compete with nonstop fares.²⁵ Because US Airways would no longer be competing with American, the DOJ expressed concern that the merger would eliminate, or significantly curtail, US Airways' Advantage Fare program and, in turn, eliminate important competitive effects.²⁶ The merger, in theory, would put an end to the one-stop discounted rate offered by US Airways.

The DOJ additionally cited concerns that a post-merger market would increase the practice of capacity discipline. Use of capacity discipline—intentionally keeping a lower capacity growth in order to increase returns—has become ubiquitous among legacies in order to regain profitability in times of rising fuel prices and a depressed

/U.S. Airways deal would leave the sector with only four major players: United, Delta, American and Southwest. Nationally, those four firms will hold more than 70% of airline travel.”).

22. Ingram & Jacobs, *supra* note 13.
23. *See* Brown Shoe Co., Inc. v. United States, 370 U.S. 294, 322, n.38 (1962) (“Statistics reflecting the shares of the market controlled by the industry leaders and the parties to the merger are, of course, the primary index of market power; but only a further examination of the particular market—its structure, history and probable future—can provide the appropriate setting for judging the probable anticompetitive effect of the merger.”).
24. *See Complaint*, *supra* note 9, at 15–30.
25. *See Amended Complaint*, *supra* note 20, at 18 (stating that US Airways' one-stop flights are “up to 40% cheaper than other airlines' nonstop service”).
26. *Id.* at 18–23.

economy.²⁷ Industry consolidation allows for greater use, or perhaps abuse, of capacity discipline. Industry trends prove an increase in limiting service through this practice.²⁸ Noting the economic benefits, the DOJ ultimately expressed disdain for the decline in flights and resulting increase in fares.²⁹ Airline executives, including the president of US Airways, have stated the important effects of capacity discipline and show no signs of cutting this practice.³⁰ Giving more force to the DOJ's argument, post-merger United "reduced capacity at nearly all of its major hubs (including Cleveland) and at many other airports where the two airlines previously competed."³¹ Perhaps the most important effect of capacity discipline by an American-US Airways merger would

-
27. See MICHAEL D. WITTMAN, AN ASSESSMENT OF AIR SERVICE ACCESSIBILITY IN U.S. METROPOLITAN REGIONS, 2007–2012, AT 17 (2014), available at <http://hdl.handle.net/1721.1/87063> ("[T]he number of flights at most U.S. airports decreased from 2007 [to] 2012 as airlines reconfigured their networks and practiced 'capacity discipline' in the face of high fuel prices and a recessed economy . . ."); see also MICHAEL D. WITTMAN & WILLIAM S. SWELBAR, TRENDS AND MARKET FORCES SHAPING SMALL COMMUNITY AIR SERVICE IN THE UNITED STATES (2013), available at <http://hdl.handle.net/1721.1/87064> ("Instead of operating as many flights as possible in an attempt to gain market share, large airlines began a more efficient capacity and network management paradigm in an attempt to reduce operating costs by removing redundant flying and rationalizing service at some smaller hubs.").
28. See Chris Tarry, *ANALYSIS: Capacity discipline still necessary despite rosier economic outlook*, Airline Business (May 2, 2014) ("In terms of regional variation, the capacity discipline evident among the North American airlines seems to be continuing. Within the North American domestic market, capacity in 2014 is expected to be just 2% higher than in 2013, following a 2.2% increase last year."), available at <http://www.flightglobal.com/news/articles/analysis-capacity-discipline-still-necessary-despite-rosier-economic-398254/>.
29. *Amended Complaint*, *supra* note 20, at 23–26.
30. See, e.g., Press Release, Delta Air Lines, Delta Air Lines Announces September Quarter Profit (Oct. 25, 2011) <http://news.delta.com/index.php?s=20295&item=123808> ("With continued capacity discipline, coupled with improvements we are making in our product and service, we are well positioned to deal with the impact of today's high fuel prices and an uncertain economy.") (quoting Delta's President Ed Bastian); Jay Boehmer, *Carriers Continue to Make the Most of Capacity Control*, BUS. TRAVEL NEWS, June 28, 2010, at 19 ("One of the most important things that happened in the industry is capacity discipline," US Airways president Scott Kirby said. "In 2009, you saw all airlines reduce capacity, following the spike in fuel and the bad revenue environment. What was unique about 2008 and 2009 capacity is that not only the legacy carriers reduced capacity, but for the first time in history of the industry the low-cost carriers by and large reduced capacity . . .").
31. *Amended Complaint*, *supra* note 20, at 25.

be a resulting decline in connectivity.³² A more concentrated market would increase coordinated efforts to reduce seating and services in order to increase profitability.

American's original bankruptcy plan consisted of firm growth and expansion, which the DOJ believed would end if the merger goes through. American submitted a plan that consisted of concentrating on their five key hubs by "[e]xpanding American international presence," utilizing "codesharing," "implementing a long-term fleet plan, creating a capital structure that allows American to grow," and "setting up a sustainable cost structure."³³ The complaint argued that with the merger, American would likely abandon their previous plan to increase flights.³⁴ Eliminating overlapping routes, in part, makes the airline mergers financially advantageous. US Airways executives argued that the combined networks would create additional connecting routes and ultimately expand service.³⁵ A merger between American and US Airways would undercut the incentive and need for American's expansion.

The price fixing paradigm generally accepts that fewer firms in a market increases the ease in which prices can be coordinated. The complaint cited recent examples of coordinated pricing that persist at current concentration levels.³⁶ Given the close nature and transparency

-
32. See, e.g., WITTMAN, *supra* note 27, at 19 ("Very large regions of over 5 million residents saw their average Air Service Accessibility Index score decrease by 10.2% from 2007 [to] 2012. While this is a significant decline, it is less than the average decline of 11.6% for all regions [over] the same period. Medium-sized regions with populations of 0.5 million—5 million felt the biggest brunt of the decline in service at medium-sized U.S. airports. These regions lost about 14.3% of their air service accessibility, on average, from 2007 [to] 2012."); see also WITTMAN & SWELBAR, *supra* note 27, at 3 ("Instead of operating as many flights as possible in an attempt to gain market share, large airlines began a more efficient capacity and network management paradigm in an attempt to reduce operating costs by removing redundant flying and rationalizing service at some smaller hubs.").
33. *In re AMR Corp.*, 477 B.R. 384, 402 (Bankr. S.D.N.Y. 2012).
34. *Amended Complaint*, *supra* note 20, at 26.
35. *Airline Hearings*, *supra* note 21, at 35 (statement of Stephen L. Johnson, Executive Vice President, Corporate and Government Affairs of US Airways, Inc.) ("To illustrate the effect of the superior combined network, even if you focus only on airports with more than 50 departures per week, the merger will create over 1,300 new online connecting routes benefiting millions of passengers.").
36. See, e.g., *Amended Complaint*, *supra* note 20, at 27 ("American announced that it would charge for a first checked bag on May 21, 2008. On June 12, 2008, both United and US Airways followed American's lead. Similarly, over a period of just two weeks this spring, all four legacy airlines increased their ticket change fee for domestic travel from \$150 to \$200.").

of current airline practices, high levels of coordinated pricing and business schemes already exist, and it seems inconclusive whether one less legacy can aggravate the current conditions.

C. Elimination of Competition

The new American would dethrone Delta as the largest domestic airline carrier, raising concerns of a likely decrease in competition. Pre-merger American and US Airways competed against each other, with nonstop service on seventeen routes domestically.³⁷ Arguably, a generally undifferentiated product, such as airline travel, exacerbates this concern.³⁸ Indeed, LCCs, with the exception of Southwest, cannot provide the necessary competition to the legacy dominated market.³⁹ The complaint particularly singled out Reagan National, noting that the combined airline would possess 69 percent of the slots.⁴⁰ Moreover, American would no longer be competing at Reagan National against US Airways' already dominant presence. For these reasons, elimination of a legacy post-merger undercuts significant competition in the market.

D. Procompetitive Effects

The DOJ alleged an absence of procompetitive effects regarding the prospective merger.⁴¹ It may, however, be axiomatic that a DOJ complaint seeking to prevent a merger would not contain propitious effects of the proposed transaction. Specifically, the complaint states that the merger would not result in expansion and the new airline would participate in coordinating conduct.⁴²

37. *Amended Complaint*, *supra* note 20, at 30.

38. *See 2010 Merger Guidelines*, *supra* note 11, at § 6.3 (“In markets involving relatively undifferentiated products, the Agencies may evaluate whether the merged firm will find it profitable unilaterally to suppress output and elevate the market price. A firm may leave capacity idle, refrain from building or obtaining capacity that would have been obtained absent the merger, or eliminate pre-existing production capabilities.”).

39. *See Airline Hearings*, *supra* note 21, at 109 (statement of Christopher L. Sagers, James A. Thomas Distinguished Professor of Law Cleveland State University) (“While there are a few remaining LCCs that have some wherewithal to compete, the only LCC whose entry has ever persistently driven down fares in city-pair markets is Southwest, and Southwest has now achieved a nationwide presence of its own and its costs are believed to have risen as well.”).

40. *Amended Complaint*, *supra* note 20, at 30.

41. *Complaint*, *supra* note 9, at 6–7.

42. *Amended Complaint*, *supra* note 20, at 33.

II. CLEARED FOR TAKE-OFF: THE SETTLEMENT

A. Previous Mergers

The Delta-Northwest merger in 2008 and the United Airlines–Continental merger in 2010 provide the most relevant examples of the DOJ’s current antitrust policy in the airline industry. Delta acquired Northwest in a \$2.6 billion deal that crowned Delta the largest airline at the time.⁴³ The DOJ closed its investigation of the Delta-Northwest merger by issuing a statement highlighting the anticipated efficiencies and procompetitive effects.⁴⁴ The DOJ chose not to implement any remedial measures and approved the merger. The effects of the merger, however, paint a contrary picture. All other things held constant, the merger caused the total passengers in 2009 to decline by 5.3 percent⁴⁵ compared to the 3.5 percent decline the prior year.⁴⁶ Additionally, Delta’s Cincinnati hub saw a 50 percent decline in passengers between 2005 and 2009.⁴⁷ The elimination of Northwest as a separate competitor equated roughly to a 5.1 percent increase in fare price, at least in the short run.⁴⁸

-
43. John Crawley, *Delta Buys Northwest to Create Biggest Airline*, REUTERS (Oct. 30, 2008, 7:32 AM), <http://www.reuters.com/article/2008/10/30/us-delta-northwest-idUSTRE49S8BA20081030>.
 44. See Press Release, Dep’t of Justice, Statement of The Department of Justice’s Antitrust Division on Its Decision to Close Its Investigation of the Merger of Delta Air Lines Inc. and Northwest Airlines Corporation (Oct. 29, 2008), <http://www.justice.gov/opa/pr/2008/October/08-at-963.html> (“[T]he merger likely will result in efficiencies such as cost savings in airport operations, information technology, supply chain economics, and fleet optimization that will benefit consumers. Consumers are also likely to benefit from improved service made possible by combining under single ownership the complementary aspects of the airlines’ networks.”).
 45. Press Release, Dep’t of Transp., Summary 2009 Traffic Data for U.S and Foreign Airlines: Total Passengers Down 5.3 Percent from 2008 (March 29, 2010), http://www.rita.dot.gov/bts/sites/default/files/rita_archives/bts_press_releases/2010/bts015_10/pdf/bts015_10.pdf.
 46. Press Release, Dep’t of Transp., Summary 2008 Traffic Data for U.S and Foreign Airlines: Total Passengers Down 3.5 Percent from 2007 (Apr. 23, 2009), http://www.rita.dot.gov/bts/sites/default/files/rita_archives/bts_press_releases/2009/bts019_09/pdf/bts019_09.pdf.
 47. John W. Fischer & Michaela D. Platzer, *Airline Industry Mergers: Issues of Congressional Interest*, in AIRLINE INDUSTRY MERGERS: BACKGROUND AND ISSUES 1, 7 (Felix J. Mercado ed., 2011).
 48. See Dan Luo, *The Price Effects of the Delta/Northwest Airline Merger*, 44 REV. INDUS. ORG. 27, 45 (2013) (“Although . . . the regression coefficient of DL/NW overlap routes is insignificant in nonstop markets, the actual fares increased by 5.1%. There is a positive fare trend between the periods, but another reason for the positive price effect is that the merger appeared to cause exit by LCCs that provided nonstop service.”).

The United-Continental merger came on the heels of the DOJ's rejection of Continental's request for antitrust immunity to work with United, among other carriers, in setting prices and scheduling.⁴⁹ In a similar financial state as American, United and Continental faced significant losses in 2009.⁵⁰ Like the American-US Airways presence at Reagan National, United-Continental's resulting 60 percent control out of Newark gave the DOJ pause.⁵¹ Ultimately, the United-Continental investigation ended with the airlines agreeing to transfer slots at Continental's key hub, Newark, to Southwest.⁵² Satisfied with the remedial divestiture, the DOJ stated that the merger "will likely significantly benefit consumers on overlap routes as well as on many other routes."⁵³ For many observers, approval seemed inevitable because the airlines contained complimentary routes with minimal overlap.⁵⁴ The newly formed airline became the largest airline. The merger did not come without complications. The new airline hit turbulence with consumers, ranking worst for the number of consumer complaints, but that is an aside from the competition focus.⁵⁵

But cf. id. at 45 (finding that the change in overlap markets was close to zero). The results are based on the first quarter of 2008 (pre-merger) data and the second quarter of 2010 (post-merger) data. *Id.* at 30.

49. Dealbook, *D.O.J. Opposes Antitrust Immunity for Continental*, N.Y. TIMES (June 30, 2009, 6:05 AM), <http://dealbook.nytimes.com/2009/06/30/doj-opposes-antitrust-immunity-for-continental/>.
50. See Fischer & Platzer, *supra* note 47, at 7 ("[R]evenues were down 19.1% at United (losing \$651 million) and 17.4% at Continental (losing \$282 million) between 2008 and 2009.").
51. Julie Johnsson, *Antitrust Regulators OK United-Continental Deal*, CHI. TRIB., Aug. 28, 2010, at C8.
52. Press Release, Dep't of Justice, United Airlines and Continental Transfer Assets to Southwest Airlines in Response to Department of Justice's Antitrust Concerns (Aug. 27, 2010) [hereinafter *Continental-United Press Release*], <http://www.justice.gov/opa/pr/2010/August/10-at-974.html>.
53. *Id.*
54. See Justin Dickerson, *Antitrust in the Skies: The United and Olympic Airline Mergers*, 15 *TOURO INTL. L. REV.* 1, 8 (2012) ("Nonetheless, most industry experts also anticipated that United and Continental would face few antitrust objections. United and Continental separately shared no hubs, and were not in significant 'head-to-head' competition as horizontal competitors on many routes domestically or internationally.").
55. See U.S. DEP'T OF TRANSP., AIR TRAVEL CONSUMER REPORT 42 (2012) available at http://www.dot.gov/sites/dot.gov/files/docs/2012AugustATCR_1.pdf (averaging 6.86 complaints per 100,000 enplanements compared to the 2.50 complaints for the second worst).

More recently, the DOJ approved a Southwest–Airtran merger⁵⁶ in 2011 without the remedial measures that were present in the United–Continental merger.⁵⁷ Indeed, the DOJ believed that the merger would ultimately be beneficial to consumers through “new service on routes.”⁵⁸ The minimal route overlap and size differential prevents a meaningful analogy to the American–US Airways merger. The Southwest–Airtran merger did not involve a legacy nor did it concern the same market concentration as the American–US Airways merger.

B. Current Settlement

In remedying an anticompetitive merger, agencies utilize two types of remedies: structural and conduct.⁵⁹ Agencies express a preference for structural remedies due to the increased certainty provided and their cost-effective nature.⁶⁰ Given previous concerns over effective monitoring and collusion allegations,⁶¹ a structural divestiture settlement seemed inevitable. Furthermore, the DOJ implemented similar divestitures in the United–Continental merger.⁶²

56. The transaction is actually an acquisition but has become commonly termed a “merger” and still provides a relevant example.

57. Press Release, U.S. Dep’t of Justice, Statement of the Department of Justice Antitrust Division on Its Decision to Close Its Investigation of Southwest’s Acquisition of Airtran (Apr. 26, 2011), <http://www.justice.gov/opa/pr/2011/April/11-at-523.html> (noting that the DOJ’s Antitrust Division “did not challenge the acquisition after considering the consumer benefits”).

58. *Id.*

59. See U.S. DEP’T OF JUSTICE, ANTITRUST DIVISION POLICY GUIDE TO MERGER REMEDIES 6 (2011), available at <http://www.justice.gov/atr/public/guidelines/272350.pdf> (“Structural remedies generally will involve the sale of physical assets by the merging firms or requiring that the merged firm create new competitors through the sale or licensing of intellectual property rights. . . . A conduct remedy usually entails provisions that prescribe certain aspects of the merged firm’s post-consummation business conduct.”).

60. See U.S. DEP’T OF JUSTICE, ANTITRUST DIVISION POLICY GUIDE TO MERGER REMEDIES 7 (2004), available at <http://www.justice.gov/atr/public/guidelines/205108.pdf> (“Structural remedies are preferred to conduct remedies because in merger cases because they are relatively clean and certain, and generally avoid costly government entanglement in the market.”); see also Jessica C. Strock, *Setting the Terms of a Break-Up: The Convergence of Federal Merger Remedy Policies*, 53 WM. & MARY L. REV. 2147, 2154 (2012) (“An analysis of divestiture policy is important because the agencies favor divestitures over other types of merger remedies.”).

61. See *supra* note 36 and accompanying text.

62. See *Continental–United Press Release*, *supra* note 52.

Providing transparency for the airline industry or quelling critics, the DOJ issued its Competitive Impact Statement outlining the current settlement and its remedial nature. The settlement agreement “requires the divestiture of slots, gates, and ground facilities at key airports around the country to permit the entry or expansion of airlines that can provide meaningful competition in numerous markets. . . .”⁶³ Specifically, the new American must divest 104 slots at Reagan National, thirty-four slots at LaGuardia, and two airport gates at each Boston Logan, Chicago O’Hare, Dallas Love Field, Los Angeles International, and Miami International.⁶⁴

In application, the merged airlines lost 15 percent of the combined airline slots at Reagan and 7 percent at LaGuardia.⁶⁵ The settlement also accounted for fears of further expansion of the new airline powerhouse. The settlement prevents reacquisition of divested slots and requires advanced notification of any slot acquisition at Reagan National, regardless of whether it meets the HSR Act threshold.⁶⁶

The Department of Transportation shared interests and concerns with the DOJ and entered into its own agreement with the merging airlines. Primarily concerned with the merger’s effect on smaller communities, the agreement required the newly formed airline to “schedule all commuter slots held or operated by US Airways, AMR, or New American . . . to serve Medium, Small and Non-hub airports for a term . . . of five . . . years.”⁶⁷

Passing DOJ scrutiny represented perhaps the steepest hurdle; however, the merger required further clearance. Opponents of the settlement sought a TRO in contemplation of their pending civil suit under Section 26 of the Clayton Act.⁶⁸ The bankruptcy court ultimately denied the Plaintiffs’ TRO and allowed the transaction to proceed.⁶⁹ Determined, challengers proceeded to the D.C. District Court. The District Court held that the proposed settlement was in the public

63. Competitive Impact Statement at 2, *United States v. US Airways Grp., Inc.*, 2014 U.S. Dist. LEXIS 101877 (D.D.C. Nov. 11, 2013) (No. 1:13-cv-01236-CKK) [hereinafter *Competitive Impact Statement*].

64. *Id.* at 2–3.

65. Bart Jansen, *Justice Settles Merger Lawsuit with AA, US Airways*, USA TODAY (Nov. 12, 2013, 2:05 PM), <http://www.usatoday.com/story/travel/flights/2013/11/12/justice-merger-american-us-airways/3506367/>.

66. *Competitive Impact Statement*, *supra* note 63, at 14.

67. AGREEMENT REGARDING MERGER BETWEEN US AIRWAYS GROUP, INC., AND AMR CORPORATION 1 (2013), *available at* http://www.dot.gov/stes/dot.dev/files/docs/FinalAgreement_DOT_US_AA_.pdf.

68. Section 26 allows private parties to sue for injunctive relief based on anticipated damage caused by an alleged violation of antitrust laws. 15 U.S.C. § 26 (2012).

69. *In re AMR Corp.*, 502 B.R. 23, 42 (Bankr. S.D.N.Y. 2013).

interest under the Tunney Act.⁷⁰ Citing the low rational basis standard, the District Court rejected concerns of loss of routes and lack of scale for the divestments.⁷¹

Anticompetitive concerns surfaced on an international level as well. The European Commission notably determined that the merger would cause a monopoly for the London–Philadelphia route at the London Heathrow airport.⁷² In similar fashion to the DOJ, the European commission utilized divestitures and cleared the transaction.⁷³

While some onlookers may view the treatment of the American–US Airways merger as new antitrust policy for the airline industry, the DOJ’s action appears in congruence with previous mergers and shifting market conditions. Indeed, the \$11 billion American–US Airways merger⁷⁴ encapsulated greater route overlap in a more concentrated market⁷⁵ than the previous mergers. Perhaps the uncertainty of trial prompted the settlement, or perhaps it was an unwillingness to pay higher fares by the many DOJ employees flying out of D.C. Ultimately, the uncertainty of trial and prospective economic analysis likely carried the day.⁷⁶

70. United States v. US Airway Grp., Inc., No. 13-cv-1236 (CKK), 2014 WL 1653269 (D.C.C. Apr. 25, 2014). The District Court found the divestitures to LCCs to be adequate in order to offset the anticompetitive effects of the merger and stated that the settlement will provide LCCs “new incentives to invest in new capacity and generate additional passenger demand.” *Id.* at 29–30. 15 U.S.C. § 16(e)(1) requires a comment period for judgments entered into by the United States in order to determine whether the judgment represents public interest. 15 U.S.C. § 16(e)(1) (2012).

71. US Airway Grp. 2014 WL 1653269, at *7.

72. Press Release, European Comm’n, Mergers: Commission Approves Proposed Merger Between US Airways and American Airlines’ Holding Company AMR Corporation, Subject to Conditions (Aug. 5, 2013) http://europa.eu/rapid/press-release_IP-13-764_en.pdf.

73. *Id.* (“US Airways and American Airlines submitted commitments to release one daily slot pair at London Heathrow and Philadelphia airports, and also provided further incentives such as the possibility for a new entrant to acquire grandfathering rights after a certain period of time.”).

74. Jia Lynn Yang & Ashley Halsey III, *Antitrust Officials Sue to Block US Airways-American Airlines Merger*, WASH. POST (Aug. 13, 2013), available at http://www.washingtonpost.com/business/economy/officials-sue-to-block-us-airways-american-airlines-merger/2013/08/13/6e2f3f0e-0427-11e3-9259-e2aaf5a5f84_story.html.

75. See *supra* Part I.A.

76. See J. Parker Erkmann, *Drama at the Courthouse Door: The US Airways-American Merger*, 1 AIR & SPACE L. Jul. 1, 2014, at 1, 16 (“The DOJ’s decision to settle reflects the significant litigation risk it faced. While all settlements reflect an assessment of litigation risk, the DOJ was under intense pressure. It had the burden of proving that the transaction would substantially lessen competition. This showing would be made with

III. POSSIBLE TURBULENCE:
AN ANALYSIS OF THE SETTLEMENT

A. Adequacy of the Settlement

The airports requiring divestitures in the settlement undoubtedly address the anticompetitive arguments addressed in the DOJ complaint at least to some extent at those airports; however, the remedial nature is less certain at the other concentrated airports not requiring divestitures. Rationalizing the settlement's anticompetitive effects in other markets or airports presents a separate challenge. Additionally, the DOJ's settlement does not seek preservation of US Airways' Advantage Fare program.⁷⁷ The DOJ cannot rest on its laurels regarding the Reagan National and LaGuardia divestitures while neglecting to address the harm posed to passengers at other airports.⁷⁸ In thorough fashion, the initial complaint outlined more than 1,000 city pairs with an HHI increase in the highly concentrated range,⁷⁹ yet only seven airports require divestments. Of course, the divested airports will affect other airports through connecting routes.

The Competitive Impact Statement issued by the DOJ defends the then anticipated pushback from merger opponents.⁸⁰ Unremarkably and unsurprisingly, the CIS outlined anticipated benefits of LCC expansion and the void it will fill given the loss of a legacy. In pertinent part, the CIS estimates that the divestments allow LCCs to provide an additional four million seats per a year at Reagan National and 1.5 million seats per year at LaGuardia.⁸¹

Stepping away from market specifics, the settlement does not provide for a similar legacy powerhouse like American and its pre-merger expansion plan.⁸² The original complaint highlighted the highly

documents and testimony of the parties and industry participants and economic analysis as presented by testifying experts.”).

77. *But cf.* United States v. US Airways, Grp., Inc., 79 Fed. Reg. 14,279, 14,287 (Mar. 13, 2014) (“[T]he benefits of LCC entry and expansion enabled by the remedy will extend to a larger number of passengers and deliver a greater overall benefit to consumers as compared to the Advantage Fares program.”).
78. *See* Kottaras v. Whole Foods Mkt, Inc., 281 F.R.D. 16, 25 (D.D.C. 2012) (“[A] merger that substantially decreases competition in one place—injuring consumers there—is not saved because it benefits a separate group of consumers by creating competition elsewhere.”).
79. *See Amended Complaint*, *supra* note 20, at Appendix A.
80. *See Competitive Impact Statement*, *supra* note 63.
81. Response of Plaintiff United States to Public Comments on the Proposed Final Judgment at 11, United States v. US Airways Grp., Inc., No. 1:13-cv-01236 (CKK) (D.D.C. Mar. 10, 2014) [hereinafter *Response*].
82. *See Competitive Impact Statement*, *supra* note 63, at 8 (“The proposed remedy will not create a new independent competitor, nor does it purport

competitive effects of US Airways' Advantage Fares and their effect on competition with nonstop fares provided by legacies, yet the settlement makes little mention of remedial measures for the inevitable demise of Advantage Fares.⁸³ In other words, the settlement does not adequately explain how the divestitures will redress many of the original anticompetitive concerns.

The DOJ ended its investigation of the United-Continental merger after the airlines promised to divest certain gates.⁸⁴ Three years later, the DOJ appeared to have buyer's remorse with the deal, using the result of the transaction as a justification for blocking the American-US Airways merger.⁸⁵ Of course, the present settlement requires more extensive divestments. Even still, the total divested slots reflect an approximate 112 daily flights a day in comparison to the 6,700 daily flights that the new airline will operate a day.⁸⁶ Assistant Attorney General William Baer argued that the divestments allow for LCCs to disrupt the tight-knit, legacy-dominated market in a way that would otherwise be impossible.⁸⁷ In D.C. fashion, the DOJ turned the once cautionary tale of United-Continental into a supporting case for the current settlement. The thirty-six divested slots allowed Southwest to create five nonstop routes, which led to sixty connecting routes.⁸⁸

Slots at specific airports like Reagan National and LaGuardia and the limited gates at other airports, which rarely change hands, maintain difficult and almost insurmountable barriers to entry. Arguably, the settlement enabled the DOJ to address the longstanding concern of

to replicate American's capacity expansion plans or create Advantage Fares where they might otherwise be eliminated.”).

83. See Letter from the American Antitrust Institute et al., to William H. Stallings, Chief, Transp., Energy & Agric. Section of the Dep't of Justice Antitrust Div. 11 (Feb. 7, 2014), available at <http://www.justice.gov/atr/cases/usairways/comments/aas010.pdf> [hereinafter *AAI Letter*] (“[C]onsumers on the routes where American and US Airways competed with nonstop service will be harmed (such as those flying between Charlotte and Dallas-Ft. Worth), as will the ‘[m]illions of consumers [who] have benefitted’ from Advantage Fares”) (quoting *Complaint*, *supra* note 9).
84. See *Continental-United Press Release*, *supra* note 3.
85. See *Amended Complaint*, *supra* note 20, at 25 (“United and Continental closed their deal on October 1, 2010. The combined firm has reduced capacity at nearly all of its major hubs (including Cleveland) and at many other airports where the two airlines previously competed.”).
86. Jad Mouawad & Christopher Drew, *Justice Dept. Clears Airlines' Merger*, N.Y. TIMES, Nov. 13, 2013, at B2.
87. *Id.*
88. *Response*, *supra* note 81, at 9–10.

LCC expansion by facilitating LCC entry at major airports.⁸⁹ In consideration of the limited divestments in comparison to the inevitably greater loss of routes due to overlap, it is important to note that legacies and LCCs are not equal in market impact. Specifically, the impact on price fares caused by entry of a legacy pales in comparison to fare reductions caused by entry of an LCC.⁹⁰ The DOJ response brief cited JetBlue's entry into the Reagan National to Boston route, which reportedly caused average fares to drop by 39 percent and passengers to almost double.⁹¹ Allowing LCCs to enter the market, the settlement can prove a disrupter for previously tight-knit coordination among the legacies.

Perhaps the added competition that LCCs will provide to the divested airport slots and gates address the expansive anticompetitive arguments originally raised. Even still, the consensus on LCCs is splintered, at best, with Southwest providing the most significant competition.⁹² Most notably, LCCs do not have the necessary network to adequately compete with the now three legacies.⁹³ The settlement does, however, allow for LCC expansion, but given the limited and

89. *See id.* at 8 (“The LCCs that acquire the assets will establish stronger positions at strategically important destinations—including top business markets—where it has been particularly difficult to obtain access. These assets will provide them with the incentive to invest in new capacity and position them to offer more meaningful competition system-wide, forcing legacy carriers to respond to that increased competition.”).

90. *See* Jan K. Brueckner, Darin Lee & Ethan S. Singer, *Airline Competition and Domestic US Airfares: A Comprehensive Reappraisal*, 2 ECON. OF TRANSP. 1, 2 (2013) (“The presence of in-market, nonstop LCC competition reduces fares by as much as 33% in the nonstop markets, and adjacent LCC competition in these markets reduces fares by as much as 20%. . . . The addition of a second legacy nonstop carrier reduces fares by at most 5.3% in these markets, with a third carrier having no fare effect.”).

91. *Response*, *supra* note 81, at 10.

92. *Compare* MICHAEL D. WITTMAN & WILLIAM SWELBAR, *EVOLVING TRENDS OF U.S. DOMESTIC AIRFARES: THE IMPACTS OF COMPETITION, CONSOLIDATION, AND LOW-COST CARRIERS*, 20 (2013) (“The presence of an LCC like Southwest, JetBlue, Allegiant, or Spirit is associated with a decrease in average one-way fare of between \$15 [and] \$36, depending on the airline and the year and controlling for distance and other airport characteristics. However, the presence of AirTran and Frontier no longer have a significant effect on average one-way fares once other LCC competition is taken into account.”), *with* Luo, *supra* note 48, at 37 (“The presence of Southwest lowers fares by 7%, while the coefficient of other LCC competitors providing connecting service is insignificant.”).

93. *See Amended Complaint*, *supra* note 20, at 3–4 (“That enhanced cooperation is unlikely to be significantly disrupted by Southwest and JetBlue, which, while offering important competition on the routes they fly, have less extensive domestic and international route networks than the legacy airlines.”).

airport-specific divestments, the LCCs will likely be unable to realize the growth needed to generate systemic competition.⁹⁴ In modern times, Low Cost Carrier may be a misnomer as operating costs of LCCs increase.⁹⁵ Additionally, the uncertainty as to which LCCs will receive the divested slots and gates, along with the uncertainty as to how those assets will be used, casts doubt on the sufficiency of the settlement.

B. Impact on Market Efficiency

Market efficiency may be ancillary to the DOJ's primary concern of maintaining competition and protecting consumers, but it remains relevant to the point of sustainable growth.⁹⁶ Proponents of market consolidation calculate that the airline market currently underprices fares, and an increase in individual market share—by merging airlines or by market exits—will only ameliorate the current inefficiencies.⁹⁷ While raising fare prices may appear contrary to competition concerns, under a long-run lens, consolidating the market would assuage previous allocative inefficiencies and allow airlines to move closer to Pareto optimal pricing.⁹⁸ The Delta-Northwest and United-Continental mergers arguably proved the benefits of achieving economies of scale.

-
94. See AAI Letter, *supra* note 83, at 10 (“[D]ivestitures to smaller LCCs will have no system-wide impact, and indeed arguably reduce the likelihood that Southwest or JetBlue could conceivably discipline the oligopoly behavior of the ‘Big 3.’”).
95. See Mauricio Emboaba Moreira, John F. O’Connell & George Williams, *The Viability of Long-Haul, Low Cost Business Models*, 2 J. OF AIR TRANSP. STUD. 69, 88 (2011) (finding that LCCs have no more than a 10% cost advantage over legacies through three studies).
96. Antitrust policy concerns the total welfare standard, not the consumer surplus standard. See Barak Y. Orbach, *The Antitrust Consumer Welfare Paradox*, 7 J. COMPETITION L. & ECON. 133, 162 (2010) (“As a surplus criterion, as opposed to welfare optimization, the total surplus standard is consistent with the antitrust methodology.”).
97. See, e.g., Paul Mifsud et al., *Commentary: United + Continental Is a Big Win for All Stakeholders*, 329 AIRFINANCE J. 6 (2010) (“What we found was that, for the decade ending in 2009, the industry produced an average of 7% excess capacity, and this factor alone led to \$70 billion in net losses (in 2009 \$), or negative 5.7% in revenue. The elasticity of demand analysis concluded that the industry underpriced the product by 11% over the 10 years ending 2009. . . . The only way the industry could have priced the product above its true economic cost would have been to reduce the 7% excess capacity by raising revenue to the required level. Of course, this was not possible because every airline had to grow market share in order to lower relative unit costs and expand valuation multiples.”).
98. *Id.*

Both airlines saw a reduction in both fixed⁹⁹ and variable costs¹⁰⁰ after consummating their transactions. Moving forward, the new American can expect similar reductions in operation costs and increased profits.

CONCLUSION

The airline market continues to consolidate in an attempt to achieve economies of scale. The DOJ, in recent years, exercised a unique and relaxed antitrust policy in the airline industry. Filing suit to block the American–US Airways merger appeared contrary to that prior policy; however, the DOJ’s antitrust policy in the airline industry did not change in any meaningful way, and future proposed mergers can expect similar treatment, albeit not legacies. The complaint outlined very real concerns of anticompetitive effects that will result from the merger, yet the divestitures instituted in the settlement remedy a limited number of those effects.

Mathew Drocton[†]

99. See Philip G. Gayle & Huubinh B. Le, *Measuring Merger Cost Effects: Evidence from a Dynamic Structural Econometric Model* 33 (Jan. 8, 2014) (unpublished manuscript) https://editorialexpress.com/cgi-bin/conference/download.cgi?db_name=HIOC2013&paper_id=122 (finding that the post-merger United-Continental had a \$6,479 lower than mean fixed costs among other airlines and post-merger Delta-Northwest had a \$5,478 lower than mean fixed costs).

100. See *Id.* at 29–30 (calculating a \$7.50 decline in marginal costs for Delta-Northwest and a \$13.60 decline in marginal costs for United-Continental).

[†] J.D. Candidate, 2015, Case Western Reserve University School of Law.