



The United Airlines/Continental Airlines merger: a short or long document review?

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3 May 2010 — United Air Lines and Continental Airlines announced their merger today. It will create the world's largest airline by traffic. Delta Air Lines would be unseated as the world's largest airline.

And depending on who you listen to the deal will have little trouble securing approval from the DOJ — or take forever.

For those of us who worked on the first attempt by United/Continental to tie up two years ago one thing remains the same: the two airlines have relatively little overlapping routes/infrastructure; the deal will combine complementary networks rather than strip out costs. Continental is strong in South America and across the Atlantic, while United brings the west coast and routes into Asia. So that's a big point in their favor for DOJ clearance (Continental walked away two years ago because of United's poor financial health).

Scanning the numerous blog posts and media analysis over the weekend, most antitrust lawyers (many former DOJ antitrust lawyers) fell into 2 camps:

1. The deal will be approved in fairly short order — 30 to 60 days:

a. Even if the government determines that certain aspects of the transaction are anticompetitive, the parties will have the opportunity to offer a settlement to remedy any antitrust concerns. There isn't enough route overlap between the carriers to justify killing the deal.

b. The unions won't make a fuss. The pilots (the critical constituent) at both carriers are represented by branches of the Air Line Pilots Association. United aviators are working under a concessionary contract reached when their company was in bankruptcy-court protection, and probably would get big raises to catch up to their Continental counterparts.

c. The government needs/wants an industrial policy/clear rules under which a dysfunctional and serial loss-making sector might be rationalized. Consolidation is essential. Delta-Northwest now has the most efficient cost structure of the legacy US carriers, and is starting to win market share. The government needs to help support airlines struggle to find a business model that makes sense. Consolidation gives them more leverage. Helping the situation is a brightening industry outlook and UAL's own turnaround, which has boosted its liquidity, punctuality and revenue-generating ability.

d. Talk about fares/pricing going up is overblown. In the last decade fares have declined because of pressure from low-fare airlines like Southwest Airlines and JetBlue as well as lower passenger demand. As a result, previous mergers have had a muted effect on ticket prices, especially on routes served by low-fare carriers.

2. The deal will undergo detailed, lengthy, complex scrutiny:

a. Gaining approval to combine from the DOJ and Federal Aviation Administration can take two years. This is a regulated industry where just swapping airport landing slots can be problematic (Posse List members on the US Airways/Delta landing slot swap deal will recall).

b. The Bush administration's Justice Department speedy approval of the Delta merger in finding it pro-competition is not the benchmark. United and Continental will face greater scrutiny because of that combination's size and the Obama administration's vow to "reinvigorate" antitrust enforcement.

c. While the merger could help stabilize the loss-plagued U.S. airline industry, it will take more seats out of the skies and give all carriers more leeway to raise fares. Though the new company may not intend to raise fares, one of the rationales for airline mergers is to cut capacity. That reduces the number of seats in the industry and allows airlines to increase fares.

d. United and Continental will no longer be competing against each other on some routes, allowing them to save money but offering travelers fewer options.

e. There are significant market share issues (see immediately below).

The market share issues

1. The combined airlines would have a 40 percent market share at San Francisco International and 35 percent at Chicago O'Hare International.
2. At Houston Intercontinental, one of the city's two airports, they would have 64 percent of the market and at Newark Liberty International, 55 percent.
3. Combined, United and Continental have 21 percent of domestic capacity, in terms of so-called available seat miles, or one seat flown one mile. Delta has a market share of 20 percent. Globally, the merged companies would have a 7 percent market share.

The principal players

* ***The United Airlines team:*** J.P. Morgan Chase and Goldman Sachs, and law firm Cravath, Swaine & Moore advised United. Cravath has reprised its role representing Chicago-based UAL in merger talks. According to *American Lawyer*, corporate partner Scott Barshay previously led a team from the firm advising UAL on scuttled talks with US Airways and Continental in 2008.

Also joining the United Airlines team is their long-time counsel Howrey Simon. Howrey is advising United Airlines on EU competition matters in respect of the merger. Howrey's legal team consists of partners Trevor Soames, Geert Goeteyn, Goetz Drauz and senior associates Kristian Hugmark and Sarah Jordan. Howrey's team are Brussels-based (Geert Goeteyn actually splits his time between Brussels and London) aside from Sarah Jordan who is based in London. Trevor Soames is managing partner of Howrey's Brussels office and Co-Chair of Howrey's world-wide antitrust practice group and lead partner in this matter.

* ***The Continental Airlines team:*** Lazard and Morgan Stanley, and law firms Jones Day , Vinson & Elkins LLP and Freshfields, Bruckhaus advised Continental. All three firms have long-standing ties to the Houston-based airline. V&E has handled antitrust litigation for Continental in the past, but the firm is providing securities and due diligence counsel to the airline on its proposed merger with UAL. Jones Day handled Continental's bankruptcy a decade ago and also represented the company when it was a creditor in the Chapter 11 cases of Delta Air Lines five years ago. The firm also handles litigation matters for Continental.

And according to *American Lawyer*, a big surprise: Jones Day is not involved in the antitrust arena for Continental. The firm has previously advised other prominent players in the U.S. aviation industry — such as American Airlines — on antitrust matters. Instead, the antitrust work went to Freshfields, which handled reviews of Continental's proposal to join UAL in the Star Alliance of global airlines last year.

Gregory P. Bufithis is the founder and chairman of *The Posse List* and its sister sites *The Electronic Discovery Reading Room* (<http://www.ediscoveryreadingroom.com>) and *The Posse Ranch* (www.theposseranch.com). He is also founder and chairman of *Project Counsel* (www.projectcounsel.com).