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MERGERS IN REGULATED INDUSTRIES: 
THE ROLE OF THE REGULATORY AGENCY

C. PAUL ROGERS III*

The merger of two or more independent business enterprises into a single business entity is anathema to the underlying policy of our economic system—the promotion of competition. This is particularly true when the merging businesses are direct competitors or when a business joins with a supplier or a customer, for it is then that restraints on competition are most likely to occur. The storied antitrust legislation known as the Sherman Act and the Clayton Act were intended to be legal checks on restraints of competition and monopolization of industries. Section 7 of the latter specifically prohibits any corporation from absorbing all or any part of another company “where in any line of commerce in any section of the country, the effect thereof may be substantially to lessen competition or to tend to create a monopoly.” This provision, intended to restrict monopolistic tendencies in their incipiency, requires a strict legislative enforcement policy against mergers which restrain the freedom of choice so vital to competition.

The consolidation and merger of companies in regulated industries presents different policy considerations than do mergers in nonregu

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1. Consolidation between direct competitors is known as horizontal integration. Direct competitors can be generally defined as business entities which offer the same or similar products for sale for profit in the same or in close geographic proximity.
2. Consolidation between a business entity and a supplier of the business is known as vertical integration.
4. Id. §§ 12, 13, 14-27, 44 (1970).
lated sectors of the economy. Regulation of an industry generally develops when it is determined that some type of monopolistic market structure is better suited to obtain maximum efficiency in an industry than the traditional competitive system. The regulating agencies which are established, generally seek at least some competitive objectives as well as additional performance goals peculiar to each industry. Each regulatory agency functions under statutory enactments unique to that regulated sector.\(^7\) The “public interest” is usually the primary objective emphasized by the statutes.\(^8\)

Regulated sectors of the economy are regulated because the competitive system does not maximize the “public interest.” In order to attain this maximization, restrictions are placed on competition in the particular industry such as restricting the freedom of entry, rate regulation, and control over areas of operation. Herein lies the dilemma regarding mergers in the regulated sectors: Mergers typically have anti-competitive impacts on an industry, depending of course on the size of the merging firms and on the structure of the industry. The antitrust provisions applicable to the merger situation were designed to promote competition.\(^9\) Competition is restricted in industries regulated by federal statute. The quandary results from the problem of applying pro-competitive antitrust provisions against anti-competitive mergers in an industry in which competition is restricted, at least to some degree. Regulatory agencies thus face the problem of applying antitrust provisions emphasizing freedom of competition in an industry where competition is restricted by law. This article will concentrate on how the Civil Aeronautics Board and the Interstate Commerce Commission approach and handle this problem, as applied to the transportation industry, the statutory guidelines within which they have to work, and the view the federal courts take of their determinations in this complex area.

**STATUTORY BACKGROUND**

The threshold question to be answered is what is the statutory role

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of regulatory commissions when two companies within a regulated sector desire to merge. Generally, a merger proposal must be submitted for approval to the appropriate agency. These agencies have absolute statutory authority to approve or deny any merger proposal, subject only to review by the federal judiciary. Congress, recognizing the need for regulation of the economic structure of regulated industries through control of acquisitions, consolidations and mergers, enacted an amendment to Section 408 of the Federal Aviation Act which gives the CAB supervisory power over one seeking to acquire control of an air carrier. This extended the CAB's jurisdiction to any noncarriers or entities outside the aeronautics industry attempting to gain control of an air carrier and closed a substantial loophole in the Board's authority over air carrier mergers. Since regulatory agencies are authorized to approve or deny any merger within their regulatory jurisdiction, the agencies must enforce antitrust policy if it is to be enforced at all. But the role of antitrust laws in regulated mergers is more complex than a simple inquiry into whether the various commissions apply antitrust law when considering a prospective merger.

Generally, a merger is exempt from antitrust law upon approval by the regulating agency. Section 7 of the Clayton Act, restricting mergers which have a tendency to lessen competition or create a monopoly, exempts itself from application to transactions consummated pursuant to authority given by the regulatory agencies, including the Civil Aeronautics Board and the Interstate Commerce Commission. Section 5 of the Interstate Commerce Act specifically exempts transactions, including mergers approved by the Commission, from the operation of antitrust laws. The effect is that agency approval of a merger in a regulated sector shields the transaction from antitrust attack even if it is violative of the anti-monopoly statutes.

12. See Rasenberger, Control of an Air Carrier By 'Any Other Person'—Flying Blind Under the Federal Aviation Act, 37 J. Air L. & Com. 65 (1971).
15. But this is not to say that regulatory commissions may ignore the anti-competitive aspects of a proposed merger. The Justice Department, always attempting to promote competition, is frequently an intervening party in agency proceedings. See, e.g., United States v. ICC, 396 U.S. 491 (1970). Section 408b of the Federal Aviation Act provides that the Civil Aeronautics Board cannot approve any merger which would restrain competition or result in the creation of a monopoly. 49 U.S.C. § 1378 (1970). Furthermore, Section 11a of the Clayton Act gives the Interstate Commerce Commission, the Federal Communications Commission, the Civil Aeronautics Board, and the
While Section 11a of the Clayton Act\(^6\) authorizes regulatory bodies to enforce the section 7 prohibition against mergers which restrict competition or tend to create a monopoly, the agencies must additionally look to the special legislation appropriate in their regulated sector to determine what role Congress has required competition to play in the consideration of merger proposals. As will become apparent, the role of competition may vary significantly among the various regulated sectors of the economy.

First, it is important to note a fundamental tenet of the decision making process in the formulation of mergers in regulated industries. To the extent that an agency applies the same antitrust criteria to proposed consolidations that a court would, one decision maker is merely substituted for another. The antitrust exemptions of approved mergers in many regulated sectors are then insignificant because the agencies apply the same standards as the courts. But to the extent an agency applies different principles to merger applications than would a court, the agency can confer true immunity from later antitrust attack. In this circumstance the regulatory body has a distinct role, for antitrust considerations may be skirted and mergers may be consummated which have definite anticompetitive effects. As illustrated below, agencies frequently do apply different principles but judicial review often acts as a check on attempts to completely circumvent antitrust policy.

**INTERSTATE COMMERCE COMMISSION**

Section 5 of the Interstate Commerce Act\(^7\) authorizes the Interstate Commerce Commission to approve a proposed transaction to merge or consolidate which will be consistent with the public interest. Section 5(2)(c) specifies that the Commission, in passing upon any proposed transaction, shall weigh the effect the transaction may have on adequate public transportation service, and the effect that the inclusion or failure to include other railroads in the involved territory may have on the public interest.\(^8\) There is no mention in the statute of what role, if

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\(^ {18}\) Id. § 5(2)(c) (1970). The specific language of the statute provides the following guidelines which the Commission must consider when ruling on proposed mergers and consolidations:

1. The effect of the proposed transaction upon adequate transportation service to the public;
2. The effect upon the public interest of the inclusion, or failure to include, other railroads in the territory involved in the proposed transaction;
any, the maintenance of competition is to play in the Commission's
determinations. This omission, coupled with the exemption from anti-
trust laws of mergers approved by the Commission, seems to evidence
a Congressional policy that antitrust considerations take a back seat to
considerations which the Commission considers to be in the public
interest.

McLean Trucking Litigation

In the landmark case of *McLean Trucking Co. v. United States*, the Supreme Court attempted to articulate the role of competition and
the antitrust laws in consolidation proposals before the regulatory
agencies. Involved was a motor carrier merger proposal of eight large
carriers with both horizontal and vertical aspects, from which would
emerge the nation's largest trucking concern. Although the Commiss-
ion's order authorizing the consolidation was not set aside, the Court's
interpretation of Section 5 of the Interstate Commerce Act has become
instrumental in subsequent adjudication involving all mergers governed
by the Interstate Commerce Commission. In 1959 the Supreme Court
specifically held the *McLean* interpretation of section 5 applicable to
railroad mergers.

The merger in *McLean* was opposed by the Antitrust Division of the
Justice Department, and by numerous competing carriers on the ground
that it would unduly restrain competition in the motor carrier industry.
The Interstate Commerce Commission acknowledged that substantial
competition between the involved carriers would be eliminated by the
merger but held that section 5 was intended to permit consolidations
which would, absent approval, result in restricting competition contrary
to antitrust laws, where advantages in the public interest overcome the
anti-competitive aspects of the merger. Further, in a detailed
analysis of the territories involved in the merger, the Commission con-
cluded that ample competitive motor carrier service would remain.

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22. *Id.* at 159-60.
The Supreme Court agreed with the Commission, holding that the national transportation policy, as set forth in the Interstate Commerce Act, is the Commission's guide to what constitutes the "public interest" in consideration of a merger proposal. Even though the policies expressed in the Interstate Commerce Act are to be the basic determinants for action by the Interstate Commerce Commission, it is not required to ignore competitive aspects of prospective consolidations. While "the premises of motor carrier regulation posit some curtailment of free and unrestrained competition," the preservation of competition is a consideration to be weighed in the attainment of the national transportation policy.

In summarizing the role of competition in regulated mergers the Court emphasized that the decline in competition resulting from consolidation must be balanced against such considerations as improved service, safer operation and lower costs in the Commission's determination of what will benefit the public interest. Thus, McLean precludes the Interstate Commerce Commission from ignoring antitrust policies in determining whether a merger is consistent with the public interest under Section 5 of the Interstate Commerce Act. The Commission clearly must give some weight to the competitive aspects of a merger, although the Court left the matter largely to the Commission's discretion.

While the Interstate Commerce Commission has specific legislation and Supreme Court decisions interpreting that legislation to serve as guidelines, the Commission must of necessity be particularly influenced by the economic structure of the railroad and motor carrier industries. This is reflected by the Court's pronouncement in McLean that the weight to be given the diminution of competition in balancing the several factors making up the public interest is a matter for the expertise of the Commission. Stated differently, the ICC, within its

23. The Supreme Court's statement of the national transportation policy was announced in McLean Trucking Co. v. United States, 321 U.S. 67, 82-83 (1944).
24. Id. at 82-83.
25. The fact that Congress had conferred immunity from antitrust prosecution on carriers participating in an approved merger does not relieve the Commission of its duty to consider the effect of the merger on competitors and on the general competitive situation in the industry. Id. at 87.
26. Id. at 87.
statutory guidelines, is free to formulate policy regarding mergers and consolidations according to what it determines will be most beneficial to the industry. This does not preclude a different approach being taken for railroads than for motor carriers, since the industries may not be identical in economic structure and well-being.

**Railroad Mergers**

A brief consideration of the recent economic difficulties of the railroad industry, combined with a look at Commission and federal court decisions, should illustrate the dependency of ICC policy regarding mergers on the economic condition of the industry. The much publicized railroad merger movement began in the mid-fifties. Behind the movement is an industry-wide reaction to the financial setbacks which have befallen railroads since the post World War II boom. The basic reason for this decline is probably the increasing competition of other forms of transportation with the railroads, that is, increasing intermodal competition. For example, the percentage of ton-miles of freight carried by the railroads dropped from 68.19 percent in 1946 to 43.24 percent in 1961, while at the same time the trucking industry increased its percentage from 7.28 percent to 23.1 percent. During this period operating revenues for the railroads fell from 70 percent of total revenue of surface carriers to 50 percent.  

The decline in the financial fortunes of the railroads, however, has not been caused solely by increased intermodal competition. No control of entry into the industry existed until the Transportation Act of 1920 was passed. This was well after the number of operating railroads had become too large for regulation to be effective. Parallel rail routes and

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29. 49 U.S.C. § 1(18) (1970), provides that:
No carrier by railroad subject to this chapter shall undertake the extension of its line of railroad, or the construction of a new line of railroad, or shall acquire or operate any line of railroad, or extension thereof, or shall engage in transportation under this chapter or by means of such additional or extended line of railroad, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require the construction, or operation, or construction and operation, of such additional or extended line of railroad, and no carrier by railroad subject to this chapter shall abandon all or any portion of a line of railroad, or the operation thereof, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity permit of such abandonment. Nothing in this paragraph or in section 5 of this title shall be considered to prohibit the making of contracts between carriers by railroad subject to this chapter, without the approval of the Commission, for the joint ownership or joint use of spur, industrial, team, switching, or side tracks.
duplicate terminal facilities were commonplace in the early 1900's because railroads had a virtual monopoly on transportation; thus the railroads had only to compete against themselves. But considering current traffic volume and increased intermodal competition, these dual facilities may be inefficient at a time when railroads need to reduce costs to a minimum.

The railroad industry in deference to formidable intermodal competition and rampant inefficiency within its own ranks has sought mergers and consolidations as a remedy. The choice is a logical one. Competition in the industry has shifted from intramodal to intermodal. Railroads, by consolidating with one another, are better able to compete with competitors outside the industry. Consolidation allows the now limited resources of railroads to be combined in a unified effort to compete with the intermodal competitors. Railroads believe that mergers can increase operational efficiency and at the same time reduce expenses by such factors as the elimination of duplicate facilities. While more profits will result for railroads, transportation, it is argued, will also profit because railroads will be able to reallocate their resources to new equipment and technological advances.30

As noted before, the Interstate Commerce Commission has been given wide discretion by the Supreme Court in its consideration of merger proposals. This enables the Commission, within its statutory boundaries, to be guided in its decisions by what it considers to be best for the industries which it regulates. The Commission has propounded no specific policy regarding railroad mergers and decides cases on a case-by-case approach, but the recent Commission decisions indicate that the agency favors consolidation as a remedy for the sagging railroad economy. Indeed, the ICC seems to be taking an increasingly liberal approach to railroad mergers with the result that competition, at least intramodal competition, is becoming less important in determining whether the public interest will be served by prospective mergers.

The recent railroad merger boom often has involved the acquisition of a financially weak road by a stronger one.31 In these types of cases the Commission often justifies a substantial lessening of competition between the merging lines because it is in the “public interest” that

a railroad is kept from going bankrupt. The 1960 merger of the Erie & Delaware Railroad with the Lackawanna & Western involved two financially weak roads. The Commission recognized that competition between the two lines was substantial. Competitive main lines existed between New York City and Buffalo, and the two lines served 55 common stations between the two terminals. However, the Commission permitted the merger, holding that the strengthening of the weak roads was in the public interest, and that strong competition from other railroads and other modes of transport would continue. Further, the Commission believed that the features of the merger which eliminated competition between the two applicants would also provide greater allocation of resources and greater efficiency of operation through elimination of duplicate plants, facilities and operations.

Such determinations by the Commission have been commonplace. In addition to allowing consolidations between two weak lines and between weak and strong lines, the Commission has also authorized mergers involving two end-to-end roads. The elimination of some competition, even substantial competition, has normally been authorized if the proposed merger was in the public interest. It is increasingly apparent that showing a merger is beneficial to the railroad industry suffices to meet the public interest requirement.

The Commission's liberal attitude toward rail mergers has resulted in consolidations between strong parallel roads in the late 1960's, even though competition between railroads was virtually eliminated in large geographic areas or in several metropolitan centers. In Florida East Coast Railway v. United States a federal court upheld ICC approval of a merger between two prosperous parallel lines which eliminated competition in 81 percent of Florida's railroad mileage. The infamous Penn-Central merger virtually eliminated competition in 32 urban centers. This merger has been considered by some to be a watershed because it established that a rail carrier with significant market power in a large area could be created despite the resultant elimination of interrail competition.

33. Id. at 246-48.
Northern Lines Merger

The Northern Lines merger of 1970 may be the furthest step yet taken by the Interstate Commerce Commission. The merger involved three large, healthy lines which were competitors. Final Supreme Court approval of the consolidation allowed two of the longest and strongest parallel lines in the western United States, the Great Northern Railway and the Northern Pacific Railway, to join together. The newly formed giant had more miles of track than any other railroad in the country. The Commission considered predicted fixed cost savings and service improvements resulting in prospective rate reductions and more efficient routing to be of prime importance in granting the merger. Intramodal competition was found not to be greatly affected despite the fact that no effort was made to define the product or geographic markets of each road and despite the fact that Great Northern and Northern Pacific were largely competitive parallel lines. Little attention was given to the strength of the merging roads or to the relative strengths and competitive effects on other competing railroads. The Commission's basic premise throughout was that intramodal competition should not be a primary element for consideration but that efficient allocation of national transportation resources is the primary objective.

The ICC seemed to suggest that consideration of intermodal rather than intramodal competition is more relevant in merger proposal evaluations. While the exact emphasis placed on intermodal competition is difficult to ascertain, the Commission stated in Northern Lines that intermodal competition was relevant in determining the degree to which competition would be eliminated by the merger. Thus, substantial elimination of intramodal competition could be offset by intermodal competitive conditions remaining adequate.

It is interesting to note a fundamental change in Commission policy occasioned by the Northern Lines litigation. In the first merger hearing in which the Commission denied permission to consolidate, it was held that the object of the Transportation Act was not to encourage mergers but to permit them only if they were shown to be in the public

39. 331 I.C.C. at 245-46.
40. Id. at 273.
interest. The Commission stated that there was no presumption favoring mergers; the burden was on the petitioning parties to establish that the mergers would further the public interest and not result in a substantial lessening of competition. On rehearing the Commission allowed consummation of the merger on essentially the same facts implicitly holding that the preservation of competition is no longer necessary to the public interest and the primary objective of the Transportation Act was the achievement of efficiency and optimal resource use. The second decision restated the Commission's view of the policy objectives of the act and concluded that mergers which are consistent with the public interest should be encouraged. Thus the ICC changed its position drastically by assuming that, in absence of evidence to the contrary, the public interest would be served by railroad mergers.

The Northern Lines case indicates that the Commission, while previously sympathetic to mergers, can now be said to be practically encouraging consolidations where it is shown that the public interest will be enhanced. A prime consideration in the evaluation of the public interest is a look at whether the railroad industry will benefit, although the Commission never expressly makes that inquiry. Thus, it is apparent that the Interstate Commerce Commission's role in the regulation of railroad mergers has been heavily influenced by the economic condition and needs of the industry. The Commission's policy has turned a complete about face from the early part of the century when railroads were king. The Commission rarely authorized a merger and rejected some proposals which, with substantially the same facts, have been approved during the recent merger increase. So

42. Id. at 522-23.
44. 331 I.C.C. 228, 269 (1967). It was stated that:
The prior report approached this case under the view that the policy of section 5... was something other and less than 'to foster and encourage' rail mergers. ... Upon reexamination ... we conclude that the policy of the act is clearly to facilitate and thereby foster and encourage consolidations which can be shown to be consistent with the public interest.
Id. at 269.
46. E.g., ICC v. Pennsylvania R.R., 169 I.C.C. 618, 619 (1930); ICC v. Baltimore & O. R.R., 160 I.C.C. 785 (1930); Control of Virginian Ry., 117 I.C.C. 67 (1926) (merger of two strong roads denied). In the first two cases the Commission held as a somewhat distinguishing factor the fact that control of a railroad had been acquired without ICC approval.
while often validly criticized the Commission is heavily influenced by changes in the industries which it regulates.\textsuperscript{47} Mergers are promoted because they are seen as a way to strengthen the railroad industry from within and to combat increasing intermodal competition.

\textbf{CIVIL AERONAUTICS BOARD AND AIRLINE Mergers}

The Civil Aeronautics Board regulates the air carrier industry and any merger attempt between two or more airlines must first be approved by the Board.\textsuperscript{48} The Board and the Interstate Commerce Commission have the same general regulatory power over mergers but there is a definite substantive difference in the specific regulatory legislation. While Section 5 of the Interstate Commerce Act makes no mention of the role of competition in regulated consolidations, Section 408b of the Federal Aviation Act directs that the Civil Aeronautics Board shall not approve any merger which creates a monopoly and restrains competition.\textsuperscript{49} Under both statutes, however, the "public interest" is the guiding consideration to be accorded merger proposals. But, as will be subsequently pointed out, factors making up the public interest may differ.

The regulatory duties of the CAB are much less complicated than those of the ICC. The Civil Aeronautics Board oversees approximately a dozen major air carriers. These airlines have little competition from surface transportation for passenger traffic; the competition is largely intramodal. On the other hand the Interstate Commerce Commission must regulate all the railroads, the domestic water carriers, and the thousands of interstate truckers, all fiercely competitive with each other.

The Civil Aeronautics Board, while stressing the anticompetitive aspects of consolidations, has also been responsive to some extent to the changing needs of the airline industry. Traditionally the Board has sought to maintain what it considers an optimum level of competition in the air carrier industry. The industry is made up of the very competitive Big Four—American Airlines, Trans World Airlines, United


\textsuperscript{49} 49 U.S.C. § 1378(b) (1970). The specific language of the statute provides that the Civil Aeronautics Board “shall not approve any consolidation, merger, purchase, . . . or acquisition of control which would result in creating a monopoly or monopolies and thereby restrain competition or jeopardize another air carrier not a party to the consolidation, merger, purchase, . . . or acquisition of control. . . .” Id. § 1378(b).
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Airlines, and Eastern Airlines—plus approximately ten smaller carriers which are competitive with the Big Four on a regional basis, and numerous local service carriers which have very limited territorial operations and normally receive federal subsidies. Until recently the Board has sought to maintain the basically oligopolistic structure of the industry by permitting few mergers, particularly if a member of the Big Four was involved. Additionally, the Board has attempted to keep the industry from becoming overly competitive by severely restricting entry.50

The Board has historically approved consolidations only in very limited circumstances, such as where there were no conflicts of competitive interest between the applicants. In two early cases, United-Western Air Express51 and American-Mid-Continent Airlines,52 the Board formulated its restricted approach to airline mergers. In each case the large size of the proposed surviving carrier and its power to control connecting traffic, thus adversely affecting competing airlines, played a leading part in the Board's disapproval of the proposed transaction.

One of the factors considered important by the Board in rejecting the American-Mid-Continent proposal was the fact that the two existing systems had a small amount of integration; that is, their routes were relatively uncomplimentary. The Board felt that the light exchange of traffic between the applicants weighed heavily against allowing the merger.53 The Board also considered the size and competitive position of American to be of prime importance, although disavowing any intent to restrict expansion by American in all circumstances. American was noted as being the largest domestic carrier. The addition of another system, though a small one, to a carrier of American's size and competitive position was considered anathema to the policies embodied in the Civil Aeronautics Act of promoting sound economic conditions and competition to the extent necessary to assure the development of an

53. There was a 4.03% exchange of passengers with Mid-Continent provided by American, and 3.36% of revenues were provided by exchange with American. Id. at 374.
air transportation system in the public interest. The Board also expressed the need to regulate air transportation in such a manner as to improve the relations between, and coordinate transportation by, air carriers.

A decisive factor in the rejection of the United-Western Merger proposal was the prospective elimination of competition between the participant carriers, a factor not considered in American-Mid-Continent. The consolidation would have eliminated Western as the only north-south carrier in the territory west of the Rocky Mountains, and would have given United an unhealthy predominance in the area. It is interesting to note that while United's rank of the fourth largest domestic carrier was mentioned in the Board's opinion, the weight accorded to this fact, if any, was not evident.

Almost without exception all the early mergers meeting Board approval involved some aspect of "the failing company doctrine." In other words the Board's principal motive in approving the combinations was a hope of improving the financial condition of one or more of the participants. For example, the first three mergers approved all involved carriers which were either bankrupt or were operating at substantial deficits. Northeast Airlines was permitted to acquire Mayflower Airlines, a company which had not operated for five years and had been adjudged bankrupt. Trans World Airlines absorbed a carrier, Marquette Airlines, which had operating deficits of more than $200,000 and had inferior equipment and infrequent, unreliable service. Similarly, Inland Airlines was shown to be unable to become a viable competitor and merged with Western Airlines. The three mergers did not eliminate any parallel service nor was potential competition foreclosed between the participants.

The Board's policy of favoring mergers in which the failing company doctrine played a significant part was further fostered in the 1950's. In fact the Board struck out on a policy of encouraging carriers in fi-
nancial straits to merge and it even attempted to find suitable airlines to absorb failing companies. As is normally the case, the Board had a reason for these efforts. The late forties witnessed a sharp decline in the earnings of domestic trunklines, occasioned by the failure of the demand for passenger air service to match the growth in capacity for carriage. The reversal stepped up the Board’s efforts to seek out opportunities for economic improvement through intramodal transactions such as mergers and acquisitions. Apparently some pressure had been brought to bear on the Board by both governmental and industrial publications alleging that the financial difficulties of many carriers had been largely attributable to regulatory policies resulting in excessive competition. In 1950 the Board investigated the feasibility and desirability of bringing about the merger of air carriers where such consolidations would improve the structure of the air transportation map of the county, and would substantially benefit the public.

The case of Colonial Airlines illustrates the Board’s policy of encouraging mergers which improved the financial condition of a carrier. The early 1950’s found Colonial heavily dependent on federal subsidies with no chance to become self-sufficient. The Board encouraged an acquisition of Colonial by an economically stable carrier. Ultimately the Board had to choose between two carriers, National and Eastern. Preliminary agreement to merge was reached by Colonial and National, but Colonial’s stockholders rejected the proposal. The Board agreed that either a Colonial-National or a Colonial-Eastern consolidation was in the public interest but favored the Colonial-Eastern combinations because it would provide a more efficient integration of the two systems. Also, a Colonial-Eastern merger would have resulted in less revenue diversion from National than would have been suffered by Eastern if National and Colonial had merged. An additional consideration was that immediate integration could be accomplished since both companies’ shareholders had ratified the plan, thus saving the federal government an $850,000 annual subsidy payable to Colonial.

The American-Mid-Continent case was not mentioned in the opinion although the cases had striking similarities. Both proposed consolida-

61. E.g., Eastern-Colonial, Acquisition of Assets, National-Colonial Integration Investigation, 18 C.A.B. 781 (1954).
64. Eastern-Colonial, Acquisition of Assets, National-Colonial Integration Investigation, 18 C.A.B. 781, 784 (1954).
65. Id. at 782.
tions involved a member of the Big Four and a much smaller, financially troubled regional carrier. The large size and dominant competitive position of the acquiring carrier was not determinative in the Colonial case as it had been in the American-Mid-Continent opinion. In allowing the merger with Eastern, the Board's desire to alleviate Colonial's financial problems was decisive; indeed, the Board had been actively seeking a merger for Colonial. The divergence in policy exemplified by the two cases 8 years apart emphasizes the extent to which the Board is influenced by changes in the economics of the airline industry.

Merger authorizations were frequent among air carriers from the late forties until 1956 when, in addition to the Colonial-Eastern integration, six mergers were consummated. The principal motive behind the approval of the consolidations was a hope of economically improving at least one participant of each merger. Not all the carrier take-overs during this period involved failing companies; several carriers offered promise of competing in the future with the carriers with which they merged. In many cases in which mergers were ultimately consummated the Board actively sought partners for one of the participants.

Following the merger fad of the early 50's, a period of general prosperity for airlines prevailed except for a short-term reversal in the early 1960's. The reason for the lean period was just as in the previous decade: the rate of growth of capacity for carriage pushed far ahead of rate growth of actual traffic. Jets, with their larger seating capacities and increased costs, were pervading the industry, and there was no particular reason for passenger revenue to keep pace. The Board, again under some pressure to promote mergers, publicly encouraged carriers to arrive at voluntary consolidation arrangements and indicated its willingness to consider promptly any merger agreements presented. An investigation was even undertaken evaluating the possible modification of air services between the southern and northeastern areas of the

United States, although nothing practical resulted.\textsuperscript{70}

Despite all the favorable talk and the brief economic decline, only one merger was approved between 1956 and 1967.\textsuperscript{71} That merger was a direct result of the extremely perilous financial position of Capital Airlines. Capital had undergone serious financial loses for five consecutive years and was unable to finance the purchase of the new jet airplanes. This resulted in curtailment of service and its share of total industry traffic falling from 6.3 percent to 4.9 percent in two years. Further, Capital was faced with a $34 million foreclosure suit for equipment already in use. Unless something was done the carrier was faced with immediate extinction.

Capital had applied for a federal subsidy, but the Board questioned the legality of such an expenditure.\textsuperscript{72} Traditionally, subsidies had been available only to the smaller, financially weaker, local service carriers. The larger trunklines, such as Capital, had never received federal funds. In addition the Board seriously doubted whether a subsidy, even if available, could be made in an amount sufficient to restore Capital as a viable air carrier since it required an estimated $100 million worth of new equipment alone. Accordingly, the Board stated it would not endorse the needed subsidy absent legal compulsion.\textsuperscript{73} Thus the Board felt that it had no practical alternative but to approve a merger between Capital and United Airlines if Capital were to survive in fact if not in name. Capital was then the fifth largest domestic carrier, and the CAB believed that its stabilization was important to the industry. The Board was unwilling to gamble on uncertain remedies and was confident a merger with a powerful carrier such as United would provide the greatest promise for a successful solution.

In approving the consolidation the Board held that the public interest in preventing Capital’s collapse outweighed all the disadvantages caused by the merger.\textsuperscript{74} The “falling business doctrine” was specifically applied. The adoption of this doctrine was held to override the consideration of whether the merger violated the first proviso of Section 408b of the Federal Aviation Act, prohibiting approval of a merger which would result in a tendency to create a monopoly or a restraint of competition. It is unlikely that the United-Capital proposal, involv-
ing a combination of one of the three largest domestic carriers with the fifth largest carrier, could have withstood the antitrust scrutiny of section 408b under normal circumstances. The Board in applying the failing business doctrine, however, made it clear that the doctrine was not to be freely used to avoid the antitrust consequences of purported mergers but rather was to be employed only in narrow circumstances when one party has serious financial problems and the prospects for rehabilitation are so remote that complete business failure is likely. 75

The United-Capital Merger Case again illustrates the flexibility of regulatory agencies. The Civil Aeronautics Board was able to deviate from its standard procedure regarding merger proposals and approve a merger in order to save a large carrier from extinction.

The air carrier prosperity of the mid 1960's was followed by a decline in the latter part of the decade. Again traffic growth failed to keep pace with the increase in capacity for carriage. Four mergers have been approved since 1967 and in each case the Board saw the proposed transaction as a means to improve the economic well-being of one or more of the participating carriers. Three of the mergers involved local service carriers 76 while the fourth, not ultimately consummated, was a combination of trunklines. 77 The principal consideration favoring the consolidations of the local service carriers was the Board's desire to reduce the increasing federal subsidies required for the small carriers to operate. 78

The local service carrier mergers did not result in the elimination of any existing point-to-point competition but the contiguous position of the participating carrier's routes did make them outstanding potential competitors. This aspect of competition has traditionally been ignored, but in the Air West case 79 the CAB recognized the elimination of potential competition as a factor to be weighed in the consideration of consolidation proposals. Potential competition would seem to be

75. Id. at 309-10.
78. C.A.B. Ann. Rep. 1 (1968). The Board noted in its annual report for 1968 that the three local service carrier mergers would produce immediate subsidy reductions of $503,000; $676,000; and $902,000.
within the ambit of the section 408b antitrust provisions. It is puzzling that the Board had not earlier recognized potential competition as an important factor to be considered, but of course a strict policy regarding potential competition could negate some of the positive aspects of proposed mergers and force the CAB into a less flexible position. If the effects of consolidations on potential competition were always considered, the Board would have a more difficult time justifying economically advantageous mergers which do not qualify for the application of the failing business doctrine.

Until recently the Supreme Court had never had occasion to review a Board decision regarding a merger and had never construed Section 408b of the Federal Aviation Act. In *Hughes Tool Co. v. Trans World Airlines*, however, the Court determined that the CAB alone has the power, subject to judicial review, to decide if acquisitions of control of an air carrier meet the standards of competition and monopoly provided by section 408b. While this holding is not surprising, the Court's further delineation of the CAB's supervisory powers are quite significant. The Court stated that the CAB has a continuing power, where it has authorized control of an air carrier by another entity, to oversee, and if necessary alter, the manner in which control is exercised. The Board also has investigatory powers and supervisory authority over specific transactions undertaken by the new parent company. This surveillance is exclusive of the governmental forces that invoke the antitrust laws, although the Board must continually appraise the effect on competition and possible monopolization which the authorized acquisition or consolidation may have.

While all the ramifications of this opinion are not yet evident, the decision definitely is authority for expanded regulation by the CAB of mergers and their aftermath. The specific holding of the case is an attestation to this. The Court held that transactions of Hughes Tool, promulgated after Hughes' acquisition of control of T.W.A., involving T.W.A. and challenged by T.W.A. as violative of antitrust laws, were under the Civil Aeronautics Board's control and surveillance; the transactions thus had immunity from the antitrust laws.

81. Id. at 389.
82. Id. at 369. It is essential to point out that while the roles of the Interstate Commerce Commission and the Civil Aeronautics Board in regulating mergers within their respective sectors are perhaps typical of the duties exercised by regulatory bodies over consolidations generally, Congress and the Supreme Court have mandated far less pervasive controls for other agencies. In California v. FPC, 369 U.S. 482 (1962) part of...
CONCLUSION

The competition which our free enterprise system promotes and the regulation of competition arising from the regulated sectors of the economy appear at least superficially to be mutually exclusive. In the real world of which our society is a part, regulation and competition must be complementary devices. Thus it is the role of the regulatory agency to determine the appropriate place competition is to play in the regulated sectors. As has been demonstrated, the various agencies in making this determination are influenced by a variety of factors. Each agency has distinct and separate legislation with which to work. Within these statutory guidelines, however, the agencies are accorded a wide discretion in formulating policy subject only to judicial review. Regulatory commissions have the sole power to approve merger proposals, and it is in these situations, although decided on a case-by-case basis, that policy formulation plays a large role.

The policy articulated by regulatory commissions in their merger decisions is to a large extent dependent on the economic state of the particular regulated sector. Policy can thus change as the financial condition of an industry changes, and the agencies are greatly influenced by the needs of the industry over which they preside. Consolidations have been thought to provide a remedy for a sagging industry; during an economic recession agencies frequently permit mergers which would not be considered in a healthier economy. Regulatory bodies are often persuaded to grant unlikely mergers in order to help a particular com-

the extended El Paso Natural Gas litigation, the Supreme Court struck down an FPC approved merger between El Paso and a pipeline company. The Commission had proceeded to approve the merger while a suit challenging the validity of the transaction under the antitrust laws was pending in a federal court. Section 7 of the Natural Gas Act gave the FPC jurisdiction over the acquisition of assets of natural gas companies leaving to Section 7 of the Clayton Act and the federal courts the control over stock acquisitions. 15 U.S.C. § 717f (1970). Since the case at hand involved a stock acquisition, the Supreme Court held that the Commission should have awaited the court decision before proceeding. The Court further pointed out that approval of the merger in the situation explained above would not bar an antitrust suit challenging the merger. California v. FPC, 369 U.S. 482, 489 (1962). See also United States v. El Paso Natural Gas Co., 291 F. Supp. 3 (D. Utah 1968), vacated sub nom. Utah Pub. Serv. Comm'n v. El Paso Natural Gas Co., 395 U.S. 464 (1969).

Thus, the Federal Power Commission has little regulatory power over certain types of mergers. Antitrust policy is entrusted solely to the courts, in contrast to the situation in the air carrier and rail industries where antitrust policy is entrusted to the regulatory body. Indeed, the Supreme Court in the El Paso case ignored the FPC finding that any lessening of competition by the consolidation was not substantial, pointing out only that the Commission had exceeded its authority. California v. FPC, 369 U.S. 482, 490 (1962).
pany, even in times of relative prosperity, if that company's well-being is considered important to the industry as a whole.

The methods of the Interstate Commerce Commission and the Civil Aeronautics Board have afforded excellent illustrations of the way regulatory agencies operate. For example, the Interstate Commerce Commission was adamant regarding the preservation of competition within the railroad industry during the first decades of this century. Railroads were king with little outside competition, and the Commission was primarily concerned with protecting the many small operators from being consumed by large powerful roads. In contrast, the Commission has reversed its position in recent years due to increasing intermodal competition and the failure of many lines which have severely weakened the industry. Consolidations have been looked to as a cure for the economic woes and as a way for railroads to better compete with the increasingly powerful intermodal competitors. The Commission has approved railroad mergers at such a rate and in such diverse circumstances that it has been suggested that the Commission's present role is but a passive one subject to the wants of the industry.

In contrast to railroads, the air carrier industry has not yet experienced significant intermodal competition. The statutory controls relating to commercial airlines, unlike those relating to railroads, emphasize the preservation of competition as a standard to be applied to consolidations. Railroads are generally considered more of a natural monopoly than are air carriers because of the wasted resources necessary to build parallel tracks and facilities. Competition is more prevalent in the air carrier industry because of lower fixed costs and because the number of airlines on each route can easily be adjusted to changes in the volume of traffic. There are other basic economic differences in the two transportation sectors. For instance railroads must utilize their own resources to provide terminal facilities and roadbeds while the government provides airway facilities, including airports.

The Civil Aeronautics Board has traditionally been concerned with

83. Only intramodal consolidations have been considered, while intermodal transactions, a phenomenon of growing importance in the railroad industry, have been omitted. Regarding the air carrier industry, intermodal mergers are similarly beyond the scope of this article. Moreover, the inquiry was limited to domestic carriers which eliminated consideration of attempted mergers involving international carriers such as Pan American.


maintaining a significant level of competition within the air carrier industry. The industry has a substantially concentrated market structure, dominated by the four largest carriers, but competition among the few is deemed essential.

In respect to merger applications, the Board has consistently opposed any transaction which would strengthen a member of the Big Four, evincing a fear that any more economic power in the Big Four would substantially damage the smaller competitors and create a truly oligopolistic industry. There have been exceptions to this policy. In two instances the Board has permitted a member of the Big Four to merge with a smaller carrier (once with the fifth largest domestic carrier); in both cases the merger was necessary to prevent a financially distressed airline from crumbling. Further, the Board's overall policy regarding mergers has been greatly influenced by the industry's economic condition. Recently, as when the industry suffered a similar decline, the Board has authorized several consolidations in order to strengthen small carriers. In these periods of heavy merger activity, some consolidations are consummated which ordinarily might not be approved. The anti-competitive aspects of the transaction, while not totally ignored, are generally outweighed in such situations by the Board's desire to strengthen either a particular carrier or the industry as a whole.