

**IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION**

UNITED STATES OF AMERICA,)	
)	
Plaintiff,)	
)	
v.)	
)	
NORTHWEST AIRLINES CORPORATION)	
and)	Civil Action No.: 98-74611
CONTINENTAL AIRLINES, INC.,)	
)	
Defendants.)	
)	

AMENDED COMPLAINT

The United States of America, plaintiff, acting under the direction of the Attorney General, brings this civil action to obtain equitable and other relief, including an order directing defendant Northwest Airlines Corporation (“Northwest”) to divest the majority voting interest it has acquired in its competitor, defendant Continental Airlines, Inc. (“Continental”), and adjudicating the agreements pursuant to which Northwest acquired that voting interest to be unlawful under the antitrust laws.

Plaintiff filed its complaint in this action on October 23, 1998, at which time Northwest had not yet acquired a voting interest in Continental. Subsequent to the filing of the complaint, Northwest modified the terms of the final agreements relating to the acquisition -- purportedly to “obviate” the harm to competition alleged by plaintiff in its complaint -- and proceeded to acquire a majority voting interest in Continental. The modifications do not remedy the

anticompetitive effects of the acquisition, and plaintiff therefore files this Amended Complaint, alleging as follows:

1. Northwest is the fourth largest airline in the United States, and Continental is the fifth largest. Both are financially sound, profitable airlines.

2. Northwest and Continental compete on price and service in thousands of routes throughout the United States. They compete for passengers by offering, among other things, promotional fares for leisure travel, frequent flyer rewards, passenger upgrades, airport and in-flight amenities, and volume discounts to businesses and other organizations. They compete against each other in additional areas as well, such as on-time performance, ticketing procedures, schedules, and customer service.

3. Northwest and Continental are each other's most significant competitor for airline passenger service on seven densely traveled routes between cities where they operate their hubs - - Detroit, Memphis, and Minneapolis for Northwest; and Cleveland, Houston, and Newark for Continental. Over 3.6 million passengers travel these seven "hub-to-hub" routes each year, generating nearly \$375 million in passenger revenues. Northwest and Continental are also direct competitors for airline travel between thousands of other cities, and are each other's most important competitor in a significant number of markets they serve on a connecting basis.

4. Northwest has acquired voting control over Continental, as well as a share in Continental's profits. The acquisition diminishes substantially both Northwest's and Continental's incentives to compete against each other on the seven existing hub-to-hub routes, as well as on other routes. Further, it will deter Continental from offering new service in competition with Northwest, such as expansion by Continental of its Cleveland hub.

5. Thus, as a result of Northwest's acquisition of voting control of Continental, consumers likely will pay higher prices and receive lower quality service for scheduled airline passenger service in the markets dominated by Northwest and Continental, and lose the benefit of new, competitive entry by Continental against Northwest.

I.

JURISDICTION AND VENUE

6. This action is instituted pursuant to Section 15 of the Clayton Act, as amended, 15 U.S.C. § 25, and Section 4 of the Sherman Act, 15 U.S.C. § 4, to prevent and restrain violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 1 of the Sherman Act, 15 U.S.C. § 1.

7. A substantial portion of each defendant's revenues is derived from the sale and provision of scheduled airline passenger service between different states. The defendants are engaged in interstate commerce and in activities that substantially affect interstate commerce. The Court has jurisdiction over this action and over the defendants pursuant to Section 12 of the Clayton Act, 15 U.S.C. § 22, and 28 U.S.C. §§ 1331 and 1337.

8. Venue is proper in this district with respect to the defendants under 15 U.S.C. § 22 and 28 U.S.C. § 1391(c), in that each of them is a corporation that transacts business and is found in the Eastern District of Michigan.

II.

DEFENDANTS

9. Defendant Northwest is a corporation organized and existing under the laws of Delaware, with its principal offices in St. Paul, Minnesota. Northwest is the fourth largest airline in the United States, reporting total revenues of \$10.2 billion in 1997.

10. Defendant Continental is a corporation organized and existing under the laws of Delaware, with its principal offices in Houston, Texas. Continental is the fifth largest passenger airline in the United States, with total revenues of \$7.1 billion in 1997.

III.

THE ACQUISITION AND RELATED AGREEMENTS

11. On January 25, 1998, Northwest entered into an agreement with Air Partners, L.P. (“Air Partners”) and certain of its affiliates for the purpose of acquiring over fifty percent of the voting power over Continental (the “Investment Agreement”). On March 2, 1998, Northwest entered into an agreement with Barlow Investors III, LLC to purchase approximately 5 percent of the voting power over Continental (the “Barlow Purchase Agreement”) to ensure Northwest would own over 50 percent of the fully diluted voting power over Continental.

12. Northwest and Air Partners amended the Investment Agreement on March 2, 1998, April 24, 1998 and November 20, 1998. Pursuant to the November 20, 1998 amendment, the percentage of voting power Northwest was to acquire from Air Partners was reduced to about 46 percent. Notwithstanding the November 20, 1998 amendment to the Investment Agreement, the Barlow Purchase Agreement ensured that Northwest would own more than 50 percent of the

fully diluted voting power over Continental. Northwest consummated the Investment Agreement and the Barlow Purchase Agreement on November 20, 1998.

13. Under both the Investment Agreement and the Barlow Purchase Agreement, Northwest bargained for and obtained Continental Class A Shares, which carry super-voting rights.

14. As Class A stock, the shares purchased by Northwest from Air Partners and Barlow represent about 14 percent and 1 percent, respectively, of the total outstanding equity of Continental, but carry 46 percent and 5 percent, respectively, of the voting power over Continental.

15. Between entering the Investment Agreement on January 25, 1998, and the closing of the Investment and Barlow Purchase Agreements on November 20, 1998, Northwest, Continental and Air Partners entered into various agreements and adopted various plans that purport to govern how Northwest will exercise its voting control over Continental during the next ten years. These agreements and plans include the Governance Agreement (and its amendments), the Supplemental Agreement, the Voting Trust Agreement, and a shareholders' rights agreement (hereinafter collectively referred to as the "Governance Agreements").

16. Notwithstanding the Governance Agreements, Northwest now owns, and will continue to own, voting control of Continental. The Governance Agreements allow Northwest to retain at all times an ability to influence Continental's management decisions -- such as through discussions with Continental directors, officers and employees, comments about Continental's performance or management, or merely the ownership of Continental stock -- and eventually to exercise full control over Continental.

17. The Governance Agreements do not divest Northwest of ownership of its Continental stock. Rather, they merely impose certain restrictions on Northwest's exercise of its voting control during the first six years of its ownership of Continental and different, less restrictive, limitations on that exercise of voting control during years seven through ten. Northwest and Continental can agree privately at any time to eliminate any or all of these restrictions; in any event, all contractual limitations on Northwest's exercise of control over Continental expire no later than the tenth anniversary of the acquisition.

18. Under the Governance Agreements, Northwest retains its ownership of over 50 percent of the voting power over Continental and significant rights in and influence over Continental during the first six years of its ownership of Continental, including inter alia:

- a. Northwest is free to direct the voting power of all its stock on key decisions that affect the future competitiveness of Continental, including major stock issuances, mergers, reorganizations, share exchanges, consolidations, or business combinations of Continental, as well as the sale of all or substantially all of Continental assets to any other company;
- b. No other shareholder can acquire voting control of Continental without the acquiescence of Northwest;
- c. In contested elections for the board of directors of Continental, Northwest can direct the vote of its controlling shares in support of the incumbent board's recommendations;
- d. In all elections for the board of directors of Continental, Northwest can register a public vote of no confidence in Continental management by

directing its vote against certain directors, including Continental managers seeking election or re-election to the board;

- e. In addition to the approximately 51 percent of the voting power of Continental it owns, Northwest has the right to direct the vote of certain additional shares owned by 1998 CAI Partners, L.P. (“CAIP”). The CAIP shares represent approximately 5 percent of the voting power over Continental. The CAIP shares must be voted as directed by Northwest on key matters such as mergers and changes to Continental’s by-laws. Northwest also can direct that the CAIP shares be voted as recommended by Continental’s board in the election of directors, if that is how Northwest chooses to vote its own shares.

19. In addition to the rights that it retains during the first six years of its ownership of voting control over Continental, Northwest obtains even greater rights and influence under the Governance Agreements during years seven through ten of its ownership:

- a. Northwest can vote 20 percent of the voting power of Continental on any issue presented to shareholders, including executive compensation;
- b. Northwest can nominate, solicit support for, and vote for its own representatives to serve on Continental’s board of directors.

20. When the Governance Agreements expire, Northwest can fully exercise its voting control over Continental.

21. As a result of the Investment Agreement, the former owners of Air Partners hold voting shares of Northwest. The Investment Agreement grants these former Air Partners owners,

through Coulco, Inc., the right to designate one individual to sit on the board of Northwest. Coulco is owned by James Coulter who, together with David Bonderman, controlled the general partner in Air Partners. The Investment Agreement requires that the Coulco designee be acceptable to Northwest, and the agreement identifies James Coulter and William S. Price as acceptable designees.

22. The Investment Agreement is likely to create interlocking directors on the boards of directors of Northwest and Continental. William S. Price currently sits on the Continental board, and if he is elected to the Northwest board, the two airlines will have a common director. In addition to Price, three other individuals formerly affiliated with Air Partners currently sit on the Continental board: David Bonderman, Thomas Barrack, and Donald Sturm. Former Air Partners owners retain through CAIP about 5 percent of the voting power of Continental. If Coulter, Price, or any other person formerly affiliated with Air Partners is designated to the Northwest board, the former Air Partners owners will have representatives on the boards of both Northwest and Continental.

23. Northwest and Continental also have entered into an alliance agreement (the “Alliance Agreement”), which provides for system-wide joint marketing of the two carriers’ services. Consummation of the Alliance Agreement is not contingent upon consummation of the Investment Agreement. Although such alliance agreements between airlines have become common in recent years, it is uncommon for such alliances to be accompanied by substantial equity ownership. Few, if any, have involved a majority interest. Both Northwest and Continental have alliances with other domestic and foreign carriers, but none involves voting control by one partner of the other.

IV.

THE RELEVANT MARKETS

24. For the vast majority of passengers who wish to travel between various origin and destination (“O&D”) airports or cities in the United States, there is no other mode of transportation they would substitute for scheduled airline passenger service in response to a significant fare increase for scheduled airline passenger service. Scheduled airline passenger service, therefore, constitutes a line of commerce and a relevant product market within the meaning of Section 7 of the Clayton Act, and within the meaning of Section 1 of the Sherman Act.

25. Few passengers currently flying nonstop between specific O&D airports or cities in the United States would substitute connecting service (i.e., flights with one or more stops en route) for nonstop service in response to a significant fare increase for nonstop scheduled airline passenger service. Nonstop scheduled airline passenger service, therefore, constitutes a line of commerce and a relevant product market within the meaning of Section 7 of the Clayton Act, and within the meaning of Section 1 of the Sherman Act.

26. With respect to both scheduled airline passenger service and nonstop scheduled airline passenger service, few passengers who wish to fly between specific O&D airports or cities in the United States would switch to flights between other airports or cities in response to a significant fare increase. Specific O&D airports or cities (“city pairs”), therefore, constitute a section of the country and a relevant geographic market with the meaning of Section 7 of the Clayton Act, and within the meaning of Section 1 of the Sherman Act.

V.

CONCENTRATION AND ENTRY

27. Northwest and Continental are among the ten largest airlines in the world. Within the United States, Northwest and Continental compete for passengers in thousands of city-pair markets.

28. Northwest operates hubs at airports in Detroit, Michigan; Minneapolis/St. Paul, Minnesota; and Memphis, Tennessee.

29. Continental operates hubs at airports in Newark, New Jersey; Cleveland, Ohio; and Houston, Texas.

30. Under the “hub and spoke” system, an airline concentrates passengers from many points at the “hub” location and then provides nonstop service from the hub airport to a large number of destinations (the “spokes”). The hub and spoke system allows a carrier to serve more city pairs with more frequencies than would be profitable without the use of a hub.

31. In seven hub-to-hub city pair markets, Northwest and Continental together dominate the market for nonstop service and for all scheduled airline passenger service. These markets are Detroit-Cleveland, Detroit-New York (including Newark), Detroit-Houston, Cleveland-Minneapolis, Minneapolis-New York (including Newark), Houston-Minneapolis, and Houston-Memphis. Northwest and Continental’s market shares for nonstop flights in each of the seven markets are:

Northwest/Continental Hub-to-Hub Nonstop Shares

Route	NW Share of Nonstop Flights	CO Share of Nonstop Flights	Combined NW & CO Share of Nonstop Flights
Detroit-Cleveland	52%	41%	93%
Detroit-New York	69%	14%	83%
Detroit-Houston	36%	64%	100%
Cleveland-Minneapolis	53%	47%	100%
Minneapolis-New York	80%	20%	100%
Houston-Minneapolis	42%	58%	100%
Houston-Memphis	39%	61%	100%

32. In two other hub-to-hub routes, Memphis-Newark and Cleveland-Memphis, Northwest currently has a nonstop monopoly. As the only airline with hubs in Newark and Cleveland, Continental is the most likely potential entrant to challenge Northwest's nonstop monopoly. After plaintiff's complaint was filed, Continental announced it would begin nonstop service on the Memphis-Newark route beginning in February 1999.

33. In total, nearly four million passengers travel in these nine hub-to-hub city pairs annually, generating revenues of nearly \$400 million per year.

34. Effective new entry for the provision of nonstop service in the hub-to-hub markets is unlikely by any carrier without a hub at one of the endpoints of the city pair. A hub carrier, such as Northwest or Continental, has significant cost advantages over a non-hub carrier attempting to offer service originating at the hub airport. Building a competing hub in the same city would require considerable time and investment, and is not likely to occur in response to fare increases in the hub-to-hub markets at issue here.

35. Other factors impede new entry, including difficulty in obtaining access to gate facilities; the effects of travel agent incentive programs offered by dominant incumbents; frequent flyer programs; and the risk of aggressive responses to new entry by the dominant incumbent carrier serving a particular market.

36. In addition to the hub-to-hub routes where Northwest and Continental share a virtual duopoly, Northwest and Continental have a large share of the passengers traveling on connecting flights in numerous city pair markets. Because of the light traffic on these routes and the short flights to the Northwest or Continental hubs, carriers with more distant hubs are unlikely to initiate or expand competitive service to these destinations through their own hubs in response to significant fare increases.

VI.

ANTICOMPETITIVE EFFECTS

37. Northwest's ownership of a controlling interest in Continental will reduce Continental's incentive to compete aggressively against Northwest. Furthermore, Northwest's more than fourteen percent equity stake in Continental's profits, plus its ability to merge in the future with Continental, will reduce Northwest's incentive to compete aggressively against Continental.

38. Northwest's ownership of a controlling interest in Continental will diminish actual competition in seven hub-to-hub markets and numerous other markets that already are concentrated. It also will diminish the potential for nonstop competition for Memphis-Cleveland and Memphis-Newark, as well as potential competition in other markets for which Northwest

and Continental are among the few likely future providers of scheduled airline passenger service. As a result, fares likely will increase and service likely will decrease in these city pairs.

39. Northwest's ownership of a controlling interest in Continental also will reduce the likelihood that Continental will initiate nonstop service from its hubs, such as Cleveland, to cities already served by Northwest through its hubs, such as Detroit.

40. The Governance Agreements do not prevent the harm likely to result from Northwest's ownership of a controlling interest in Continental. First, no privately negotiated agreement can alter the fact that Northwest retains ownership of its Continental stock, and Continental will not compete vigorously with its owner during the terms of the Governance Agreements. Second, even under the Governance Agreements, Northwest (a) may engage in "discussions with directors, officers and employees" of Continental; (b) retains direct control over key Continental strategic decisions at all times; and (c) retains significant influence over Continental's board of directors and management.

41. Northwest's ability to exercise the direct control attendant to its ownership interests increases in years seven through ten following the acquisition, even if the Governance Agreements remain in place. Those agreements may expire earlier by their own terms and, like all agreements between two parties, the Governance Agreements can be amended or revoked at any time by the parties -- Continental and its competitor and new owner, Northwest.

VII.

VIOLATIONS ALLEGED

42. The effect of Northwest's ownership of voting power over Continental may be substantially to lessen competition in interstate trade and commerce in violation of Section 7 of the Clayton Act, and to unreasonably restrain trade in violation of Section 1 of the Sherman Act in the following ways, among others:

- a. Actual and potential competition between Northwest and Continental for nonstop scheduled airline passenger service in the hub-to-hub markets will be reduced or eliminated;
- b. Actual and potential competition between Northwest and Continental for scheduled airline passenger service in city-pair markets where Northwest and Continental are dominant providers of connecting service will be reduced or eliminated;
- c. Competition generally in numerous city-pair markets for scheduled airline passenger service may be lessened substantially;
- d. Coordinated pricing activity between providers of scheduled airline passenger service likely will be facilitated; and
- e. Prices for scheduled airline passenger service in numerous concentrated city-pair markets in the United States are likely to increase.

IX.

REQUEST FOR RELIEF

WHEREFORE, Plaintiff prays:

1. That a permanent injunction be issued preventing and restraining defendant Northwest and all persons acting on its behalf from owning or holding voting stock in Continental, or any of Continental's affiliates or subsidiaries, and directing that Northwest divest promptly all voting stock in Continental on such terms and conditions as may be agreed to by plaintiff and the Court;
2. That the Investment Agreement between Northwest and Air Partners and the Barlow Purchase Agreement between Northwest and Barlow be adjudged to be in violation of Section 7 of the Clayton Act, 15 U.S.C. § 18, and Section 1 of the Sherman Act, 15 U.S.C. § 1;
3. That plaintiff have such other and further relief as the nature of this case may require and as is just and proper, including modifications to the Governance Agreements between Northwest, Continental and Air Partners as appropriate; and
4. That Plaintiff recover the costs of this action.

DATED this 18th day of December 1998.

"/s/"
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Assistant Attorney General

"/s/"
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"/s/"
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