



UNITED STATES OF AMERICA
DEPARTMENT OF TRANSPORTATION
OFFICE OF THE SECRETARY
WASHINGTON, D.C.

Issued by the Department of Transportation
on the 18th day of May, 2007

Application of

VIRGIN AMERICA INC.

for a certificate of public convenience and necessity
under 49 U.S.C. § 41102 to engage in interstate
scheduled air transportation of persons, property, and
mail

Docket OST-2005-23307

FINAL ORDER

Summary

By this order, we (1) find that, subject to conditions, Virgin America Inc. (“Virgin America”), will be a citizen of the United States and will be fit, willing, and able to engage in interstate scheduled air transportation of persons, property, and mail, and (2) issue to it a certificate of public convenience and necessity authorizing such transportation, subject to conditions.

Background

By Order 2006-12-13, issued December 27, 2006, the Department tentatively found that Virgin America had failed to establish that it was a U.S. citizen and that it would be owned by and remain under the actual control of U.S. citizens. In response to that finding, Virgin America filed a substantially revised application proposing material changes in its financial arrangements, its management, and its corporate governance. Based on these changes and additional conditions proposed by the Department, by Order 2007-3-16, issued March 20, 2007, the Department tentatively found the applicant fit to operate and that it would be a U.S. citizen. At that time, we directed all interested persons to show cause why we should not make final our tentative findings and conclusions and award to Virgin America a certificate of public convenience and necessity, authorizing it to engage in interstate scheduled air transportation of persons, property and mail. Interested persons were given 21 calendar days to file objections.

Responsive Pleadings

On April 10, 2007, Virgin America filed a responsive document in the record of this case. The applicant agreed to implement the changes it had earlier proposed with respect to, among other

things, its ownership structure, financial arrangements, and corporate governance,¹ and the conditions proposed by the Department in Order 2007-3-16, with the exception of the condition requiring the removal of Mr. Frederick Reid, Virgin America's Chief Executive Officer ("CEO"), within 90 days of the issuance of a Final Order, and termination of any subsequent consultancy within 180 days thereafter.² Specifically, Virgin America argued that, in light of the substantial changes it has agreed to make to address the Department's citizenship concerns, "this proposed condition is unnecessary and inappropriate in light of the now radically altered 'totality of the circumstances.'"³ In the alternative, Virgin America requested that the Department, should it continue to consider this condition necessary, amend the condition to allow Mr. Reid to remain as CEO



By letter dated April 10, 2007, the Association of Flight Attendants-CWA ("AFA-CWA") stated its intention to file an objection by April 19.

On April 12, 2007, Virgin America filed a motion asking the Department to strike or otherwise preclude consideration of AFA-CWA's April 10, 2007, letter, as well as any subsequent pleadings filed by AFA-CWA. Virgin America argued that the AFA-CWA had neither met the deadline for the filing of objections established by Order 2007-3-16 nor established good cause as to why untimely objections should be entertained by the Department.

On April 20, 2007, AFA-CWA filed an answer in opposition to the positions asserted by Virgin America, along with a contingent motion for leave to file an otherwise unauthorized document, which we will grant.⁵ AFA-CWA argues that the applicant does not satisfy the Department's citizenship requirements and that therefore the Department should deny its application. AFA-CWA believes that the formation of Virgin America advances the commercial interests of a foreign national who also controls foreign air carriers with which U.S. airlines compete. AFA-CWA maintains that nothing about the restructured affairs of Virgin America supports the Department's March 20, 2007, tentative findings, arguing that the Virgin Group has done very little to cede its "domination" over Virgin America's affairs in matters that it has actually sought to control.

In support of its position, AFA-CWA maintains that the totality of circumstances has not changed. It states that the Department correctly concluded, in its December tentative decision,⁶ that the applicant is owned and controlled by non-U.S. citizens, given the substantial involvement of the Virgin Group, a non-U.S. entity, in the company's management personnel; its pervasive involvement in the creation of the company; the various funding agreements; and its contractual arrangements, including the trademark licensing agreement. AFA-CWA also

¹ Objection of Virgin America, dated January 17, 2007, at 12-16 (summary chart).

² See Order 2007-3-16, at 2 and 53.

³ Comments of Virgin America, filed April 10, 2007, at 5-6.

⁴ Id., at 15.

⁵ On April 23, 2007, AFA-CWA submitted a corrected version of its submission.

⁶ See Order 2006-12-23, issued December 27, 2006,

maintains that the voting trust does not sufficiently insulate the company from Virgin Group control. Moreover, AFA-CWA asserts that the changes proposed by Virgin America to address the Department's citizenship concerns raised in our December order do not rid the applicant of the Virgin Group's ability to exert control over the company, thus transforming Virgin America into a U.S. citizen. AFA-CWA urges the Department not to finalize the tentative findings made in Order 2007-3-16.

On April 20, 2007, the applicant filed an answer to AFA-CWA's motion and answer, restating its earlier argument that AFA-CWA failed to comply with the procedural schedule established in Order 2007-3-16, and that it did not show good cause for its filing. Consequently, Virgin America asked the Department to deny AFA-CWA's motion and proceed to the issuance of Virgin America's certificate authority.

On April 30, 2007, Air Gumbo, Inc. ("Air Gumbo"), a Louisiana enterprise that is not engaged in air transportation, filed a motion supporting the Department's proposed condition regarding the term of Mr. Reid's employment with the applicant. In its motion, Air Gumbo argues that to "allow Virgin America to retain Mr. Reid would clearly contradict the citizenship requirement"⁷ and that "Virgin America claiming that its strategic survival depends on Mr. Reid serving as CEO, or in any other employment capacity, implies that a fiduciary relationship between Mr. Reid and Sir Branson will always be vital."⁸

Decision

Based on the record of this case, we here confirm and make final our tentative findings in Order 2007-3-16. Specifically, we find that Virgin America will be a U.S. citizen and will be fit, willing, and able to engage in interstate scheduled passenger air transportation, following implementation of conditions as set forth in this order and in Appendix A.

With respect to AFA-CWA's submission regarding Virgin America's citizenship, the arguments raised by AFA-CWA were raised by the interested parties, considered, and addressed comprehensively in the course of this case prior to the Department's issuance of the tentative fitness determination in Order 2007-3-16. As stated in that order, the Department's tentative findings were based on the totality of the circumstances, which changed as a result of the material changes Virgin America proposed to implement to its financial arrangements, its management, and corporate governance, as well as the numerous conditions the Department stipulated that the applicant must fulfill to have its certificate authority made effective.

AFA-CWA argues that Virgin America would not exist today as an applicant in the absence of the substantial financial support of the Virgin Group. We agree that the Virgin Group has provided the impetus for its formation and provided financial support for the applicant's start-up. We did include those circumstances in our review of the totality the foreign interest's involvement and on whether Virgin America eliminated the Virgin Group's ability to control the airline by, among other things, amendments to the various corporate instruments, and whether or

⁷ Motion of Air Gumbo, dated April 30, 2007, at 1. We will treat the motion of Air Gumbo as a motion to file an unauthorized pleadings, and will grant it.

⁸ *Id.*, at 2.

to what degree the remaining provisions in the debt agreement operate to turn the Virgin Group's loans into more than a passive investment.⁹ Based on our review, we tentatively found that, together with other required changes, Virgin America had revised its loan agreements with the Virgin Group to eliminate certain provisions and, as a result, the Virgin Group's non-voting debt investment did not create a control problem.¹⁰ AFA-CWA has presented no new argument to persuade us to change our tentative finding.

AFA-CWA also argues that the trademark licensing agreement is a means by which the foreign investors can unlawfully enter the U.S. domestic market. It states that the only way to assure that these types of arrangements are properly balanced is to enforce the requirement of arms-length bargaining and independence of action. We see merit to this argument, but find that our tentative determinations in this matter sufficiently address these concerns. Specifically, in Order 2007-3-16, we proposed to condition certification of the applicant on modification of the License Agreement so as to permit *any* operations (including code sharing)—even in direct competition with Virgin Atlantic—so long as the applicant does not use the “Virgin” name in those operations. We also proposed to condition certification of the applicant on a modification of the license such that the applicant's operations are unrestricted, *except* in certain limited respects such as operations that use the Virgin mark. Moreover, we saw no reason why the applicant's operations outside of the license should be subject to a royalty obligation to the Virgin Group. Payment of “royalties” on revenues not derived from use of the brand name would undermine the applicant's independence; therefore, we proposed to condition the applicant's certificate on an amendment to the license that allows such activities to occur without royalty obligation. We continue to believe that our condition, along with the other changes that Virgin America had agreed to make to the trademark licensing agreement, eliminates any concern about the trademark agreement as an element of control in this case.

AFA-CWA maintains that Virgin America's proposed voting trust does not insulate the foreign investors from exerting control over the applicant. We disagree. The purpose of the voting trust, in this case, is to neutralize or mitigate the potential foreign control the Virgin Group might otherwise be in a position to exert over Virgin America through its overall equity interest, which complies with the numerical ownership limit. Under these circumstances, we tentatively found that the voting trust proposed by the applicant to govern the voting interests and the governance rights of the Virgin Group, in addition to the conditions we proposed throughout our show-cause order, should mitigate issues regarding the Virgin Group's control over the applicant through its equity investment. AFA-CWA has not presented arguments to persuade us otherwise.

AFA-CWA argues that the Virgin Group has substantial involvement in the company's management personnel. The Department agreed. However, the applicant offered to (1) replace Mr. Frederick Reid as CEO; (2) remove or replace any officer that the DOT required; (3) permanently relinquish one of the Virgin Group's Board designees (from three to two); and (4) amend its by-laws and Subscription and Stockholders Agreements to remove certain voting powers of representatives of non-U.S. interests. We also tentatively found that ratification of the rest of the company's non-Virgin Group directors would facilitate assurance that control over the company would be with U.S. citizens. Moreover, to lessen further the possibility that the Virgin

⁹ See Order 2007-3-16, issued March 20, 2007, at 55.

¹⁰ Id., at 55.

Group would accomplish indirectly what it could not accomplish directly, we proposed to condition the effectiveness of the applicant's authority upon the removal of the Virgin Group's right [REDACTED]. Finally, we tentatively found that, because VAI itself was not a citizen, those members of the Board that VAI had approved were not U.S. citizens under our precedent. Therefore, we determined that, once VAI had been restructured so as to "wall off" the interests of foreign citizen investors in the various investment vehicles controlling VAI, we would require it to formally re-approve the Board. We tentatively found these conditions sufficient to address our concerns about the company's management. We continue to believe that these changes and condition enable VAI to meet the statutory citizenship requirement.

Finally, Virgin America has asked the Department to either remove in its entirety or amend our proposed condition regarding Mr. Reid's employment with the company. Air Gumbo supports our tentative finding that Virgin America must terminate Mr. Reid's employment. We agree that such a condition is necessary to ensure that U.S. citizens will control Virgin America. We find that Virgin America's replacement of Mr. Reid as CEO and board member with a U.S. citizen who has no prior affiliation with the Virgin Group would, with the other VAM changes and implementation of our proposed conditions, remedy our concerns over the independence of the applicant's management from the Virgin Group. We recognize and are mindful, however, that the replacement of a company's CEO is difficult. For this reason, we have decided to condition certification of Virgin America on Mr. Reid's replacement as CEO no later than six months after the issuance of a Final Order. Moreover, if the company wishes to retain him as a consultant to facilitate further an orderly transition, we would permit Mr. Reid to remain as a consultant for up to three months following his replacement as CEO. Mr. Reid's total transitional period will thus remain no more than nine months, as originally proposed in our Order to Show Cause.

Because no new arguments have been presented to convince us that our tentative findings in Order 2007-3-16 should not be made final, we find that Virgin America will meet our citizenship requirements.

ACCORDINGLY:

1. We find that, subject to conditions, Virgin America Inc., will be fit, willing, and able to engage in interstate scheduled air transportation of persons, property and mail.
2. We issue a certificate of public convenience and necessity to Virgin America Inc., to engage in interstate scheduled passenger air transportation in the form and subject to the Terms, Conditions, and Limitations attached and specified in Appendix A.
3. We grant the April 20 and April 30, 2007, Motions filed by the Association of Flight Attendants-CWA and Air Gumbo, Inc., respectively.
4. We direct Virgin America, Inc. to notify the Department should the Virgin Group acquire additional equity interest in Virgin America, indicating through the conversion of the notes or the exercise of the warrants, consistent with 14 CFR Part 204, and of any decision by the disinterested directors to repurchase any of the Class H Common Shares.

5. Should Virgin America Inc., propose to operate more than 17 aircraft, we direct it to notify the Department in writing at least 45 days prior to the proposed operation and demonstrate its fitness to conduct such operations before their commencement.

6. We direct Virgin America, Inc. to submit to the Air Carrier Fitness Division a first year progress report within 45 days following the end of its first year of certificated operations.¹¹

7. We will serve a copy of this order on all interested parties.

By:

ANDREW B. STEINBERG
Assistant Secretary for Aviation
and International Affairs

*An electronic version of this document is available on the World Wide Web at:
<http://dms.dot.gov/search>*

¹¹ The report shall include a description of the air carrier's current operations (number and type of aircraft, principal markets served, total number of full-time and part-time employees), a summary of how these operations have changed during the year, a discussion of any changes it anticipates from its current operations during its second year, current financial statements, and a listing of current senior management and key technical personnel. The air carrier should also be prepared to meet with staff members of the Fitness Division to discuss its current and future operations.



Certificate of Public Convenience and Necessity for Interstate Air Transportation

This Certifies That

VIRGIN AMERICA INC.

is authorized, subject to the provisions of Subtitle VII of Title 49 of United States Code, the orders, rules, and regulations issued thereunder, and the attached Terms, Conditions, and Limitations, to engage in interstate air transportation of persons, property, and mail.

This Certificate is not transferable without the approval of the Department of Transportation.

By Direction of the Secretary

*Issued by Order 2007-5-11
On May 18, 2007
Effective on (see attached)*

*Andrew B. Steinberg
Assistant Secretary for
Aviation and International Affairs*



Terms, Conditions, and Limitations

VIRGIN AMERICA INC.

is authorized to engage in interstate air transportation of persons, property, and mail between any point in any State, territory, or possession of the United States or the District of Columbia, and any other point in any of those entities.

This authority is subject to the following provisions:

(1) *The authority to operate under this certificate will not become effective until the Department has determined that the holder has satisfactorily met the conditions specified herein and in Appendix A of this order.*

(2) *Pending receipt of effective authority, the holder may not accept payment of any kind (i.e., cash, check, or credit card) or issue tickets for the operations proposed under this certificate, and any advertisement or listing of flights by the holder must prominently state: "This service is subject to receipt of government operating authority."*

(3) *The holder shall at all times conduct its operations in accordance with the regulations prescribed by the Department of Transportation for the services authorized by this certificate, and with such other reasonable terms, conditions, and limitations as the Department of Transportation may prescribe in the public interest.*

(4) *The holder's authority under this certificate is effective only to the extent that such operations are also authorized by the Federal Aviation Administration (FAA), and comply with all U.S. Government requirements concerning security, including, but not limited to 49 CFR Part 1544.**

(5) *The holder shall at all times remain a "Citizen of the United States" as required by 49 U.S.C. 40102(a)(15).*

(6) *The holder shall maintain in effect liability insurance coverage as required under 14 CFR Part 205. Failure to maintain such insurance coverage will render a certificate ineffective, and this or other failure to comply with the provisions of Subtitle VII of Title 49 of the United States Code or the Department's regulations shall be sufficient grounds to revoke this certificate.*

** To assure compliance with all applicable U.S. Government requirements concerning security, the holder shall, before commencing any new service (including charter flights) to or from a foreign airport, contact its Principal Security Inspector (PSI) to advise the PSI of its plans and to find out whether the Transportation Security Administration has determined that security is adequate to allow such airport(s) to be served.*

(7) *The holder is authorized to conduct charter flights in interstate and/or foreign air transportation in accordance with the provisions of 14 CFR 212.*

(8) *In the event that the holder receives effective scheduled passenger authority, the following additional conditions will apply:*

(a) *The holder may reduce or terminate service at any point or between any two points, subject to compliance with the provisions of 49 U.S.C. 41734 and all orders and regulations issued by the Department of Transportation under that section.*

(b) *The holder may not provide scheduled passenger air transportation to or from Dallas (Love Field), Texas, except within the limits set forth in section 29 of the International Air Transportation Competition Act of 1979, as amended or as modified by any future legislation addressing access restrictions to or from Love Field.*

(9) *Should the holder propose any substantial change in its ownership, management, or operations (as defined in 14 CFR 204.2(l)), it must first comply with the requirements of 14 CFR 204.5.*

(10) *In the event that the holder does not commence actual flying operations under this certificate within one year of the date of the Department's determination of its fitness, its authority shall be revoked for dormancy, unless the holder is conducting operations under another type of certificate authority. Further, in the event that the holder commences operations for which it was found "fit, willing, and able" and subsequently ceases all such operations, its authority under all certificates held shall be suspended under the terms of 14 CFR 204.7 and the holder may neither recommence nor advertise such operations unless its fitness to do so has been redetermined by the Department. Moreover, if the holder does not resume operations within one year of its cessation, its authority shall be revoked for dormancy.*

CONDITIONS TO VIRGIN AMERICA INC.'S EFFECTIVE AUTHORITY

Virgin America's certificate authority will be made effective when it has submitted in a form satisfactory to DOT:

1. Signed documents demonstrating and certifying that:
 - a. Virgin America has completed its second financial closing.
 - b. Each of its U.S. investor entities has created a separate fund or class of interest that effectively excludes participation by non-U.S. citizens in VAI. This documentation shall include:
 - i. A showing that all non-U.S. investors have been effectively walled off from investing in, and participating in, any proceeds from VAI or Virgin America;
 - ii. Citizenship information for all investors demonstrating compliance with 49 U.S.C. §40102(a)(15);
 - iii. A diagram detailing VAI's ownership structure and information regarding the nationality and percentage of foreign investment in VAI and its owners.
 - c. Virgin America has re-appointed its Board of Directors after VAI restructured its ownership.
 - d. Virgin America has satisfactorily amended its employment contract with Mr. Frederick Reid, the company's Chief Executive Officer ("CEO"), providing for the termination of his employment with the company as CEO within 180 days of the issuance of this order. In the event that Virgin America should decide to retain Mr. Frederick Reid as a consultant for up to three months following his termination as CEO, the applicant will have to provide to the Department a copy of his employment contract that specifically identifies his position and responsibilities as that of a consultant and that specifically limits his term as a consultant to a period not to exceed three months.
2. A copy of all signed and executed documents and/or agreements related to the:
 - a. Reduction of the Virgin Group's representation on Virgin America's Board of Directors.
 - b. Termination of the Virgin Group's special voting powers and its right [REDACTED] including the company's Bylaws and Subscription and Stockholders' Agreements.
 - c. Removal of the following restrictions and covenants included in the Interim Note and Subordinate Note Agreements, the Senior Secured Promissory Notes and the Senior Secured Promissory Notes, Series B, and the Security Agreement:
 - i. Restrictions related to the payment of dividends, the incurrence of senior indebtedness, and the making of a fundamental change to Virgin America's business;

- ii. Restrictions related to the incurrence of certain senior indebtedness, the transfer of certain assets of Virgin America, the maintenance of Virgin America's corporate restriction, and the notification of events or defaults or other defaults; and
 - iii. Covenants related to material Virgin America contracts.
 - d. Issuance of the new Class H Common Stock, including an Amended Stockholders Agreement, an Amended Certificate of Incorporation, and a new Subscription Agreement.
 - e. Additional financing from the Virgin Group and Virgin America's U.S. Investors.
- 3. A copy of the following signed and executed agreements:
 - a. Trademark License Agreement that includes provisions that expressly permit:
 - i. The company to conduct *any* operations (including code sharing), even in direct competition with Virgin Atlantic and without any royalty obligations to the Virgin Group, so long as the company does not use the "Virgin" name in those operations; and
 - ii. Virgin America to conduct operations that use the Virgin mark, *except* in certain limited respects.
 - b. Voting Trust Agreement that will govern the Virgin Group's equity interest in Virgin America that include the following conditions:
 - i. The U.S. members (*i.e.*, the disinterested parties) of Virgin America's Board of Directors must confirm the nomination and the removal of the Voting Trustee;
 - ii. Any change in the Voting Trustee must be reported to the Department; and
 - iii. Should the majority of the Board directors appointed by the U.S. investors determine that the interests of the Virgin Group as a shareholder in a matter subject to shareholder approval potentially conflict with those of the other shareholders, the trustee will vote proportionately to the non-Virgin Group shareholders.
- 4. The following documents:
 - a. A copy of the holder's Air Carrier Certificate and Operations Specifications authorizing such operations from the Federal Aviation Administration (FAA);
 - b. A certificate of insurance on OST Form 6410 evidencing liability insurance coverage meeting the requirements of 14 CFR 205.5(b) for all of its aircraft;
 - c. A statement of any changes the holder has undergone in its ownership, key personnel, operating plans, financial posture, or compliance history, since the date of the Show Cause Order in this case; and
 - d. A revised list of pre-operating expenses already paid and those remaining to be paid, as well as independent verification that the holder has available to it funds sufficient to cover any remaining pre-operating expenses and to provide a working capital reserve equal to the operating costs that would be incurred in three months of operations.

5. Documentation showing any amendments and the dates these amendments were made to Virgin America's aircraft lease agreements.
6. A sworn certificate that Virgin America's current management, with the exception of Mr. Frederick Reid, has been ratified by the company's non-Virgin Group directors.
7. Evidence that the Virgin Group's stock has been placed in the voting trust.
8. The name, qualifications, compliance history, and citizenship of the Voting Trustee.