

ALERT



November 2007

Mesa Air Ordered to Pay \$80 Million for Misusing Confidential Investment Material Obtained in Hawaiian Airlines Chapter 11 Case

On October 30, 2007, U.S. Bankruptcy Judge Robert J. Faris ordered Mesa Air Group, the parent company of the inter-island airline, “go!,” to pay Hawaiian Airlines \$80 million in damages for breach of a confidentiality agreement. The Court found that Mesa created go! last year using confidential information received as a potential investor in Hawaiian Airlines, a chapter 11 debtor. The Court also found that Mesa’s chief financial officer intentionally and in bad faith destroyed relevant evidence after being told to preserve the evidence for the lawsuit. Representing approximately one-third of Mesa’s cash, cash equivalents and marketable securities, the judgment comes at a significant cost and serves as an important reminder of the need to avoid misuse of confidential information.

Factual Background

Hawaiian Airlines commenced its chapter 11 case on March 21, 2003. During the case, as part of a sale process to solicit investments to fund a plan of reorganization, Hawaiian sent a “teaser” to about 50 potential investors. Parties expressing interest received additional documents and access to a secure electronic database, subject to execution of a confidentiality agreement. Mesa was one of the prospective investors that participated in the sale process, and Mesa’s CFO, on behalf of Mesa, signed a confidentiality agreement, accessed the electronic database and downloaded numerous documents.

Mesa ultimately did not enter into the proposed investment in Hawaiian. Instead, Mesa started its own Hawaiian inter-island airline, go!. On February 13, 2006, Hawaiian filed a complaint alleging that Mesa breached its confidentiality agreement by failing to return or destroy confidential information and by misusing that information in creating go! in direct competition with Hawaiian.

The day after the complaint was filed, Mesa’s counsel advised Mesa’s top three officers, including Mesa’s CFO, to “preserve any and all documents that may be related to the matters set forth in the Complaint, including emails, electronic documents, notes, models, etc.” After receiving this advice, and as the litigation was pending, Mesa’s CFO deleted files on his two laptop computers, using a program that rendered the deleted files unrecoverable and deleted certain files from Mesa’s network “H drive.” He also changed the system clock on his computers in an attempt to make it appear that he had deleted the files before Hawaiian filed the complaint.

Bankruptcy Court Ruling

The Court found that Mesa retained Hawaiian's confidential information and did not return or destroy it as the confidentiality agreement required. The Court also found that Mesa misused the confidential information to gain a competitive advantage by entering into the market for Hawaiian inter-island air transportation services. The Court also found that the CFO destroyed potential evidence intentionally and in bad faith. As a result, the Court held that Mesa, as the CFO's employer, was accountable for that misconduct.

Mesa still claimed that it should bear no liability, because the information at issue was publicly available and therefore not in fact confidential. The Court disagreed and separately found that a significant portion of the information — such as figures detailing the profitability of local routes and Hawaii-U.S. mainland routes, passenger profiles and expansion plans — was never made publicly available.

Based on its ruling, the Court awarded Hawaiian \$80 million in damages to compensate it for the reduced revenue and increased costs it incurred when go! entered the market and

introduced lower fares and expanded flight schedules. The Court did not, however, award future damages, stating that they could not be determined with "adequate certainty." The Court also denied Hawaiian's request to ban Mesa from selling inter-island flight tickets for one year.

Conclusion

The judgment against Mesa is the most recent example where significant penalties have been imposed on a party for breaching a confidentiality agreement in the chapter 11 context. In a bankruptcy case, where the process is supposed to be open and transparent, and where the goal is to maximize value for stakeholders, the risk of liability — and the nature of sanctions — for misuse of confidential information may be greater than otherwise. Thus, parties should ensure careful compliance with confidentiality agreements, particularly in the bankruptcy context.

A copy of the Court's decisions can be found at <https://ecf.hib.uscourts.gov/cgi-bin/PublicOpinion.pl>

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