A New Flight in the International Aviation Industry: The Implications of the United States-European Union Open Skies Agreement

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I. INTRODUCTION

The international aviation industry has been overdue for change. While internally the United States and the European Union have adopted a laissez-faire attitude toward the aviation industry, the two have almost entirely excluded foreign competition.[1] However, due to the economic hardships faced by several major airline carriers, the United States and the European Union have begun to reevaluate their bilateral agreement system.[2] Most recently, this movement has culminated in the United States and European Union Air Transport Agreement.[3] Effective as of March 30, 2008, this agreement seemed to offer a genuine opportunity to move the aviation industry toward a more liberal, freer market, but is the

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* © 2008 Jessica Finan. J.D. candidate 2009, Tulane University School of Law; B.S. 2005, University of Georgia. The author would like to thank her parents for their constant encourage-ment and support.

1. Robert M. Hardaway, *Of Cabbages and Cabotage: The Case for Opening Up the U.S. Airline Industry to International Competition*, 34 TRANSP. L.J. 1, 2 (2007).

2. Berry White, *Beginning of a Redefined Industry: How the European Court of Justice's Decision in the Open Skies Case Could Change the Global Aviation Industry*, 29 TRANSP. L.J. 267, 269-70 (2002).

3. Air Transport Agreement, U.S.-E.U., Apr. 30, 2007, 46 I.L.M. 470 (2007).

Air Transport Agreement everything that the signatory parties had hoped?

In Part II of this Comment, I will address the history and development of international aviation law and the movement from the bilateral regime to a multilateral system. Part III examines the positions the Parties took during negotiations and the impact of the decisions ultimately made. Finally, Part IV speculates which groups have the most to benefit from the Air Transport Agreement.

II. HISTORY OF AVIATION LAW

A. How International Aviation Regulation Began

The Convention on International Civil Aviation in 1944[4] (Chicago Convention) created the modern international aviation legal structure. Fifty-four nations attended the Chicago Convention to "make arrangements for the immediate establishment of provisional world air routes and services."[5] At the outset, the United States made efforts to liberalize international aviation by promoting an authority with limited powers.[6] However, once convened, the delegates were unable to agree on the extent to which international air services should be controlled.[7] Key discussion concerned the five "freedoms" of the sky.[8] These five "freedoms" were proposed to express the right of a country's civil airline to: (1) fly over the territory of another nation to reach a third; (2) land in another state's territory for noncommercial, technical reasons; (3) carry traffic from its country of registry to another; (4) carry traffic from another country to its homeland; and (5) carry traffic between two countries outside its homeland.[9] The delegates could not agree on how to accept all five freedoms, and the final agreement provided for only the first two.[10] Had all five freedoms attained approval, the Chicago Convention, in effect, would have established a multilateral open skies agreement among many of the world's industrialized nations. Instead, the Chicago Convention abandoned the final three "freedoms" from the

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4. Convention on International Civil Aviation, Dec. 7, 1944, 61 Stat. 1180, T.I.A.S. 1591, 15 U.N.T.S. 295.

5. Int'l Civ. Aviation Org. [ICAO], *International Civil Aviation Conference: Chicago, Illinois, 1 November to 7 December 1944*, http://www.icao.int/icao/en/Chicago_Conf/ (last visited Oct. 25, 2008).

6. *See* Ved P. Nanda, *Substantial Ownership and Control of International Airlines in the United States*, 50 AM. J. COMP. L. 357, 359 (2002); White, *supra* note 2, at 268.

7. Nanda, *supra* note 6, at 359.

8. White, *supra* note 2, at 268.

9. *Id.* at 268-69.

10. *See id.* at 268.

agreement and left it up to the individual nations to negotiate them with one another through bilateral treaties and executive agreements.[11]

After the Chicago Convention, countries individually began negotiating their nation's aviation interests through government-to-government bilateral agreements.[12] Under these bilateral agreements, nations most often nurtured their own national air carriers and regulated the number of international flights scheduled, the routes flown, and the fares charged.[13] In addition, fifth freedom rights were extremely limited and travel of a foreign airline within a nation was entirely prohibited. The result was a restrictive regime that, even seventy years later, is largely still in place and composes "over 1,500 bilateral, highly detailed, and often contested individual agreements between countries."[14]

Perhaps the most significant restrictive bilateral agreement has been between the United States and the United Kingdom. Because it influences the largest transatlantic aviation market, this complex agreement, known as Bermuda II, imposes severe restrictions on passenger services.[15] Bermuda II permits only four carriers, two per country,[16] to operate between the United States and London's Heathrow Airport.[17] It also prevents U.S. carriers from traveling from the United Kingdom to Continental Europe and does not allow any U.K. airlines to operate between two U.S. cities.[18] Bermuda II is a principal example of a nation guarding its national airlines at the expense of free competition. Critics have argued it is responsible for British Airways' capture of more than sixty percent of U.S.-U.K. passenger traffic.[19] Fortunately, however, Bermuda II came as an anomaly in a period featuring movements toward more liberal aviation agreements.

Although the Chicago Convention failed to produce a multilateral system to regulate international aviation, it did establish the International

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11. *Id.* at 268-69.

12. Stephen D. Rynerson, *Everybody Wants To Go to Heaven, but Nobody Wants To Die: The Story of the Transatlantic Common Aviation Area*, 30 DENV. J. INT'L L. & POL'Y 421, 422, 427-28 (2002).

13. *Id.* at 426-27.

14. White, *supra* note 2, at 268.

15. *Id.*; Gabriel S. Meyer, *U.S.-China Aviation Relations: Flight Path Toward Open Skies?*, 35 CORNELL INT'L L.J. 427, 435 (2002).

16. The two U.S. "flag carriers" are American Airlines and United Airlines. Currently, the two British carriers are British Airways and Virgin Atlantic. Meyer, *supra* note 15, at 435.

17. Svetlana Mosin, *Riding the Merger Wave: Strategic Alliances in the Airline Industry*, 27 TRANSP. L.J. 271, 282 (2000).

18. *Id.*

19. White, *supra* note 2, at 269.

Civil Aviation Organization (ICAO).[20] As a specialized agency of the United Nations, the ICAO promotes civil aviation through its 190 members.[21] Generally, the ICAO aims "to develop the principles and techniques of international air navigation and to foster the planning and development of international air transport."[22] It promulgates its directives through standards and recommended practices which mandate safe, efficient, and orderly international air travel.[23] The ICAO standards and recommended practices include all technical, security, and facilitation aspects of international civil aviation.[24] Its standards range from personnel licensing to air traffic services to the environment.[25]

B. Movement Toward Multilateral Agreements

In recent decades, as airlines began facing economic hardships, the United States and the European Community have realized the pressing need for movement toward multilateral aviation agreements. In the United States, the Airline Deregulation Act of 1978 (ADA) marked the beginning of a more liberalized aviation system.[26] While purely domestic, the ADA put an end to forty years of strict, government-sponsored price fixing and exclusion of competition.[27] In the years immediately following the ADA, the effects of deregulation on the U.S. airline industry were convincing. For example, reports showed that in the five years following the ADA, operating efficiency of the airline carriers increased.[28] Only three years after deregulation, eleven new airlines had entered the market causing a decrease in airline fares.[29] Consequently, deregulation made frequent air travel available to average Americans. Inspired by their domestic success with liberalization and eager to capture the international market, the United States began negotiating more liberal bilateral aviation agreements with European nations.[30]

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20. Nanda, *supra* note 6, at 360; Convention on International Civil Aviation, *supra* note 4, art. 43.

21. ICAO, Making an ICAO Standard, http://www.icao.int/icao/en/anb/mais/index.html (last visited Sept. 7, 2008); ICAO, Contracting States, http://www.eurocontrol.int/icard/gallery/content/public/icaoctry.pdf (last visited Sept. 7, 2008).

22. Convention on International Civil Aviation, *supra* note 4, art. 44.

23. ICAO, Making an ICAO Standard, *supra* note 21.

24. *Id.*

25. *Id.*

26. Airline Deregulation Act of 1978, Pub. L. No. 95-504, 92 Stat. 1705 (1978).

27. Hardaway, *supra* note 1, at 9.

28. *Id.* at 9-10.

29. *Id.* at 10.

30. *See id.*; BRATTLE GROUP, THE ECONOMIC IMPACT OF AN EU-US OPEN AVIATION AREA § 1.2 (2002).

The adoption of more bilateral treaties significantly opened airline traffic between the United States and other foreign countries. The United States Department of Transportation (DOT) termed these liberal bilateral agreements "open skies." The DOT believed open skies agreements would offer a structure to "allow both United States and foreign carriers the greatest flexibility to conduct their business without undue government intervention, benefiting the traveling and shipping public to an extent that is not possible under traditional bilateral arrangements."[31] Unlike their former bilateral counterparts, for example, the open skies agreements provided for unrestricted capacity and frequency on all routes, the right to operate between any point in the United States and any point in a European country, and procompetitive provisions on commercial opportunities, user charges, and fair competition.[32] They also permitted U.S. carriers to fly between any point in the United States and any point in a European country.[33] As many advocates expected, the open skies agreements produced effects similar to the deregulation of the U.S. aviation market—increased travel and decreased fares.[34]

Despite the proximity amongst Member States, the European Union did not internally deregulate their aviation system as quickly as the United States. The European Union took its first step in 1993, when several reforms, identified as the "Third Package," were implemented.[35] These reforms removed commercial controls on aviation within the European Union by allowing Member States to establish carriers and fly them freely between each other's airports and even set up an airline in another Member State.[36] However, the "Third Package" fell short because the Member States' 800 bilateral agreements essentially remained in place.[37] Consequently, the Comité des Sages (Comité), in a report to the European Commission, illuminated the economic limitations of its bilateral framework. In the report, the Comité called for a multilateral system under the control of the European Union rather than the individual Member States.[38] It asserted, correctly, that bilaterals "ignore the new realities of the Single European Aviation Market" by

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31. *In re* Defining "Open Skies," 57 Fed. Reg. 48,130 (Dep't of Transp. May 5, 1992).
32. *Id.*; White, *supra* note 2, at 270.
33. *In re* Defining "Open Skies," 57 Fed. Reg. 48,130; White, *supra* note 2, at 270.
34. One report indicates that the number of passengers traveling from the United States to a foreign nation on a U.S. airline increased by forty-seven percent from 1987 to 1993. BRATTLE GROUP, *supra* note 30, § 1.4.
35. Rynerson, *supra* note 12, at 428.
36. *Id.*
37. *Id.* at 429.
38. *Id.*

fostering inefficient bargaining processes and aviation operations.[39] Nevertheless, ultimate demand for change did not occur until almost eight years later by the European Court of Justice.

On November 5, 2002, the European Court of Justice issued judgments against eight Member States that had refused to dispose of their bilateral regimes.[40] The Court held that these members, by maintaining their individual bilateral agreements with the United States, had breached law.[41] The Court concluded that individual nationality clauses in the agreements violated the right of establishment under article 43 of the EC treaty by discriminating on grounds of nationality.[42] Essentially, these bilaterals infringed on "the external competence" of the European Union, and only the European Union, not the individual Member States, could enter into international commitments.[43] The European Commission compelled Member States to denounce the bilateral agreements they had signed and instead forge unified deals with third countries through horizontal agreements.[44] As a unified negotiator, the European Union became more attractive to foreign nations, including the United States, than it had been as individual nations. Through a single agreement a third country can currently gain entry into twenty-seven developed countries.[45] As a result, by 2007, the European Union had entered into twenty-two horizontal agreements with third countries and "established contact with major partners such as China, Australia, India, and the Russian Federation."[46]

III. UNITED STATES-EUROPEAN UNION AIR TRANSPORT AGREEMENT

After the European Court of Justice held that EC Member States' bilateral negotiations with the United States violated EC law, pressure to reach a multilateral agreement and set up one system regulating transatlantic aviation escalated. Negotiations between the United States and the European Union for an open skies agreement began in October

39. *Id.* For example, the Comité calculated that most EU carriers relied on extra-European routes for half or more of their activity. *Id.*

40. Ruwantissa Abeyratne, *The US/EU Open Skies Agreement—Some Issues*, 72 J. AIR L. & COM. 21, 30 (2007).

41. *Id.* at 30-31.

42. *Id.*

43. *Id.* at 31.

44. *Id.*; White, *supra* note 2, at 275.

45. Abeyratne, *supra* note 40, at 31.

46. *Id.* at 32.

of 2003.[47] The principal focus of the negotiations was to promote a more liberal and expansive international aviation system.[48] On April 30, 2007, the parties signed the U.S.-EU Air Transport Agreement.[49] The Air Transport Agreement is provisionally applied[50] as of March 30, 2008. U.S.-EU negotiations on a second stage of aviation liberalization were set to commence within two months of the application date.[51] The following analyses discuss the impact of the Air Transport Agreement on the economy, safety, security, and environments of the United States and the European Union.

A. Economic Effects

Undoubtedly, more liberal aviation rights will have powerful economic effects on the economies of the United States and the European Union. During negotiations, both Parties wanted a multilateral regime that reflected the open skies framework, which the United States had previously negotiated individually with Member States.[52] Foremost, U.S. negotiators sought the freedom to operate between the United States and the European Union and extend that service to points within the European Union.[53] This would allow a U.S.-registered aircraft to fly directly from Paris to London without having to return to New York first. They also wanted the two airline restrictions in London's Heathrow airport imposed by Bermuda II replaced with free access.[54] Similarly, the European carriers wanted the right "to operate between the EU and the United States from any point within the EU" and the eighth freedom right to "extend that service to points within the United States."[55]

Articles 3 and 22 of the Air Transport Agreement are the products of these negotiations. Article 3 replaces the existing bilateral agreements

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47. John R. Byerly, Deputy Assistant Sec'y for Transp. Affairs, Remarks on the EU Open Skies Agreement, Remarks at the ACI-NA 16th Annual Conference and Exhibition (Sept. 29, 2007) (transcript *available at* http://www.state.gov/e/eeb/rls/rm/2007/94398.htm.).

48. *Id.*

49. Air Transport Agreement, *supra* note 3.

50. *Id.* art. 25 ("Either Party may at any time give notice in writing through diplomatic channels to the other Party of a decision to no longer apply this Agreement. In that event, application shall cease . . . at the end of the . . . traffic season in effect one year following the date of written notification, unless the notice is withdrawn by agreement of the Parties before the end of this period.").

51. Byerly, *supra* note 47.

52. *See* Abeyratne, *supra* note 40, at 24.

53. *Id.* at 25, 30.

54. *Id.* at 30. Currently only United Airlines and American Airlines are allowed to fly to Heathrow Airport in London.

55. *Id.* at 29.

with an open skies framework.[56] It awards the U.S. airlines the right to fly from one European country to another, without returning to their country of origin.[57] It states that any airline may

> operate flights in either or both directions; . . . serve behind, intermediate, and beyond points and points in the territories of the Parties in any combination and in any order; . . . make stopovers at any points whether within or outside the territory of either Party . . . and combine traffic on the same aircraft regardless of where such traffic originates.[58]

Article 3 also eases the U.S. airlines' fear of unlimited access by not granting foreign airlines consecutive cabotage—the right to fly to two points within the same country. This means the Italian airline, Alitalia, could not land in New York with one set of passengers then continue onward to Denver with another set of passengers.

In addition, article 22 suspends the highly restrictive Bermuda II agreement, and grants U.S. airlines unlimited access to London's Heathrow Airport.[59] In accord with the United States' open skies initiative to promote "[p]rocompetitive provisions on commercial opportunities, user charges, fair competition and intermodal rights,"[60] the Air Transport Agreement authorizes every U.S. and EU airline to operate without restriction on the number of flights, aircraft, and routes.[61] Furthermore, under the Air Transport Agreement the individual carriers can set fares according to market demand[62] and can enter into cooperative arrangements including franchising and leasing.[63] For instance, each party can bring its specialized staff to perform managerial, sale, technical, and operational functions, and has the right to select among competing suppliers for ground-handling services.[64]

The effects of removing operating restrictions on routes will increase efficiency in the aviation industry through economies of scope. Most airlines have already developed a hub and spoke system to take advantage of the average cost decreases experienced when flights are full. Yet, additional profits can be captured as airlines are able to add

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56. *See* Air Transport Agreement, *supra* note 3, art. 3.
57. *Id.*
58. *Id.* art. 3, ¶ 2.
59. *See id.* art. 22.
60. *In re* Defining "Open Skies," 57 Fed. Reg. 48,130 (Dep't of Transp. May 5, 1992).
61. Air Transport Agreement, *supra* note 3, art. 3, ¶ 4.
62. *See id.* art. 13, ¶ 1 ("Prices for air transportation services operated pursuant to this Agreement shall be established freely and shall not be subject to approval, nor may they be required to be filed.").
63. *Id.* art. 10, ¶ 8.
64. *See id.* art. 10, ¶¶ 2-3(a)(ii).

new cities to their already established hub and spoke networks.[65] To consumers, these profits translate into lower fares. Most commentators agree the liberalization will result in services carried out with greater efficiency and prices that are more competitive.[66] In particular, a 2002 report prepared by the Brattle Group for the European Commission projected that the gain in consumer surplus as a result of an agreement like the Air Transport Agreement could range from €629 million to €1,374 million a year.[67] These figures are significant because they give Americans and Europeans the opportunity to travel internationally for business and pleasure more frequently, which promotes globalization. All industries could experience a decrease in their freight charges as cargo airlines like FedEx and UPS are able to increase their networks. Also, opening the United States and the European Union, two of the world's largest tourist markets, will have significant secondary effects in a wide range of sectors, including employment.

The Air Transport Agreement also resolved some disputes concerning user charges and public subsidies. Not surprisingly, during negotiations, the United States and European Union lobbied for rights, like user charges and public subsidies, which enabled them to support their national airline companies and the jobs they provide.[68] However, most economists recognize that user charges distort market conditions because they permit local airlines to pay less than foreign airlines.[69] Excessive user fees often discourage foreign carriers from entering a new market because it puts them at a disadvantage to national carriers that pay lower charges. Under article 12, user charges must be "just, reasonable and not unjustly discriminatory."[70] More importantly, the user charges must be uniform. The Air Transport Agreement assesses user charges "on terms not less favourable than the most favourable terms available to any other airline."[71] Mandating uniform user fees will encourage EU airlines to enter the U.S. market and vice versa and support competition. It assures foreign airlines that they may compete abroad freely and on terms equal to national airlines.

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65. BRATTLE GROUP, *supra* note 30, § 5.2.

66. *Id.*

67. *Id.* § 4.2.

68. Charles A. Hunnicutt, *US and EU: New Era, New Agreement?: Opportunity To Build a Global System*, 18 AIR & SPACE LAW. 1, 16 (2003).

69. *See id.*

70. Air Transport Agreement, *supra* note 3, art. 12, ¶ 1. The Air Transport Agreement defines a user charge as "a charge imposed on airlines for the provision of airport, airport environmental, air navigation or aviation security facilities or services." *Id.* art. 1, ¶ 10.

71. *Id.* art. 12, ¶ 1.

Another issue on the table was public subsidies. Airlines, especially after September 11, believe that without the ability to receive periodic public subsidies, they would be forced into bankruptcy, leaving too few airlines to support the remaining market.[72] They argue that this sudden decrease in supply will cause prices to increase dramatically.[73] These sentiments are further backed by consumers who, addicted to bargain fares, cannot bear to see any price increases, even necessary ones.[74] Unlike the airlines, economists feel that subsidies distort the market as the federal government continues to bailout struggling airlines that should go out of business. As one critic explained, "because struggling airlines are not allowed to go out of business, an intensely competitive market remains with many air carriers fighting for the same customers, thereby driving down prices."[75] Although they recognize that there could be short term pains after a large airline carrier does go bankrupt, critics argue that in the long run the remaining companies will be stronger and better able to tackle the international market.[76]

Despite these strong positions, the Air Transport Agreement took a middle-of-the-road approach effectively avoiding many of these underlying concerns. Under article 14, public subsidies are permitted unless they "adversely affect [the] fair and equal opportunity of the airlines . . . to compete."[77] For example, one government could not unfairly subsidize its nation's airlines to drive foreign airlines out of business. The Air Transport Agreement will not appease economists who call for an end to public subsidies because article 14 permits them.

However, in the context of the Air Transport Agreement, keeping the option to issue public subsidies may have been the right move. Because the Air Transport Agreement is the initial phase in the multilateral aviation agreement, it will need the confidence of the airlines and their investors in order live up to its expectations. Generally, subsidies provide confidence because airlines recognize that they will have the support of their governments if they fail. Therefore, the stability public subsidies provide may lessen airlines' anxiety about competing in newly offered markets, like London's Heathrow.

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72. Richard D. Cudahy, *The Airlines: Destined To Fail?*, 71 J. AIR L. & COM. 3, 13-14, 31-32 (2006); BRATTLE GROUP, *supra* note 30, § 1.10.

73. Cudahy, *supra* note 72, 31-32.

74. *Id.* at 14.

75. Christopher McBay, *Airline Deregulation Deserves Another Shot: How Foreign Investment Restrictions and Subsidies Actually Hurt the Airline Industry*, 72 J. AIR L. & COM. 173, 197 (2007).

76. *Id.*

77. *See* Air Transport Agreement, *supra* note 3, art. 14, ¶ 1.

B. Safety and Security

The primary objective of the Air Transport Agreement was to provide a more liberalized aviation system. Yet, this was not the only issue affecting aviation. Several of the restrictions in the bilateral regimes were imposed to protect national safety and security, and the DOT, in particular, was concerned that a more liberalized structure could threaten these measures.[78] Under the current regulatory system, the ICAO develops and disseminates detailed international standards, and the signatory states, through national civil aviation authorities (CAAs), apply and enforce the ICAO standards.[79] The United States and the European Union have superb safety records because they not only comply but often exceed the standards imposed by the ICAO.[80] The Air Transport Agreement maintains this regulated structure and will not encumber their states' strong regulatory systems.

Because the United States and the European Union have maintained extremely low accident rates, some groups, like the International Transport Workers' Federation (ITF), fear that further deregulation could jeopardize safety and security.[81] The ITF has asserted the same arguments with regard to safety that they made when the United States sought to deregulate internally in the 1970s. It contends that a completely liberalized aviation area would weaken airline safety because, absent government aviation regulations, airlines might spend too little to protect safety and security in order to keep prices lower or more competitive.[82]

The ITF's argument should not be ignored because airline safety must be constantly monitored; however, it is unlikely that deregulation would have an adverse effect on safety or security. First, it must be conceded that the Air Transport Agreement does liberalize safety and security requirements.[83] Article 8, for example, simply requires that for certificates or licenses for operating internationally, air transportation must meet the minimum standards established pursuant to the Chicago Convention.[84] It also merely gives authorities the right to "refuse to recognise as valid for purposes of flight above their own territory,

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78. *Id.* § 8, ¶ 1.
79. BRATTLE GROUP, *supra* note 30, § 9.2.
80. *Id.*
81. Int'l Transp. Workers' Fed'n, Civil Aviation Education Resource Pack (June 2006), http://www.itfglobal.org/files/extranet/-1/4066/Aviation.pdf.
82. *Id.*
83. *See generally* Air Transport Agreement, *supra* note 3, art. 8.
84. *Id.* art. 8, ¶ 1.

certificates of competency and licences granted to . . . their own nationals by such other authorities," which means that the United States cannot require EU airlines to meet their higher standards, only the minimum.[85] However, there is no evidence that the deregulation advanced in the Air Transport Agreement will negatively impact safety. This is clearly supported by empirical evidence. Most prominently, a 1991 study by National Research Council examined how the deregulation of the aviation industry in 1978 had affected airline safety.[86] It found that from 1978 to 1990, accident rates for major jet carriers fluctuated yearly but at a very low level and generally moved downward.[87] Therefore, roughly in line with long-term trends, commercial aviation safety had improved with deregulation.[88]

The ITF also underscores the role of the tough internal controls of the United States and the European Union. Like other open skies agreements, the Air Transport Agreement preserves the role of the ICAO, and does not affect the internal enforcement systems, the Federal Aviation Administration (FAA) and the European Aviation Safety Agency (EASA). Because it is working, this framework should not be altered. The United States and the European Union have the lowest accident rates in the world. From 1992 through 2001, the rate of major accidents per million departures was 0.5 in the United States and Canada and 0.8 in European States, both much lower than the rest of the world.[89]

It is important to warn that the failure of the Air Transport Agreement to completely liberalize aviation could have an effect on safety and security. Under article 10, air carriers are allowed to enter into collaborative arrangements,[90] but the Agreement does not permit foreign carriers to merge or acquire one another. Therefore, while ancillary aviation activities contract out operations that they used to perform themselves, they combine to form a single entity. This could create problems. Contracting out activities that occur in physically distant locations with different sovereignties and language barriers could result in safety oversights, and differing ICAO compliance rates magnify this challenge.[91] If the Air Transport Agreement would allow the merging of

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85. *Id.*
86. BRATTLE GROUP, *supra* note 30, § 9.3.
87. *Id.*
88. *Id.*
89. *Id.* § 9.1. In contrast, the rate of major accidents per million departures was 2.6 in Asia, 3.0 in non-JAA European States, 3.2 in Latin America, 3.4 in the Middle East, and 12.1 in Africa. *Id.*
90. Air Transport Agreement, *supra* note 3, art. 10.
91. BRATTLE GROUP, *supra* note 30, § 9.3.

foreign airline corporations, it could minimize this problem. A single, merged airline carrier, acting collectively, would be easier to regulate than two or three independent companies. Because the Air Transport Agreement does not allow foreign air carriers to merge or acquire one another, the solution to this problem remains entirely with the internal regulatory agencies who should respond by continuing to bolster regulatory control.

C. The Environment

The Air Transport Agreement, to the dismay of environmental groups, lacks important protections to help the environment and combat climate change. The Air Transport Agreement evidences that environmental concerns are secondary to the other rights contained in the Agreement.[92] It states, "When a Party is considering proposed environmental measures it should evaluate possible adverse effects on the exercise of rights contained in this Agreement, and . . . take appropriate steps to mitigate any such adverse effects."[93] Therefore, according to the agreement, when faced with an environmental proposal that could cause negative consequences to the rights granted in the Agreement, the rights should prevail.

Although the United States and the European Union currently comply with environmental standards set by the ICAO, internal organizations who have set their standards higher believe that the agreement prevents them from reaching those goals.[94] For example, in the European Union, groups like the European Federation for Transport and Environment had hoped to meet climate targets and bring aviation into the EU's carbon emissions trading system.[95] However, they believe that the 3.5 million tons of extra carbon dioxide emitted as a result of increased transatlantic travel will completely undermine these goals.[96]

Additionally, article 15 does not preserve the regulators' ability to oversee emissions produced by foreign airlines.[97] This prevents the parties' regulatory organizations, like the FAA and EASA, from refusing foreign airlines that are not compliant with their internal standards and

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92. *See* Air Transport Agreement, *supra* note 3, art. 15, ¶ 2.

93. *Id.*

94. Eur. Fed'n for Transp. & Env't, Open Skies Deal a 'Serious Setback' to EU Climate Policy (Mar. 22, 2007), http://www.transportenvironment.org/Article386.html.

95. Stephen Castle, *Open Skies Pact 'Will Worsen Climate Change,'* INDEPENDENT, Mar. 22, 2007, *available at* http://www.independent.co.uk/environment/climate-change/open-skies-pact-will-worsen-climate-change-441293.html.

96. *Id.*

97. *See generally* Air Transport Agreement, *supra* note 3, art. 15.

regulations. It could also discourage the airlines from increasing environmental standards on their own, especially as competition increases. What is clear from article 15 is that the climate control was not a top priority to negotiators. Rather, their interest lay with the economic outcomes, like increasing productivity and lowering fares. Therefore, in the second round of open skies negotiations, environmentalists should demand more stringent environmental regulations that coincide with their current goals toward climate control.

IV. WHO WILL BENEFIT FROM THE AIR TRANSPORT AGREEMENT?

Standards for rights to own and control foreign airlines were highly deliberated between the United States and the European Union.[98] The European Union clearly wanted to abolish the ownership limits established in the United States, which restrict foreign ownership of U.S. airlines to twenty-five percent,[99] and struck down several draft agreements for failure to comply with its limits.[100] Conversely, the United States held tightly to its twenty-five percent threshold, primarily to protect its labor groups, national airlines, and its Civil Reserve Air Fleet (CRAF)—a group of more than nine hundred U.S commercial aircraft accessible to the DOT in the event of a defense emergency.[101] Nevertheless, the European Union wanted its investors to have the opportunity to benefit from commercial opportunities in the U.S. aviation market, but to the U.S. negotiators, protection of its own national carriers from external operators was more important than the ability to compete freely in the European Union.

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98. *See* Hardaway, *supra* note 1, at 3.

99. 49 U.S.C. § 1102(a) (1958) requires an air carrier to remain a "citizen of the United States."

> 49 U.S.C. § 1102(a)(15) defines "citizen of the United States" in the case of a corporation as "a corporation organized under the laws of the United States, or a State . . . , of which the president and at least two-thirds of the board of directors and other managing officers are citizens of the United States, and in which at least 75 percent of the voting interest is *owned or controlled* by persons that are citizens of the United States."

BRATTLE GROUP, *supra* note 30, annex II (emphasis added). Administrative holding by the DOT has modified the literal meaning of "owned or controlled" to mean, "owned and controlled." Furthermore, the term "control" is not defined by the statute and has been subject to change over the years. *Id.*

100. Hardaway, *supra* note 1, at 28 ("In 2002, the European Court struck down the draft Open Skies agreement, saying it violated the laws of the 15-nation EU common market. The court, however, urged the sides to continue negotiations and, in 2005, the EU and the U.S. began a fifth round of aviation talks to attempt to resolve their differences.").

101. BRATTLE GROUP, *supra* note 30, § 7.1.

Articles 4, 5, and 6 of the Air Transport Agreement address the resolution of these negotiations. Article 4 confers authorization qualifications that must be met by U.S. airlines and airlines of the European Community and its Member States (Community airlines).[102] It states that after receiving an application from an airline of one party, the other party must grant appropriate authorization with minimal delay provided that "substantial ownership and effective control" of an airline are vested in the party where it is licensed and has its principal place of business.[103] Article 5 complements article 4 by allowing either party to revoke, suspend, or limit the operating authorization of airlines that do not comply with the substantial ownership and effective control requirement.[104] In furtherance of matters related to ownership, investment, and control, article 6 mandates the use of the provisions in annex 4.[105]

Annex 4 provides standards for ownership, investment, and control.[106] Article 1 of annex 4 provides different ownership standards for U.S. and Community airlines. The first paragraph establishes the ownership standards for U.S. airlines by nationals of a Member State.[107] It asserts, "ownership by nationals of a Member State . . . of the equity of a US airline shall be permitted, subject to two limitations."[108] The first limitation prohibits ownership of more than twenty-five percent of a corporation's voting equity by foreign nationals.[109] However, under this twenty-five percent limitation, "ownership by nationals of a Member State . . . of as much as 25% of the voting equity; and/or as much as 49.9% of the total equity," alone, cannot constitute control of that airline.[110] Moreover, ownership by nationals of a Member State of fifty percent or more of the total equity cannot be presumed to constitute control of a U.S. airline.[111] Rather, ownership is considered on a case-by-case basis.[112] The second limitation excludes "actual control of a U.S. airline by foreign nationals."[113]

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102. Air Transport Agreement, *supra* note 3, art. 4.
103. *Id.*
104. *Id.* art. 5, ¶ 1.
105. *Id.* art. 6.
106. *Id.* annex 4, art. 1, ¶ 1.
107. *Id.*
108. *Id.*
109. *Id.*
110. *Id.* annex 4, art. 1, ¶ 1(a)(1)-(2).
111. *Id.*
112. *Id.*
113. *Id.*

The second paragraph of article 1 addresses the ownership standards for Community airlines by U.S. nationals.[114] It provides no changes to the current EU law, which "prohibits non-EU shareholders collectively from owning a majority of an EU carrier, or having the possibility directly or indirectly of exercising decisive influence over an EU carrier."[115] Thus, whereas the U.S. regulations contain requirements dealing with the nationality of the airline management, the European Union addresses the external control of the airline by stockholders. Paragraph 2 of article 1 permits ownership by U.S. nationals of a Community airline as long as the majority of the airline is "owned by Member States and/or nationals of Member States."[116] The Community airlines must also be "effectively controlled" by Member States and/or nationals of Member States.[117] While the ownership limitations for U.S. airlines appear more stringent than those required for Community airlines, paragraph 4 attempts to even the standards. It holds that in light of paragraph 2, the Member States reserve "the right to limit investments by US nationals in the voting equity of a Community airline . . . to a level equivalent to that allowed by the United States for foreign nationals in US airlines."[118]

Despite the insistence of the European Union, the Air Transport Agreement does not allow any amendment to the twenty-five percent condition of voting equity, but does allow EU investors to retain nonvoting capital control of an American carrier. These standards can benefit the parties because they prevent third parties not privy to the agreement from obtaining the negotiated privileges through the back door.[119] For example, if a Moroccan airline merges with an English airline, the new Moroccan-English airline would not be given the open skies benefits like a fully owned English airline. Still, to be designated a U.S. airline carrier, the corporation must be overwhelmingly owned and controlled by U.S. nationals which does not satisfy EU investors hoping to gain from the profitability of U.S. airlines.

Nevertheless, under these anticompetitive regulations the Parties will see less effective carriers due to the Air Transport Agreement because they have precluded airlines from restructuring with foreign airlines through mergers and acquisitions. Mergers and acquisitions are

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114. *Id.* annex 4, art. 1, ¶ 2.

115. BRATTLE GROUP, *supra* note 30, § 1.7 ("In addition, some EU Member States have their own prohibitions on airline takeovers by non-EU investors.").

116. Air Transport Agreement, *supra* note 3, annex 4, art. 1.

117. *Id.*

118. *Id.*

119. BRATTLE GROUP, *supra* note 30, § 1.9.

important to the aviation industry because they enable restructuring and allow efficient airlines to take control over failing ones.[120] When two firms combine, the merged corporation can increase its output level to greater than the output level of the two firms individually, which allows the merged firm to spread fixed overhead costs in administration, sales, marketing, and maintenance over larger passenger volumes.[121] Furthermore, because mergers and acquisitions help replace inefficient airlines with more efficient ones, the more efficient airlines can diffuse their new technologies and industry best management practices.[122]

To airlines, the result of the Agreement is higher costs from unrealized economies of scale.[123] To consumers, capturing these efficiencies would translate into lower fares.[124] A report by the Brattle Group suggests that the total consumer benefits to an Open Aviation Area, such as the Air Transport Agreement, through the form of reduced fares, would be €3 billion annually, but likely more with the gains from transatlantic mergers and acquisitions.[125] Eliminating the possibility that foreign aviation corporations can restructure not only prevents corporations from benefitting from greater economies of scale, but also prevents consumers from benefitting from lower prices. Thus, the ownership and control standards the Air Transport Agreements provide will allow failing national airlines to remain national, and, again, we see the prospect of governments providing subsidies to keep their ailing national airlines afloat. This does not mean, however, that European airlines cannot engage in cross-border mergers, and it is expected that many will.

The most recognizable faction that may benefit from the anticompetitive measures preserved in the Air Transport Agreement is organized labor. Prior to negotiations, labor groups from both parties feared that a liberalized agreement would decrease total airlines employment in order to boost economies of scale.[126] U.S. workers, in particular, believed that a foreign owned and controlled American carrier would substitute foreign labor for cheaper domestic workers.[127] For example, if American Airlines were to purchase Air Portugal, it could

120. *See generally id.* § 2.1.
121. *Id.*
122. *Id.*
123. *See id.*
124. *See id.* § 3.3.
125. *Id.*
126. *Id.* § 8.1.
127. *Id.* § 8.3.

substitute Portuguese pilots on transatlantic flights.[128] The Air Transport Agreement could have permitted this, but as it does not permit transatlantic mergers, the effects on labor groups should be minimal. Rather, it is expected that the Agreement will create an additional 72,000 jobs in the United States and the European Union in the next five years.[129] It seems, then, that the anticompetitive regime that the Air Transport Agreement preserves, while harming consumers and airline corporations hoping to benefit from greater economies of scale, benefits the labor groups and national airlines, particularly those in the United States.

V. CONCLUSION

In conclusion, the Air Transport Agreement has taken several great steps toward liberalizing the transatlantic aviation industry. More efficient route structures will increase competition by allowing airlines to better coordinate flights. This translates into lower operating costs for the airlines and lower fares for travelers. The Agreement will also generate more passengers and jobs. However, environmental groups are far from satisfied and are likely to demand more eco-friendly measures during the next round of negotiations. The parties also did not liberalize ownership and control standards, so consumers and airlines may not benefit to their fullest potential. Not only will provisions inhibiting transatlantic mergers diminish potential benefits but it also may provoke additional difficulties with aviation safety and security. Despite some of the Air Transport Agreement's faults, though, it has given the United States and the European Union the foundation they need to take transatlantic aviation off the ground.

128. *See id.*
129. Castle, *supra* note 95.