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IMPACT OF THE EC SINGLE MARKET ON THE RELATIONS BETWEEN THE EC AND KOREA

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ABSTRACT

At present European air transport is undergoing radical changes as a result of the liberalization measures taken by the European Community. The traditional system, characterized by nationalism, protectionism, and bilateralism, which prevented true competition and protected national carriers, has broken up. The creation of a common air transport policy for the Community has important implications for relationships between Member States and third countries.

The world airline industry is very much concerned by the emergence of a series of new principles and laws affecting the international air transport of third countries, such as the principle of non-discrimination, freedom of establishment, freedom of services, and EC competition law. Korea, which has fewer bargaining tools to attract the EC air carriers, must understand correctly the present changes in the air transport field of the EC and try to seek its own possible strategies.

RESUMÉ

Actuellement, le transport aérien européen connaît des changements radicaux suite aux mesures de libéralisation prises par la Communauté Européene. Le système traditionnel, caractérisé par le nationalisme, le protectionisme et le libéralisme et qui a freiné la libre concurrence pour protéger les transporteurs nationaux, appartient désormais au passé.

La création d'une politique commune en matière de transport aérien a des conséquences importantes pour les relations entre États membres et les pays tiers. L'industrie du transport aérien mondial est très influencée par l'émergence d'une serie de nouveaux principes et par les lois affectant le transport aérien international des pays tiers. Ces principes sont ceux de la non-discrimination, de la liberté d'établissement, de la liberté de services et du droit de la concurrence de la CE.

La Corée, qui a peu d'instruments économiques qui lui permettrait d'attirer les transporteurs de la CE doit s'adapter aux changements présents dans le domaine du transport aérien de la CE et essayer de trouver ses stratégies face à cet adversaire.

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APPENDICES

INTRODUCTION

The international system of Air Transport Regulation has been functioning for more than 40 years based on its three pillars: the International Civil Aviation Organization (ICAO)[1] provided technical and safety regulations; the International Air Transport Association (IATA)[2] provided the framework for tariff and fare coordination; and bilateral agreements, eventually, established a world-wide network.

However, political and economic changes in recent years have altered the operating environment for international air transport and created a widely felt need to re-assess the post-war aviation regulatory regime.[3]

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[1] ICAO was created by the *Convention on International Civil Aviation*, ICAO Doc. 7300/6; 15 UNTS 295 (opened for signature 7 December 1944, entered into force 4 April 1947) [hereinafter *Chicago Convention*]. For details about ICAO, see Bin Cheng, *The Law of International Air Transport* (London: Stevens & Sons, 1962) Part one at 31-172.

[2] IATA was founded by the International Air Transport Operators Conference held at Havana (Cuba) in April 1945. It is a corporate body under Canadian law and its headquarters are located in Montreal. For a general discussion of IATA, see P.P.C. Haanappel, *Pricing and Capacity Determination in International Air Transport: A Legal Analysis* (Deventer: Kluwer, 1984) Ch. 2 at 61-116.

[3] IATA White Paper, "Air Transport in a Changing World: Facing the Challenges of Tomorrow" (December 1992) at 21.

Among those changes, liberalization of air transport in the European Community (EC)[4] may most significantly have affected the traditional international system of air transport regulation[5] characterized by nationalism, protectionism and bilateralism, which prevented true competition and protected national carriers.

On 1 January 1993, the third and final phase of EC air transport liberalization came into force.[6] According to this,[7] national ownership and control criteria for airlines are replaced by Community criteria so as to make it possible for citizens of Community countries to establish their airline business in other Community countries. Member States must permit any community air carrier to exercise traffic rights on any route between two airports within the EC subject to certain exceptions. Furthermore, fares and rates including charter fares, seat fares and cargo rates may be freely set.

These measures in the EC do not appear to be easily reconcilable with a number of principles and provisions of the Chicago Convention of 1944.[8]

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[4] See *Treaty Establishing the European Economic Community*, 298 UNTS (opened for signature 27 March 1957, entered into force 1 January 1958) [hereinafter *EEC Treaty*].

[5] Ronald Schmid, "Air Transport within the European Single Market - how will it look after 1992?" (1992) 17 Air & Space L. 199 at 199.

[6] EC, O.J. Legislation (1992) No. L240 at 1-20.

[7] P.P.C. Haanappel, "Recent European Air Transport Developments" (1992) 17:2 Ann. Air & Sp. L. 217 at 220-224.

[8] Ludwig Weber, "External Aspects of European Liberalization" (1990) 15:5/6 Air L. 277 at 280.

The principle of nationality as embodied in the Chicago Convention does not require ownership by nationals of the flag state.[9] However, under international law, nationality requires a "genuine and effective link between the flag state and its nationals of ships or aircraft".[10] It is difficult to see how this requirement would be satisfied by ownership by a foreign national merely operating on the national territory of the state of registry.[11] This principle is particularly important in the area of safety, as will be discussed in Chapter II.

Article 7 of the Chicago Convention prohibits the granting of cabotage rights on an exclusive basis.[12] It is not clear whether the exchange of cabotage rights between EC Member States is compatible with Article 7 of the Chicago Convention. Although there is no stipulation of exclusivity in this grant of cabotage rights, the fact that it is made through Community measures, which naturally only apply to Member States, will result in an appearance of exclusivity.[13]

The implications of the liberalization process for existing relations of EC Member States with the outside world is one of the most complex aspects of the process.

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[9] Chicago Convention, *supra* note 1, Arts. 17-21.

[10] Ian Brownlie, *Principles of Public International Law*, 4th ed. (Oxford: Clarendon Press, 1990) at 407-420.

[11] Ludwig Weber, *European Integration and Air Transport* (LL.M. Thesis, McGill University, Institute of Air and Space Law 1976) at 189.

[12] Chicago Convention, *supra* note 1, Art. 7.

[13] Weber, *supra* note 8 at 283.

The liberalization in the EC will increase the competitiveness of the airlines in the region and integration will enhance the bargaining power of the region against the countries outside Europe. Non-discrimination within the Community may lead, at the same time, to a discriminatory and block-forming attitude on the part of the Community toward third countries.[14] Therefore, many non-EC countries are concerned that "Fortress Europe" may affect their traffic rights to, from and within the EC.

Korea is also concerned about a "Fortress Europe" because it has experienced limited bargaining power against the United States[15]

It is the aim of this thesis to analyze the implications of liberalization of air transport in the EC for the relationship between the EC and Korea. For that purpose, Chapter I of this thesis deals with the evolution of Community law in the air transport field. Its incompatibility with the present legal system will be discussed in Chapter II. Chapter III will review the external relations of the EC with third countries and analyze the existing effects of Community measures.

Despite the development in the EC of a common air transport policy designed to create a truly integrated internal market, to date there has been no common policy toward third countries outside EC. However, the creation of the internal market gives new opportunities to Community air carriers and their competitive position could be even

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[14] Maria Cristina G. Vilao, *Air Cabotage: Current Legal Issues* (LL.M. Thesis, McGill University, Institute of Air and Space Law, 1991) at 3.

[15] The structure imbalance in traffic rights between Korea and the United States will be explained in Chapter IV at 4-3.

further enhanced if, with regard to third countries, the Community would take full advantage of its changed position and instead of being divided, would speak with one voice.

In Chapter IV, after briefly reviewing the history of air transport in Korea and analysing the implications and effects of Community air transport liberalization on relations between the EC and Korea, I will propose, from a Korean perspective, the strategies Korea should adopt to overcome the challenges posed by the EC air transport policy.

During the preparation of this thesis, the Treaty on European Union (hereinafter Union Treaty) came into force on 1 November 1993.[16] It amended some contents of the EEC Treaty. Under the Union Treaty, the "European Community" is the new official term for the European Economic Community. The "European Union" comprises the European Community, the European Coal and Steel Community, and Euratom. In addition, the European Union has received new powers in the areas of foreign affairs, security policy, justice and home affairs. This thesis concern exclusively matters within the purview of the European Community, and the term "European Community" will be used throughout except where the articles and materials quoted use the term "EEC". However, the numbering of articles used prior to the Union Treaty is adopted herein.[17]

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[16] *Infra* note 210: At this point, the Union Treaty does not directly affect the air transport policy of the EC. However, Member States are expected to be more cooperative toward the outside EC.

[17] Appendix I. Article of the Union Treaty relevant to this Thesis.

It can be assumed that the term "European Union" will in future be used more often in bilateral and multilateral negotiations.

CHAPTER I

LIBERALIZATION OF AIR TRANSPORT IN THE EUROPEAN COMMUNITY

According to the Single European Act of 1986,[18] which went into effect on 1 July 1987, the internal market in the European Community was to be completed by 1 January 1993. Article 8a of this Act states that the internal market shall comprise a market without frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Act.[19]

The development of a common transport policy is listed in the EEC Treaty as being among the measures necessary to create the internal market.[20] There were many reasons for the long delay in initiating a common EC air transport policy.[21] However, a worldwide trend towards liberalized or deregulated air transport, judicial activism on the part of the Court of Justice of the European Communities[22] and administrative

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[18] *The Single European Act*, 28 February 1986, 30 O.J. Legislation (1987) No. L169 at 1.

[19] *Ibid.*, Art. 8a.

[20] *Supra* note 4, Art. 3(e) states that the activities of the Community shall include "the adoption of a common policy in the sphere of transport".

[21] P.P.C. Haanappel, "The External Aviation Relations of the European Economic Community and of EEC Member States into the Twenty-first Century" (1989) 14 Air L. 69 at 72.

[22] [Hereinafter *ECJ*].

activism on the part of the Commission of the European Communities[23] have prompted the Council of the European Communities to produce common air transport polices - the so-called first,[24] second[25] and third packages[26] - measures aiming at the liberalization of air transport in the EC.

I-1 MEMORANDA OF THE COMMISSION

The EC Commission's first major initiative with regard to air transport policy was the publication in 1979 of a memorandum entitled "Air Transport: A Community Approach".[27] There were six main points in it:[28]

(a) Increased possibilities for market entry and innovation were desirable *but full freedom of access was a long-term prospect.*

(b) There was a need for the introduction of various forms of cheap fares.

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[23] *Ibid.* at 72-73.

[24] EC, O.J. Legislation (1987) No. L374 at 1-25.

[25] EC, O.J. Legislation (1990) No. L217 at 1-16.

[26] EC, O.J. Legislation (1992) No. L240 at 1-20.

[27] Memorandum of the Commission, *Air Transport: A Community Approach*, Bull. of the Eur. Communities (Supp. May 1979) at 31.

[28] M.W. Tretheway, "European Air Transport in the 1990s: Deregulating the Internal Market and Changing Relationships with the Rest of the World", Working paper no. 91-TRA-003 (Faculty of Commerce, The University of British Columbia, Vancouver, Canada) at 34.

(c) There was also a need to develop new cross frontier services connecting regional centres within the Community.

(d) An implementing regulation applying Articles 85 and 86 directly to air services was essential.

(e) Increased competition emphasized the need for a policy on state aid to airlines.

(f) Whilst the right of establishment applied directly to airlines, Council action was necessary since practical and political obstacles would otherwise still exist.

However, the EC Council took no official action at that time, due in part to the fear held by Member States' governments that national airlines would be weakened by these proposals.[29]

In 1984, the Commission published a second memorandum on air transport entitled "Progress Towards the Development of a Community Air Transport Policy".[30] In this Memorandum the Commission recommended three measures on air transport:[31] (a) a specific Community regulation of the air industry; (b) an amendment to the machinery for the settlement of air tariffs; and (c) a limit on non-competitive bilateral agreements. But because of the bitter resistance of European air carriers,[32] little legislative progress was made until December 1987, when the Council reached agreement

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[29] Monica L. Luebker, "The 1992 European Unification: Effects in the Air Transport Industry" (1990) 56 J. Air L. & Com. 589 at 607.

[30] Memorandum of the Commission, *Progress Towards the Development of a Community Policy on Air Transport*, Bull. of the Eur. Communities (Supp. March 1984).

[31] Luebker, *supra* note 29.

[32] *Ibid.* at 607-609.

on certain of the Commission's proposals and adopted what has come to be known as the first "package", which included legislation on fares, capacity and access.[33]

I-2 INTER-REGIONAL AIR SERVICES DIRECTIVE[34]

In the regulatory field, the first significant action of the Council occurred in 1983. However, the impact of this directive was limited. The directive applied only to the international flights within the Community of aircraft with no more than 70 seats over a distance of at least 400 kilometres,[35] and to small airports, so called category 2 and/or 3.[36] As a result the practical importance of the Council's first step towards air transport liberalization remained modest.[37]

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[33] Frere Cholmeley, *Air Law and the European Community* (London: Butterworths, 1990) at 5-6.

[34] EC, *Council Directive 83/416* concerning the authorization of scheduled inter-regional services for the transport of passengers, mail and cargo between Member States, O.J. Legislation (1983) No. L237 at 19.

[35] *Ibid.*, Art. 1.

[36] *Ibid.*, Appendix A.

[37] Ebke and Wenglorz, "Liberalizing Scheduled Air Transport Within the European Community: From the First Phase to the Second and Beyond" (1991) 19 Trans. L. J. 417 at 430.

In the 1989 amendments to the Directive,[38] airlines were allowed to service routes under 400 kilometres.[39] Furthermore, aircraft size restrictions were removed. Explaining this rather advanced step towards the aim of a deregulated framework for regional air transport services, the Council adopted the Commission's attitude, which was that regional air service between Member States was to be strongly promoted in order to take pressure off the large congested airports within the Community.[40]

I-3 THE SINGLE EUROPEAN ACT

A decisive step towards the liberalization of scheduled air transport within the Community finally came with the Single European Act.[41] This is the legislation which spelled out the objective of completing the European internal market by the end of 1992.[42] An amendment to Article 8a of the EEC Treaty included air transport as part of the EC internal market.[43]

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[38] Council Directive 89/463 amending Directive (83/416) concerning the authorization of scheduled inter-regional air services for the transport of passengers, mail and cargo between Member States, O.J. Legislation (1989) No. L226 at 14.

[39] *Ibid.*, Art. 1.

[40] Ebke and Wenglorz, *supra* note 37.

[41] Single European Act, *supra* note 18.

[42] For details, see Paul Stephen Dempsey, "Aerial Dogfights Over Europe: The Liberalization of EEC Air Transport" (1988) 53 J. Air L. & Com. 615 at 673-677.

[43] EEC Treaty, Art. 8a, as inserted by the Single European Act, Art. 13.

It was also important in changing the way the Council makes decisions. Decisions concerning the establishment of a single market for air transport no longer would require unanimous voting by Member States; rather, measures could now be taken by a "qualified majority" of votes.[44]

In general, the EEC Treaty originally provided for the use of unanimity in Council decisions. This effectively gave individual countries veto power over issues, regardless of their overall importance. Such a procedure was an obstacle to effective decision making.[45]

The effect of majority votes for air transportation is that individual countries could no longer block reform. This induced a change of strategy for those countries opposed to air transport liberalization. Instead of blocking any change at all, their strategy became to win concessions in the reform package likely to be approved by the majority of the Council.[46]

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[44] EEC Treaty, Art. 84(2) as amended by the Single European Act, Art. 16: The 12 individual ministers on the Council have votes of differing weights. The weight of each Member State is spelled out in the Art. 148 of the EEC Treaty. Fifty-four votes from total seventy-six votes constitute a "qualified majority".

[45] M.W. Tretheway, *supra* note 28 at 35.

[46] *Ibid.*

I-4 THE PACKAGES OF EUROPEAN COMMUNITIES

I-4-1 FIRST PACKAGE

In December 1987, the Council took a number of steps toward the liberalization of air transport that are commonly referred to as the First Package of Liberalization. This consists of two Council Regulations, one Council Directive, and one Council Decision, each of which became effective on 1 January 1988.[47] The Package signalled (a) that the Council was joining the Commission in supporting air transport regulatory reforms; (b) that a competitive common market for air transport would be established by the end of 1992 - the same timetable as for other sectors of the European economy, and (c) while air transport would continue to be excluded from applicability of Article 85 of the EEC Treaty, this exclusion would eventually be removed.[48]

The measures mentioned were applicable only to flights between Member States. They did not apply to domestic flights within a given Member State, nor did they apply

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[47] O.J. Legislation (1987) No. L374 at 1-25.
- Regulation No. 3975/87 laying down the procedure for the application of the rules on competition to understanding in the air transport sector;
- Regulation No. 3976/87 on the application of Art. 85(3) of the Treaty to certain categories of agreements and concerted practices in the air transport sector;
- Directive 87/601 on fares for scheduled air services between Member States;
- Decision 87/602 on the sharing of the passenger capacity between air carriers and scheduled air services between Member States and on access for air carriers to scheduled air service routes between Member States.

[48] M.W. Tretheway, *supra* note 28 at 39.

to flights between a Member State and third countries[49] and they were the minimum measures[50] to be applied by the regulatory agencies in each country. Countries individually or bilaterally could enact more flexible arrangements.

A. Competition

In particular, Articles 85 and 86 of the EEC Treaty applied to air transportation.[51] Certain technical agreements were excluded from the applicability of Article 85.[52] The Commission had the power to investigate and impose sanctions on both airlines and Member States for violations of Articles 85 and 86 of the Treaty.[53]

However, Regulation 3976/87 established authority for the Commission to adopt block exemptions for certain categories of agreement and concerted practices in

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[49] Regulation No. 3975/87, *supra* note 47, Art. 1(2).

[50] For a detailed discussion of the First Package, see *European Air Law: Taxts and Documents* (Boston: Kluwer, 1992) at 32-34; WCP Status Report: Aviation in the European Community (Brussels: Wilmer, Cutler & Pickering, 1992) at 2-5; Ebke and Wenglorz, *supra* note 37 at 434-438; Dempsy, *supra* note 42 at 677-692; Constantin Economides, *Air Transport Law and Policy in the Europe of the EEC and ECAC: Now and Beyond 1992* (LL.M. Thesis, McGill University, Institute of Air and Space Law, 1989) at 106-133.

[51] Regulation No. 3975/87, *supra* note 44, Art. 1: Anti-competitive agreements or concerted partices which may affect trade between Member States are prohibited and void unless exemption is granted by the Commission (Art. 85 of the EEC Treaty); the abusive exploitation of a dominant position by one or more undertakings in the common market which may affect trade between Member States is prohibited (Art. 86 of the EEC Treaty).

[52] *Ibid.*, Art. 2.

[53] *Ibid.*, Arts. 3-6.

international air transport between Member States. The following activities between airlines could be exempted:[54] agreements on capacity, tariffs, revenue sharing, airport slots, computer reservation systems, and ground handling. Those exemptions granted by the Commission were far-reaching and remained effective until 31 January 1991.[55] With regard to competition, the EC recognized, in principle, the unlimited application of anti-trust rules laid down in Article 85 and Article 86 of the Treaty. However, the exemptions provided the airlines concerned with a significant amount of protection in an increasingly competitive market.[56]

B. Fares

Directive 87/601 maintained the traditional fares approval procedure. Thus, a fare became effective only if it had been approved by the governments of both Member States.[57] It also laid down criteria, linked to costs, by which Member States would approve air fares if they were reasonably related to the long-term fully allocated costs of the applicant air carrier[58] and provided for a consultation and arbitration procedure to settle disputes.[59] The centerpiece of this Directive was the fare approval system with

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[54] Regulation No. 3976/87, *supra* note 47, Art. 2.

[55] *Ibid.*, Art. 3.

[56] Ebke and Wenglorz, *supra* note 37 at 435.

[57] Directive 87/601, *supra* note 47, Art. 4.

[58] *Ibid.*, Art.3.

[59] *Ibid.*, Art. 7.

zones of flexibility.[60] The approval in these zones was automatic and was no longer submitted to a double approval rule.[61] Provided certain conditions were met,[62] fares could be reduced below the reference fare by different amounts.[63] The "discount zone" below the reference fare extended from 90% to 65% of the reference fare, the "deep discount zone" from 65% to 45%. An additional flexibility zone could reach as low as 35% of the reference fare.

C. Market Access and Capacity Sharing

Carriers could increase their share of the market to 55% during the period 1 January 1988 - 30 September 1989. After 30 September 1989, carriers could increase their market shares to 60%.[64] If a carrier could demonstrate to the Commission that it had incurred serious financial damage, the 55/60 per cent capacity rules could be

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[60] *Ibid.*, Art. 5.

[61] "Double Approval" rule means that prices (fares, rates, tariffs) be approved by the competent national aeronautical autorities of both sides. It was driven from the Bermuda I type bilateral air transport agreement. Until now, many bilateral air transport agreements have adopted this rule. However, under the influence of the "deregulation" policy, the United States has begun to use new form of bilateral air transport agreement, the so-called "liberal agreement". As to pricing "liberal", the United States may contain one out of three different tariff clauses: dual tariff disapproval rule, country of origin tariff disapproval rule and tariff band system, see P.P.C. Haanappel, "Bilateral Agreement" in *Governmental Regulation of Air Transport: Cases and Materials* edited by Richard A. Janda for Lectures at McGill University, IASL, 1992 at 450-457.

[62] *Ibid.*, Annex II.

[63] *Ibid.*, Art. 5.

[64] Decision 87/602, *supra* note 47, Art. 3.

suspended.[65] On third and fourth freedom routes, a Member State was obliged to accept any multi-designation of carriers by another Member State according to the following schedule: markets of more than 250,000 passengers per year (1988); markets of more than 200,000 passengers or more than 1,200 return flights per year (1989); markets of more than 180,000 passengers or more than 1,000 return flights per year (1990).[66]

Community carriers were permitted to establish flight connections between major airports in the territory of one Member State and regional airports in the territory of another Member State[67] and to operate a fifth-freedom scheduled air services where third or fourth traffic rights existed (with many restrictions).[68]

Even though the first package was only the first step in the creation of an internal market by the end of 1992, the provisions of the first package, which was characterized as "a watered down version"[69] did not bring any great changes to the European aviation environment, probably due to the fact that the changes it provided were accompanied by significant antitrust exceptions for EC air carriers.[70] Consequently, additional, more

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[65] *Ibid.*, Art. 4.

[66] *Ibid.*, Art. 5.

[67] *Ibid.*, Art. 6.

[68] *Ibid.*, Art. 8.

[69] P.P.C. Haanappel, *supra* note 21 at 82.

[70] Jeffrey R. Platt, "The Creation of a Community Cabotage Area in the European Community and its Implications for the US Bilateral System" (1992) 17 AL 4/6 183 at 185.

far-reaching measures were necessary if the objective of competitive market structures, in the area of scheduled air transport within the EC, was to be accomplished by January 1993.

I-4-2 SECOND PACKAGE

In June 1990, the Council adopted three regulations,[71] referred to as the "Second Package", regarding the liberalization of air transport,[72] effective as of November 1, 1990. They were designed to pave the way for phase three and the goal of full integration of air transport in a unified internal market after January 1, 1993.[73]

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[71] O.J. Legislation (1990) No. L217 at 1-16.
- Regulation No. 2342/90 on fares for scheduled air service;
- Regulation No. 2343/90 on access of air carriers to scheduled intra-community air service routes and on the sharing of passenger capacity between air carriers on scheduled air services between Member States;
- Regulation No. 2344/90 amending Regulation No. 3976/87 on the application of Art. 85(3) of the Treaty to certain categories of agreements and concerted practices in the air transport sector.

[72] For a detailed discussion of the Second Package, see European Air Law, *supra* note 50 at 40-45; WCP Status Report, *supra* note 50 at 2-5; Ebke and Wenglorz, *supra* note 37 at 441-451; P.P.C. Haanappel, "Regulatory Development in Europe" (1991) 16 Ann. of Air & Sp. L. 107 at 110-112.

[73] Stacey K. Weinberg, "Liberalization of Air Transport: Time for the EEC to Unfasten its Seatbelt" (1991) U. Pa. J. Int'l Bus. L. 433 at 442.

A. Fares

Regulation 2342/90 was the centerpiece of the second package and it provided more flexibility in the fare setting and approval system.[74] Fare approval followed from one of three procedures. Double disapproval was applied to cases of more than 105% of the reference fare.[75] To fares outside the zone of flexibility the double approval applied,[76] and within the so-called zones of flexibility automatic approval applied.[77]

Fare setting in general was made more flexible than in the first package by the introduction of three fare zones based on the reference fare,[78] the normal economic fare zone (105% - 95% of the reference fare); the discount zone (94% - 80%); and the deep-discount zone (79% - 30%). Also, the prerequisites for purchasing a ticket within the discount zone were eased.[79]

Only Community air carriers were permitted to introduce lower fares than existing ones when they operated on the basis of third and fourth freedom traffic rights.[80] In case of fifth freedom traffic rights, such lower fares could only be introduced when fares

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[74] Ebke and Wenglorz, *supra* note 37 at 442.

[75] Regulation No. 2342/90, *supra* note 71, Art. 4(4).

[76] *Ibid.*, Art. 4(5).

[77] *Ibid.*, Art. 4(3).

[78] *Ibid.*

[79] *Ibid.*, Annex II, No. 1.

[80] *Ibid.*, Art. 3(b).

proposed by the airlines remained within the flexibility zones.[81] This provision appeared to strengthen considerably competition on third, fourth and fifth freedom routes which airlines operate.

Member States could permit an airline of another Member State, operating a direct scheduled air service, to match prices already offered by a charter airline, provided that both services were equivalent in terms of quality and conditions.[82] This clause, originally demanded by southern EC countries, further blurred the distinction between scheduled and charter services.

B. Market Access and Capacity

The Market for EC air carriers and the seating capacities in scheduled air traffic was further liberalized by Regulation 2343/90,[83] which replaced Decision 87/602. Community air carriers that operated under the third and fourth freedom rights had free access to all EC airports,[84] subject to certain exceptions.[85] Furthermore, the capacity of the aircraft which could be used for fifth-freedom traffic were increased from 30% to 50%.[86] The 20% increase constituted modest improvement towards more competition.

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[81] *Ibid.*

[82] *Ibid.*, Art. 3(5).

[83] *Supra* note 71.

[84] *Ibid.*, Art. 4.

[85] *Ibid.*, Arts. 5(3), 5(4), 10(1), & 10(3).

[86] *Ibid.*, Art. 8(1).

However, the Council did not follow the Commission's proposal to allow carriers to make use of their fifth freedom rights in regard to third countries, if such countries agreed.[87] Thus, there was considerable room for further liberalization in the future.[88]

Multiple designation was accepted, as from 1 January 1991, if there were more than 140,000 passengers, or more than 800 return flights on a specific route per year. As from 1 January 1992 the thresholds were lowered to 100,000 passengers or 600 flights.[89]

With regard to capacity sharing, as of 1 November 1990 it became possible for each Member State to increase the share of capacity offered by its airlines, as compared to the capacity offered by airlines from another Member State by 7.5% compared to the previous corresponding season, provided that each Member State was entitled to a minimum share of 60% in any case.[90] At the request of a Member State, the Commission could, however, limit the growth in capacity, if the capacity increase resulted in substantial damage to a carrier registered in that Member State.[91]

Irrespective of the size of the aircraft employed, there were no capacity limits with respect to services between regional airports.[92] This regulation, which replaced

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[87] COM(89) 373 final (Sept. 8, 1989) Annex II, Art. 8 No. 2.

[88] Ebke and Wenglorz, *supra* note 37 at 442-452.

[89] *Ibid.*, Art. 6(2).

[90] *Ibid.*, Art. 11.

[91] *Ibid.*, Art. 12(1).

[92] *Ibid.*, Art. 11(3).

the inter-regional Air Service Directive of 1983, would protect airlines that service regional airports and that have opened new routes, against carriers operating larger aircraft.[93]

C. Competition

Regulation 2344/90 consisted of one provision which empowered the Commission to continue to exempt until December 31, 1992, certain airline practices and airline agreements from the EC anti-trust laws.[94]

Consultations on cargo rates were added to the exemptions.[95] The Commission proposed that amendments would broaden the scope of the Regulation to include international air transport between the Community and third countries and domestic air transport within a single Member State.[96] However, the Council's failure to adopt the Commission's proposal was unfortunate because the Council simply ignored the holding of the European Court of Justice in the *Ahmed Saeed* case.[97]

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[93] *Ibid.*, Art. 5(4).

[94] *Supra* note 71, Art. 1.

[95] *Ibid.*

[96] COM (89) 417 final (Sept. 8, 1989).

[97] Ebke and Wenglorz, *supra* note 37 at 407; the *Ahmed Aseed* case will be discussed in Chapter III.

The second package resulted in changes to the existing system in a number of respects.[98] In the areas of market access, tariff and capacities it constituted considerable progress towards the creation of more competitive and more market oriented structures. However, there were a number of issues that needed to be solved. These issues included cabotage rights and reverse discrimination against domestic carriers as well as technically updated air traffic infrastructure.[99]

1-4-3 THIRD PACKAGE

The third and final phase of EC air transport liberalization came into force on 1 January 1993. The third package consisted of five principal Council Regulations.[100]

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[98] See, Ebke and Wenglorz, *ibid.* at 442-452; *European Air Law: Texts and Documents* (Boston: Kluwer, 1992) *supra* note 37 at 40-45.

[99] Ebke and Wenglorz, *ibid.* at 452.

[100] O.J. Legislation (1992) No. L240 at 1-20.
- Regulation No. 2407/92 on licensing of air carriers;
- Regulation No. 2408/92 on access for Community air carriers to intra-community air routes;
Regulation No. 2409/92 on fares and rates for air services;
- Regulation No. 2410/92 amending Regulation No. 3975/87 laying down the procedure for the application of the rules on competition to undertakings in the air transport sector;
- Regulation No. 2411/92 amending Regulation No. 3976/87 on the application of Art. 85(3) of the Treaty to the certain categories of agreements and concerted practices in the air transport sector.

A. Air Carrier Licensing

Regulation 2407/92 harmonizes the criteria applicable to the granting of operating licenses and air operators certificates (AOC) by Member States in relation to air carriers established in the Community.[101]

Licensing will continue to be granted by individual EC Member States. A Member State may not grant or maintain in force an operating licensing unless specified requirements[102] are satisfied.[103]

A company satisfying the requirements must be granted an operating license but such license does not confer in itself any right of access to specific routes or markets.[104] National ownership and control criteria for airlines are replaced by Community criteria so as to make it possible for citizens of Community countries to establish in other Community countries.[105]

The requirement of majority ownership and effective control by EC nationals qualifies the rules which presently exist in all Member States requiring ownership and control by local nationals.

It thus paves the way for full cross-border airline mergers and takeovers and also permits airlines from one Member State to set up operating subsidiaries in others.

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[101] *Ibid.*, Regulation No. 2407/92, Art. 1(1).

[102] *Ibid.*, Arts. 4, 5(1), 7, & 8(1).

[103] *Ibid.*, Art. 3(1).

[104] *Ibid.*, Art. 3(2).

[105] *Ibid.*, Art. 4(2).

However, in one respect there will be less flexibility than at present, in that it will no longer be possible for Member States to allow control by non-EC nationals.

B. Market Access

Regulation 2408/92 significantly advances the process of liberalization of access to routes within the EC started by the first and second packages. It applies to routes within the EC for scheduled and non-scheduled air services (subject to temporary exemptions for Gibraltar, the Greek Islands and Azores).

Member States must permit any community air carriers to exercise traffic rights on any routes between two airports within the EC[106] subject to certain exceptions:[107] a Member State's right to distribute traffic within an airport system and the right for a Member State to limit or refuse access when serious congestion or environmental problems exist.

Cabotage need not be permitted until April 1997 unless it is consecutive cabotage[108] and not more than 50% of seasonal capacity on the primary route is used for cabotage traffic.[109] As regards carriers licensed by it, a Member State may

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[106] Regulation No. 2408/92, *supra* note 100, Art. 3(1).

[107] *Ibid.*, Arts. 4, 8(1), 8(2) & 9.

[108] Consecutive cabotage represents the situation where a Community air carrier from country A wants to serve a domestic route in country B, such route must be a continuation of or preliminary to serve originating in and respectively destined for a point in country A, see P.P.C Haanappel, "Recent European Air Transport Development" (1992) 17:2 Ann. of Air & Sp. L. 217 at 222.

[109] *Ibid.*, Art. 3(2).

continue to regulate access to domestic routes, but only without discrimination on grounds of nationality of ownership and air carrier identity, whether incumbent or applicant on routes concerned.[110]

The continuing limitations on cabotage are inconsistent with the principle of the internal market. However, airlines may be able to overcome some of the limitations by establishing a subsidiary company in another Member State. Moreover, cabotage will be fully liberalized automatically from April 1997 - no further legislation is needed.

While it may remain possible, until April 1997 at any rate, for Member States substantially to maintain monopolies for their national carriers in respect of domestic routes, they must basically allow all Community air carriers access to routes between two Member States.

No capacity limitation may be applied as between Member States, although the Commission may authorize stabilizing measures if this leads to serious financial damage for scheduled carriers of a Member State.[111]

C. Fares and Rates

As a basic rule, fares and rates, including charter fares, seat fares and cargo rates,[112] may be freely set.[113] However, pricing freedom for airlines will be limited

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[110] *Ibid.*, Art. 3(4).

[111] *Ibid.*, Art. 10.

[112] *Ibid.*, Regulation No. 2409/92, *supra* note 100, Art. 1.

by the disapproval of a Member State concerned. A Member State may decide to disapprove a fare that is excessive or too low in relation to long term fully allocated costs of the carrier, including return on capital. Disapproval takes effect only if (i) within 14 days no other Member State or the Commission disagree, or (ii) after investigation, the Commission determines that disapproval is justified.[114] In the case of conflict between Member States, the Commission may fulfil a dispute settlement role. Although this regulation does not generally apply to non-EC carriers, it provides that "only community air carriers may introduce new products or lower fares than ones existing for identical products".[115] This obviously has implications for fifth freedom operations within the EC by non-EC carriers.

D. Competition

Previously the Commission could only enforce the rules in respect of air transport between two Member States. Regulation 2410/92 extends the Commission's power to cover domestic air transport within a Member States and took effect on 25 August 1992.[116]

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[113] *Ibid.*, Art. 5(1).

[114] *Ibid.*, Arts. 6 & 7.

[115] *Ibid.*, Art. 3(3).

[116] Regulation No. 2410/92, *supra* note 100.

In order to issue "block exemptions", the Commission needs authority to do so. Regulation 2411/92[117] amends the scope of the previous authority, taking effect as of 27 August 1992. The new regulation changes the scope of authority given to the Commission to issue exemptions: it does not actually amend the present block exemptions. However, the Commission will soon be issuing new block exemptions on the basis of the new authority.

Whereas the jury is still out on the competition regime which will apply during the third phase of EEC air transport liberalization, the areas of air carrier licensing, market access, and tarriffs can already be evaluated.[118]

The air carrier licensing system can indeed be considered as very liberal; it actually resembles the "fit, willing, and able" system which characterises deregulated American and Canadan air carrier licensing. The market access regime is subject to many restrictions on route entry.

In the area of scheduled passenger fares, the third phase is also more restrictive than many had expected and hoped in a sense that EC Member States and EC Commission retain considerable power over scheduled fares.

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[117] Regulation No. 2411/92, *supra* note 100.

[118] P.P.C. Haanappel, *supra* note 108 at 223: For effects of third package, see Appendix II. Comparison between Third and Second package.

CHAPTER II

INCOMPATIBILITIES CAUSED BY EC LIBERALIZATION WITH PRESENT REGULATORY SYSTEM OF INTERNATIONAL AIR TRANSPORT

The basis for the regulatory framework of postwar international civil aviation was laid down by the International Civil Aviation Conference, held in Chicago in 1944.[119] As a compromise between the different positions, the Chicago Conference distinguished between institutional and technical questions on the one hand and economic or commercial matters on the other. However, this Conference, a success in the technical field of civil aviation, left many economic questions of postwar international civil aviation unresolved.[120] The failure of the Chicago Conference to produce a large scale multilateral agreement on the economic regulation of postwar international air transport induced States to exchange air traffic rights between their territories on the basis of bilateral air transport agreements. The airlines themselves took the initiative and created IATA for the international regulation of rates and fares.[121] Since then, the world civil aviation industry has achieved a rapid growth under the present regulatory system, which consisted of the Chicago Convention, bilateral air transport agreements and IATA,

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[119] International Civil Aviation Conference, Chicago (Nov. 1 - Dec. 7, 1944) ICAO Doc. 2187 [hereinafter *Chicago Conference*].

[120] For details about Chicago Conference, see Haanappel, *supra* note 2 at 9-18.

[121] Haanappel, *ibid.* at 7.

characterized by nationalism, protectionism and bilateralism, which prevented true competition and built up national carriers.

However, the common air transport policy of the European Communities creating an internal market may significantly affect the present regulatory system. In particular, the concepts of "Community air carrier"[122] and "community cabotage area"[123] coupled with the application of competition rules are likely to be incompatible with the current system.[124] In this connection we will analyse four subjects: nationality of aircraft, cabotage, bilateral air transport agreements, and IATA, all of which are likely to influence directly the relations between the EC and non-EC countries.

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[122] "Community air carrier" is defined as follows:
"an air carrier which has and continues to have its central administration and principal place of business in the Community, the majority of whose shares are and continue to be owned by Member States and/or nationals of Member States and which is and continues to be effectively controlled by such States or persons", Council Regulation No. 2343/90, *supra* note 71, Art. 2(e).

[123] The concept of a "Community cabotage area", where traffic within and between Member States would be considered to be equivalent to cabotage and in principle reserved for Community carriers, was introduced by the Commission: *Communication on community relations with third countries in aviation matters*, proposal for a Council Decision, COM (90) 17 final, Brussels, Feb. 23, 1990, para. 37-42.

[124] Weber, *supra* note 8 at 277-278.

II-1 NATIONALITY OF AIRCRAFT

National ownership and control criteria for airlines are replaced by Community criteria to make it possible for citizens of Community countries to establish airlines in other Community countries.[125]

The concept of community air carrier is likely to be incompatible with the principle of nationality of aircraft as embodied in the present regulatory system of international air transport.[126]

The legal status of aircraft, including its definition and its treatment under international and national law, may undergo changes associated with progress made in flight technology and application.[127] From the beginning of this century, the status of aircraft began to attract the attention of lawyers, followed by legislators as it began to be recognized informally that aircraft had something resembling national status.[128]

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[125] *Supra* note 105.

[126] The nationality of airlines, which is also affected by the community clause, will be discussed in Chapter II at 3-2.

[127] Marek Zylicz, *International Air Transport Law* (Dordrecht: Martinus Nijhoff, 1992) at 67.

[128] For details of the legal status of aircraft, see J.C. Cooper, *Explanations in Aerospace Law: selected essays edited by I.A. Vlasic* (Montreal: McGill University, 1968) at 205-254.

The principle of aircraft nationality was formally incorporated into the Paris Convention of 1919,[129] and the Chicago Convention contains several provisions concerning the nationality of aircraft.[130] As one of the consequences of aircraft nationality, the State of registration may bear international responsibility for the conduct of its national aircraft. This is reflected in the undertaking by each State to ensure that every aircraft carrying its national mark, wherever such aircraft may be, shall comply with the rules of the air there in force.[131] Therefore, regarding Community air carriers

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[129] *Convention Relating to the Regulation of Aerial Navigation*, signed at Paris on 13 October 1919, 11 LNTS 173; 1922 UKTS 2; (1965) 3 *Air Laws and Treaties of the World* 3085, Art. 5.

[130] Chicago Convention, *supra* note 1, Arts. 17-21. The articles applicable directly to "Nationality of Aircraft" constitute Chapter III of the Chicago Convention and are as follows:

Article 17: Aircraft have the nationality of the State in which they are registered.

Article 18: An aircraft cannot be validly registered in more than one State, but its registration may be changed from one State to another.

Article 19: The registration or transfer of registration of aircraft in any contracting State shall be made in accordance with its laws and regulations.

Article 20: Every aircraft engaged in international air navigation shall bear its appropriate nationality and registration marks.

Article 21: Each contracting State undertakes to supply to any other contracting State or to the International Civil Aviation Organization, on demand, information concerning the registration and ownership of any particular aircraft registered in that State.

[131] *Ibid.*, Art. 11. To deal with the problems that may arise in the case where an aircraft is registered in one State and used by an operator having his principal place of business or permanent residence in another State, Article 83 bis was adopted on 6 October 1985 to provide for the possibility of the transfer of certain functions and duties with respect to an aircraft from the State of registry to the State of the operator, in case of lease, charter and interchange of aircraft: ICAO, *Protocol relating to an amendment to the Convention on International Civil Aviation* [Article 83 bis] ICAO Doc. 9318 (signed on 6 October 1980, not yet in force). For details about Article 83 bis, see Gerald F. FitzGerald, "The Lease and Charter and Interchange of Aircraft in International Operations - Article 83 bis of the Chicago Convention on International Civil

the basic question will be raised: which Member State will be (1) the registrar of aircraft owned by Community air carriers and (2) responsible for the conduct of those aircraft?

In the case of SAS (Scandinavian Airline System), the consortium owns the aircraft contributed to it as part of the capital as well as aircraft later acquired by it, but these aircraft are registered as follows: 3/7 of each type of aircraft in Sweden; 2/7 in Denmark; and 2/7 in Norway. This avoids contravention of Article 18 of the Chicago Convention.[132] However, the SAS case will not be applied to community air carriers because of difficulties in decision-making concerning apportionment between Member States.

On the other hand, the Chicago Convention allows airlines to be multinational enterprises, subject to the provisions of the Convention.[133] Article 77 of the Chicago Convention specifies that "the Council shall determine in what manner the provisions of this Convention relating to nationality of aircraft shall apply to aircraft operated by joint air transport operating organizations or international operating agencies".

In 1983, according to the ICAO Council's determination, Arab Air Cargo's aircraft are registered in a joint register, separate and distinct from the national registers of Jordan and Iraq, and maintained by the Government of Jordan which, on behalf of the

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Aviation" (1981) 6 Ann. Air & Sp. L. 49 at 49-65.

[132] N.M. Matte, *Treatise on Air-Aeronautical Law* (Toronto: Carswell Co. Ltd., 1981) at 181.

[133] Chicago Convention, *supra* note 1, Arts. 77-79.

two carriers, fulfils the functions of the State of registry under the Chicago Convention.[134] Besides this Council determination, an ICAO Council Regulation of 14 December 1967 would in principle allow aircraft registration with an international organization having legal personality.[135] That could possibly include the EC and its supranational institutions. An important issue in this respect is whether the ICAO Council will allow an international organization, and more particularly, a supranational organization such as the EC, to perform the tasks of a state of registry.[136]

The opinions are divided. Dr. Michael Milde has stated that such performance is impossible, since it would necessitate an amendment to the Chicago Convention.[137]

Prof. P.P.C. Haanappel suggests that "the possibility of the EC performing state of registry functions should exist, even now, by way of an ICAO Council determination under Article 77 of the Chicago Convention. He attaches three conditions to this possibility:[138] (a) that the setting up of a non-national EC aircraft is tied in with the creation by the EC States, all being members of ICAO and acting through the Council of the European Communities, of an "international operating agency" or "agencies"; (b) that the EC States are jointly and severally bound to assume the obligations which the

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[134] M. Milde, "Nationality and Registration of Aircraft Operated by Joint Air Transport Operating Organization or International Operating Agencies" (1985) 10 Ann. Air & Sp. L. at 133.

[135] *Ibid.* at 147.

[136] Haanappel, *supra* note 21 at 143.

[137] Milde, *ibid.* at 151.

[138] Haanappel, *ibid.* at 144.

Chicago Convention places on a State of registry; and (c) that there are sufficient guarantees that the provisions of the Chicago Convention will be complied with.

II-2 CABOTAGE

"Cabotage", first applied to maritime navigation,[139] is a term which, at present, is frequently used in international civil aviation. It is also referred to as the eighth freedom of the air,[140] indicating the carriage of traffic between two points which are both located within the territory of a foreign State. Traditionally, cabotage rights have been entirely denied or severely restricted by the generally accepted doctrine that every State should have the right to control its own affairs, including trade and commerce, within its own airspace.[141] As a result, national airlines have been carefully protected from foreign competition on domestic routes. However, cabotage between Member States of the EC is not compatible with the genuine, barrier-free internal market intended by the Single European Act. Moreover, the size of domestic air transport markets of Member States would make their exclusion from a market-based Community regime in

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[139] Pablo Mendes de Leon, *Cabotage in Air Transport Regulation* (Dordrecht: Martinus Nijhoff, 1992) at 1.

[140] Bin Cheng, *supra* note 1 at 15-17.

[141] Article 1 of the Chicago Convention states: "The Contracting States recognize that every State has complete and exclusive sovereignty over the airspace above its territory". Article 2 of the Chicago Convention defines "territory" as "the land areas and territorial waters adjacent thereto under the sovereignty, suzerainty, protection or mandate of such State" thereby providing for cabotage, the right to reserve traffic between a State and its overseas possessions.

air transport a serious impediment to the liberalization of international traffic. As domestic services also serve intra-Member State traffic, their exclusion would hinder the development of one of the principal instruments for achieving integration: free competition.[142] Therefore, according to the third package the exchange of cabotage rights between Member States is permitted in spite of some limitations. Moreover, cabotage will be fully liberalized automatically from April 1997.[143]

II-2-1 ARTICLE 7 OF THE CHICAGO CONVENTION

The basic legal framework regarding the grant of cabotage rights is laid down by the Chicago Convention. Article 7 allows States to reserve cabotage traffic to their own aircraft and furthermore forbids the Contracting States to exchange cabotage rights on an exclusive basis.[144] The first sentence of Article 7 creates no problems since it allows each ICAO Contracting State to refuse to grant permission to the aircraft of other

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[142] Jan Erst C. de Groot, "Cabotage Liberalization in the European Economic Community and Article 7 of the Chicago Convention" (1989) 14 Ann. Air & Sp. L. 139 at 151-152.

[143] *Supra* note 109.

[144] Article 7 of the Chicago Convention states: "Each Contracting State shall have the right to refuse permission to the aircraft of other Contracting States to take on in its territory passengers, mail and cargo carried for remuneration or hire and destined for another point within its territory. Each Contracting State undertakes not to enter into any arrangements which specifically grant any such privilege on an exclusive basis to any other State and not to obtain any such exclusive privilege from any other State."

Contracting States to carry domestic (cabotage) traffic within its territory.[145] However, the second sentence has been open to interpretation. The meaning of the restriction contained in the sentence has been clouded, due to the ambiguous terms "specifically" and "on an exclusive basis". Two interpretations of this language have been postulated by legal scholars.[146] The first approach, referred to as the strict approach, places the emphasis on the phrase "on an exclusive basis". Under this approach cabotage privileges can only be granted on a non-exclusive basis, creating an absolute prohibition against discriminatory grants. This means that cabotage rights may either be granted to no other State, or to all States which request such rights. The second approach, deemed the flexible approach, places the emphasis on the phrase "specifically". Under this approach cabotage rights can be granted on an exclusive basis where it is not stipulated that they are exclusive, without third States having the right to demand similar privileges. Therefore States may make arrangements granting cabotage rights to other States so long as the agreement does not explicitly state that the rights are exclusive. The second approach has been applied in ICAO practice for the SAS case.[147]

It is not clear whether the exchange of cabotage rights between EC Member States is compatible with Article 7 of Chicago Convention.

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[145] Haanappel, *supra* note 21 at 138.

[146] Douglas R. Lewis, "Air Cabotage: Historical and Modern-Day Perspective" (1980) 45 J. Air L. & Com. 1059 at 1062-1065.

[147] Weber, *supra* note 8 at 282.

Although there is no stipulation of exclusivity in this grant of cabotage rights, the fact that it is made through Community measures, which naturally only apply to Member States, will result in an appearance of exclusivity.[148]

An SAS-type safeguard clause, providing for termination of the availability of intra-community cabotage rights in case a third country demanded the same rights based on Article 7 of the Chicago Convention, does not seem compatible with the stability of the Community legal order, as it would lead to unacceptable uncertainty.[149] In practice, third state intervention did not occur in the SAS case because the routes at issue were not deemed commercially attractive by third states or possibly because no fifth-freedom rights were affected.[150] In the European Community, on the other hand, a substantial number of commercially attractive cabotage routes exist.[151] For this reason, it is entirely possible that the other non-EC members of ICAO will be unwilling to accept the establishment of a Community cabotage area under the SAS approach.[152]

Without such a safeguard clause, an amendment of Article 7 of the Chicago Convention will be required if the Community is to pursue its objective.[153] If the second sentence of Article 7 is deleted, Member States would still be free under the first

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[148] *Ibid.*

[149] Haanappel, *ibid.*

[150] Platt, *supra* note 70 at 187.

[151] *Ibid.*

[152] *Ibid.*

[153] Weber, *supra* note 8 at 283.

sentence of Article 7 to refuse to grant cabotage rights to other States or airlines thereof; on the other hand, if they wish to grant and/or obtain cabotage rights in other countries, they could then deal with such rights as they deal with any other air transport rights, i.e. they may negotiate and exchange them exclusively with the country or countries involved.[154] However, the deletion of the second sentence of Article 7 is not likely to occur in the short run. According to Article 94 of the Chicago Convention, amendments to the Convention must be approved by a two-thirds majority vote of the Member States of ICAO and must be ratified by at least that number.

Therefore it can be expected that this subject will be discussed among ICAO Member States before the Community proceeds to take concrete steps for the adoption of a respective Community measure.[155]

II-2-2 "COMMUNITY CABOTAGE AREA"

The completion of the European internal market as defined in Article 8a of the EEC Treaty will not turn the Community into a single political entity under public international law. Its Member States will remain separate and independent states to which the Chicago Convention will continue to be applicable.[156] Traffic between

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[154] Haanappel, *supra* note 21 at 139.

[155] Weber, *ibid.*

[156] Ludwig Weber, "Effect of EEC Air Transport on International Cooperation" (1989) 24 European Transport Law 448 at 452.

Member States will still be regarded as international and will not qualify as cabotage. Therefore there is no legal basis for existing, or new fifth freedom rights between points in the Community countries to be considered as cabotage, and Article 7 of the Chicago Convention cannot serve to deny fifth freedom rights to non-EC air carriers.[157].

However, the concept that fifth freedom rights within the Community are a "Community asset", even if not used as a justification for considering the Community airspace as a "cabotage area", will certainly recommend that any negotiation on fifth freedom rights for third countries in Europe will be subject either to a coordination of negotiating positions of the several Member States or to a Community joint negotiation procedure.[158]

One possible strategy for the EC might be to renegotiate (e.g. with the U.S.) bilateral agreements with third countries on the basis that current fifth freedom rights would be eliminated unless additional compensation for European carriers (cabotage) were provided in exchange for those rights. All this would not be founded in legal arguments related with Article 7 of the Chicago Convention, but in purely political and aviation policy considerations.[159] But such an approach does not seem feasible as it would most certainly produce an undesirable block-forming climate and provoke international tensions.

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[157] Vilao, *supra* note 14 at 122.

[158] *Ibid.* at 125.

[159] Weber, *supra* note 8 at 286.

II-3 BILATERAL AIR TRANSPORT AGREEMENTS

The cornerstone of the Chicago Convention is the recognition that each State has complete and exclusive sovereignty over its airspace. This fundamental principle is the basis of the more than 2,500 inter-governmental bilateral air service agreements which regulate international air transport markets and determine market access, capacity and pricing conditions.[160] The present bilateral regulatory sytem emphasises the national ownership and control of airlines and the primary importance of traffic to and from the designating State as a basis for the provision of capacity. It also provides for a balance and reciprocal exchange of rights between two States on the basis of "fair and equal opportunity" and reciprocity. However, the concept of "Community Cabotage Area" was intended to meld Member States together in order to form one block in international aviation relations, and the concept of "Community air carrier", does away with national designation clauses. Together, these two concepts will influence future bilateral air transport agreements between Member States and non-EC countries.

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[160] IATA White Paper, *supra* note 3 at 2.

II-3-1 REPRESENTATIVE[161]

According to developments in the EC common transport policy toward a truly integrated internal market, there is an urgent need to clarify whether the Community will negotiate as a single entity with third countries or whether Member States will maintain their traditional competence for external aviation negotiations. Member States do not appear to be willing to allow their sovereignty to be transferred to the Community in respect to aviation agreements with third counties.

Traffic rights granted under bilateral agreements are considered to be the property of States for the benefit of their designated airlines, and a joint EC negotiation would pose obvious problems of internal distribution of the traffic rights granted to Community carriers in the course of negotiations. Conflicts of national interest could arise, and a non-discriminatory mechanism of designation of airlines would have to be adopted.

However, the necessity of a common air transport policy, the avoidance of conflicts between Member States and a much stronger bargaining position will eventually lead Member States to seek to coordinate as a block in bilateral agreements with third countries.

A recent communication of the Commission to the Council on "Air transport relations with third countries" proposed the full involvement of the Commission in the

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[161] EC external civil aviation competence will be discussed in detail in Ch. III-1.

negotiation process by giving it power to monitor and review provisions contrary to EC law.[162]

II-2-2 SUBSTANTIAL OWNERSHIP AND EFFECTIVE CONTROL

According to traditional bilateral agreements, a Contracting Party has the right to withhold or revoke its operating permission to an airline or airlines from the other Contracting Party in any case where it is not satisfied that the airline or airlines are "substantially owned and effectively controlled" by nationals of that Contracting Party. But in the EC, national ownership and control criteria for airlines are replaced by community criteria so as to make it possible for citizens of Community countries to establish airlines in other Community countries.

Requirements of national ownership or control are not compatible with the general principle of non-discrimination on grounds of nationality within the Community,[163] nor with the right of establishment and the freedom to provide services.

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[162] Communication from the Commission to the Council on Air Transport with Third Countries, COM (92) 434 final, Brussels, 21 October 1992.

[163] Article 7 of the EEC Treaty states: "Within the scope of application of this Treaty, and without prejudice to any special provisions contained therein, any discrimination on grounds of nationality shall be prohibited".

The Commission, in a letter sent in September 1989 to all Member States, has urged them to amend their bilateral agreements with third countries in order to introduce a Community ownership and control clause which reads as follows:[164]

> "The ownership of the air carriers designated to operate the services provided for in the Annex to this Agreement on behalf of the Party that is a member of the European Communities must have its central administration and principal place of business in the Community, the majority of whose shares are owned by nationals of Member States and/or Member States and which is effectively controlled by such persons or states."

It has been argued that Member States are not legally required to follow the Commission's request in their bilateral agreements, as long as they maintain their external relations competence in aviation matters.[165] However, the national ownership and control clause will soon create an incompatibility with international agreements and the Community legal order, and will therefore have to be eliminated under Article 234 of the EEC Treaty.[166]

Nevertheless, there is no realistic prospect for any alternative system to supersede existing bilateral air transport agreements on a world scale in the near future. Therefore, the bilateral system with its principles of fair and equal opportunity and reciprocity, will probably continue to function despite changes in airline ownership and control.

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[164] *Supra* note 123, para. 14.

[165] Weber, *supra* note 8 at 283.

[166] Art. 234 of the EEC Treaty states: "... to the extent that such agreements are not compatible with this Treaty, the Member State or States concerned shall take all appropriate steps to eliminate the incompatibilities established...".

It might be left to the designating State to determine whether it is satisfied with the ownership of an airline.[167] "Community air carriers" could be accommodated within the traditional system if non-community States accept that an air carrier operating from as EC state does not need to be owned and controlled any longer by that state, provided that it is substantially Community-owned and controlled.[168] This approach may be a useful bargaining chip for Korea in bilateral agreements with the EC or Member States of the EC.

II-4 INTERNATIONAL AIR TRANSPORT ASSOCIATION

After the failure of the Chicago Conference to establish a comprehensive multilateral system to regulate international commercial air services, such regulation became the object of bilateral air transport agreements. However, recognizing the need for world-wide co-ordination of tariffs and relevant conditions, governments found it convenient to leave that duty to IATA as the best qualified specialized organization, subject - where necessary - to government control.[169]

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[167] IATA White Paper, *supra* note 3 at 22.

[168] *Ibid.*

[169] Zylicz, *supra* note 127 at 157.

Reference to the IATA conference machinery was made in the Bermuda I agreement [170] and in a great number of other bilateral air transport agreements since the Second World War.[171]

According to the Articles of the Association,[172] the aims and objectives of the IATA are:

(a) to promote safe, regular and economical air transport for the benefit of the peoples of the world, to foster air commerce and to study the problems connected therewith

(b) to provide means for collaboration amoung the air transport enterprises engaged directly or indirectly in international air transport service;

(c) to co-operate with the ICAO and other international organizations.

These abstract objectives have materialized in five major activities of the organization:[173] tariff "coordination"; interlining "co-operation"; organization of a

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[170] Paragraph (b) of Annex II to Bermuda I agreement relates to the determination of international air fares and rates in the IATA rate making machinery. The paragraph reads:
"The Civil Aeronautics Board of the United States having announced its intention to approve the rate conference machinery of the International Air Transport Association (hereinafter called *IATA*), as submitted, for a period of one year beginning in February, 1946, any rate agreements concluded through this machinery during this period and involving United States air carriers will be subject to approval by the Board."

[171] Zylicz, *ibid.*

[172] IATA, Rules and Regulations Handbook (1990).

[173] Andreas Loewenstein, *European Air Transport within the International System of Air Regulation* (LL.M. Thesis, McGill University, Institute of Air & Space Law, 1990) at 250.

"distribution system"; technical, economic and legal study and assistance; and lobbying with international and national authorities.

IATA is continuously adjusting its legal structure and practices, largely due to outside pressure.[174] The EC liberalization measures in the air transport field, especially the European-wide competition regime based on Articles 85 and 86 of the EEC Treaty are no longer compatible with some of the activities of IATA any longer.

Until now the Commission has not issued new block exemptions.[175] Therefore, some activities of IATA such as tariff coordination and interlining cooperation are immune from the competition law of the EC. However, in the near future, the tariff coordination function of IATA will disappear, at least in relation to the carriers of Member States of the EC within the EC and international air routes between Member States and non-EC Countries, because fares and rates including charter fares, seat fares and cargo rates may be freely set between Member States.[176] According to the *Ahmed Saeed* case, the EC competition rules will be applied to international air transport routes between the EC and non-EC countries.

As regards the interlining co-operation function of IATA, certain interlining co-operation concerning technical[177] and operational ground handling, refuelling and

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[174] IATA's Reorganization, see Haanappel, *supra* note 2 at 61-63.

[175] See Ch. I-4-3 at 27, above.

[176] *Supra* note 113.

[177] The category of technical co-operative interlining agreements appeared in Annex I of Council Regulation No. 3975/87, *supra* note 47.

security services, handling of passengers, mail, freight and baggage at airports and in-flight catering will probably continue to be allowed within the EC and elsewhere provided that the sharing of these services is arranged on a non-discriminatory basis and that outside carriers are not excluded from essential facilities at airports.

However, other interlining co-operation such as joint operations, capacity sharing, revenue pools, royalty agreements[178] and so on are classified two categories according to its anti-competitive effects.[179]

Agreements which may have strong anti-competitive effects are joint operations; royalty agreements; revenue pools; capacity sharing and so on. This category of co-operation agreements will be prohibited under the EC law because it restrains, hinders or distorts free competition. Another category of agreements which have a less significant impact on competition and may contribute to certain efficiencies in the air transport system are likely to be exempt from the EC law on condition that their effect on competition will be regularly investigated. These are agreements concerning co-operation on computer reservation systems, code-sharing, joint schedules and so on.

IATA's agencies programme based on objective rather than quantity-restricting criteria, allowing access to the distribution network for every travel agent fulfilling the

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[178] For an explanation of joint operations, capacity sharing, revenue pools, royalty agreements Organization for Economic Co-operation and Development, *Deregulation and Airline Competition* (OECD: Paris, 1988) at 67-74.

[179] *Ibid.*

set conditions such as sufficient financing, equipment requirements, etc. will be compatible with EC law.[180]

As mentioned above, EC liberalization measures will influence the function of IATA to such a degree that it will have to reform its structure to survive as global air carrier association.

[180] Loewenstein, *supra* note 173 at 189.

CHAPTER III

EXTERNAL RELATIONS OF THE EC WITH NON-EC COUNTRIES

The EC's air transport relations with countries outside the Community fall into two groups:[181] relations with non-EC countries within Europe and relations with countries outside Europe. External relations within Europe, particularly in the context of EFTA (European Free Trade Association)[182] and with respect to Eastern European Countries, in the process being developed.

However, EC external relations with countries outside Europe have not really been addressed yet, although the Commission has made several proposals in this respect, both in the field of the application of EC competition law to air routes to/from the Community and in the field of traffic rights. It is anticipated that EC external air transport relations with countries outside Europe will be given higher priority with the possible aim of developing a general EC policy for such relations in the years to come. This is because air transport relations between the EC and countries outside Europe have become, now that the EC internal air transport market has been largely completed,

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[181] Memorandum of IATA, *Recent European Air Transport Development* (July 1992) para. 6-2.

[182] EFTA consists of seven countries: Austria, Finland, Iceland, Liechtenstein, Norway, Sweden and Switzerland.

politically, the most sensitive air transport subject in the Community.[183] Also the creation of the EC single market may seriously affect non-EC countries' traffic rights to, from and within the EC. Therefore, non-EC countries are very concerned about EC policy toward them.

III-1 EXTERNAL COMPETENCE[184] OF THE EC IN AIR TRANSPORT

III-1-1 EXCLUSIVE COMMUNITY COMPETENCE FOR AVIATION BILATERALS

There are two alternative paths which the Community, represented by the Commission,[185] might pursue in obtaining competence in the field of air transport.[186]

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[183] P.P.C. Haanappel, "Recent European Air Transport Development: 1992-93" (1993) 18 Ann. Air & Sp. L. 1 at 8.

[184] The term "competence" denotes legal authority to act in a field of policy. It differs only in emphasis from the notion of "power", which indicates the authority to use an instrument by which competence is exercised: thus there is *norm-setting power* (legislative power and treaty making power), *executive power* (representation, administrative execution, and so on), and *judicial power*. See Nanette A. Neuwahl, "Joint Participation in International Treaties and the Exercise of Power by the EEC and Its Member States: Mixed Agreements" (1991) 28 Common Market L. Review 717 at 718.

[185] The Commission of the EC is organized into 23 Directorate Generals. Three of the DGs are of particular importance for air transport. First, DG1 is responsible for negotiation of treaties between the EC and other countries. The second is DG4, whose responsibilities are the enforcement of the Community's competition laws. The third, DG7 is directly responsible for transportation. For details about the European Community Institutions, see M.W. Tretheway, *supra* note 28 at 12-22.

[186] Tretheway, *ibid.* at 53.

One is that Article 113[187] of the EC Treaty gives broad power to the Commission to negotiate with non-EC countries. If it is determined that Article 113 applies to air transport, the Commission would not need to seek specific authorization from the Council every time it needs to conduct a negotiation. The other path is via Article 84, paragraph 2,[188] which applies specifically to transportation industries. Under Article 84 (2), the Council determines the competency of the Commission on a case-by case basis.

In its Communication entitled "Community Relations with Third Countries in Aviation Matters"[189] the Commission adopted a new policy objective, which was to have negotiations with third countries in matters of commercial air policy treated as part

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[187] Article 113 of the EEC Treaty states:

"1. After the transitional period has ended, the common commercial policy shall be based on uniform principles, particularly in regard to changes in tariff rates, the conclusion of tariff and trade agreements, the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to be taken in case of dumping or subsidies.

2. The Commission shall submit a proposal to the Council for implementing the common commercial policy.

3. Where agreements with third countries need to be negotiated, the Commission shall make recommendations to the Council, which shall authorise the Commission to open the necessary negotiations.

The Commission shall conduct these negotiations in consultation with a special committee appointed by the Council to assist the Commission in this task and within the framework of such directives as the Council may issue to it.

4. In exercising the powers conferred upon it by this Article, the Council shall act by a qualified majority."

[188] Paragraph 2 of Article 84 of the EEC Treaty states: "The Council may, acting by a qualified majority, decide whether, to what extent and by what procedure appropriate provisions may be laid down for sea and air transport. The procedural provisions of Article 75(1) and (3) shall apply."

[189] *Supra* note 123.

of the commercial air policy. The Commission's reasoning is as follows:[190] the exchange of goods and services with third countries is the subject of the common commercial policy; international air transport is a service; therefore the exchange of international air services between the Community and third countries is a matter for the common commercial policy.

The application of the Commission's reasoning requires that Article 113 of the EEC Treaty become the appropriate legal basis for negotiating and concluding agreements with third countries on commercial matters.[191] This means that the Community would have exclusive competence and that the Member States would not be able to conclude bilateral air transport agreements with third countries.[192] On the other hand, the Commission asserted that Community competence in other than commercial aspects depended on the results of the application of the case law of the Court of Justice[193] in the AETR (the European Agreement concerning the work of crews of vehicles engaged in international road transport) judgement[194] or in opinion 1/76.[195]

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[190] G.L. Close, "External Competence for air policy in the third phase - trade policy or transport policy?" (1990) 15:5/6 Air L. 295 at 295.

[191] *Ibid.*

[192] The Communication, *supra* note 123, para. 24.

[193] *Ibid.*, para. 25.

[194] Case 22/70 [1971], E.C.R. 263. In its AETR decision of 1970, ECJ held that to the extent the Community internally laid down common rules on a given subject matter, the Community acquired the power to negotiate and conclude international agreements on that subject matter with third countries. See Ludwig Weber, "EEC Air Transport Liberalization and the Chicago Convention" (1992) 17:1 Ann. Air & Sp. L. 245 at 258.

This Communication was the first occasion when the Commission asserted that common commercial policy comprehends the external aspects of transport. Indeed in the past, its position with respect to the transport sector generally was that there was a situation of parallel competence, which means that Member States retain their competence to conclude agreements with third countries, except in two limited cases. These are, first, where there was Community competence by virtue of internal Community legislation which would necessarily affect external negotiations (the AETR case) and, second, where the Council had decided that it was necessary that the Community itself should negotiate (opinion 1/76).[196]

In the new Communication entitled "Air Transport Relations with Third Countries" the Commission, eager to see its alleged exclusive competence confirmed by the Council, repeats its point of view that common external aviation policy will cover provisions governing matters which fall within the meaning of article 113 of the EEC Treaty. Such provisions may be maintained in force until December 31, 1998, if not covered by Community agreements and if these are not contrary to the common external aviation policy.[197]

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[195] Opinion 1/76 given prusuant to Article 228(1) of the EEC Treaty [1977], E.C.R. 741. In this opinion the Council had expressly conferred competence on the Community where necessary to achieve Treaty objectives. See G.L. Close, "External Relations in the Air Transport Sector: Air Transport Policy or the Common Commercial Policy?" (1990) 27 Common Market L. Review 107 at 110-112.

[196] *Ibid.* at 109-110.

[197] *Supra* note 162, Article 5 of the proposal amended Council Decision.

However, Article 113 applies to a very specific field only, i.e. tariff and trade negotiations with third countries.[198] As long as air transport and other services are excluded from the scope of the General Agreement on Tariffs and Trade (GATT), Article 113 does not seem particularly relevant to the Community's treaty making power in the field of air transport.[199] The Draft General Agreement on Trade in Services and the attached drafts of sectoral agreements were submitted to GATT Brussels meeting in December 1990. The air transport services annex creates an extremely important limitation to the application of the general provisions of the agreement by stating that no provision of the latter shall apply to traffic rights and - tentatively - to all related activities that would limit or affect the ability of the parties to negotiate, to grant or to receive traffic rights, or that would have the effect of limiting their exercise. It is, however, tentatively proposed that the provisions of the agreement must apply to an agreed list of activities, subject to periodical revision, including aircraft repair and maintenance, CRS, selling and marketing of air transport services and ground handling services.[200]

On the other hand, Article 113 forms part of the title on common commercial policy and relates to Article 3(b)[201] of the EEC Treaty. However, transport is subject

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[198] Article 113(1) of the EEC Treaty

[199] Haanappel, *supra* note 21 at 84.

[200] Zylicz, *supra* note 127 at 178.

[201] Article 3(b) of the EEC Treaty states: "(b) the establishment of a common customs tariff and of a common commercial policy towards third countries."

to Article 3(e)[202] of the EEC Treaty because Article 3(e) is more specific in its application than Article 3(b), and more directly related to the subject-matter of air transport negotiations, the legal regime flowing from Article 3(e) ought to apply to external air transport relations. This suggests that Article 84, which is directly related to air transport, rather than Article 113, which is related to common commercial policy, ought to govern. Furthermore, Article 74 of the EEC Treaty expressly states that the objectives of the Treaty shall, in matters governed by this [transport] Title, be pursued by Member States within the framework of a common transport policy. Article 75 of the EEC Treaty expressly refers to the need to take into account the "distinctive features of transport" when implementing Article 74. Articles 74 and 75 therefore appear to specify that air transport is to be treated as a distinctive head of jurisdiction and not as part of general commercial policy. All of this points to the application of Article 84(2) rather than Article 113. Also, from the practical point of view, Article 84(2) gives room for the application of the "subsidiarity" principle. Individual Ministers in the Council take into account their national interests and each of them can argue that its government in a certain matter acts independently from the Council on the basis of the "subsidiarity" principle, meaning that what national authorities can do, should not be done by the Community.[203]

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[202] Article 3(e) of the EEC Treaty states: "(e) the adoption of a common policy in the sphere of air transport."

[203] H.A. Wassenbergh, "The external relations of the EEC after January 1, 1993" (1993) in material for the Guest Lectures of Prof. H.A. Wassenbergh at McGill University, IASL, March 1993 at 49. For details about the history and development of the principle of subsidiarity, see D.Z. Cass, "The Word that Saves Maastricht? The Principle of Subsidiarity and the Division of Powers within the European Community"

Therefore, Article 84(2) will be likely viewed as the legal basis of the Community competence for air transport.[204] It is also likely that the issue of Community competence will not be resolved by the Council of Transport Ministers, but rather will be dealt with at a higher level in the Council (i.e., the Council of First Ministers).[205]

III-1-2 COMMUNITY INVOLVEMENT IN BILATERAL AIR TRANSPORT NEGOTIATIONS

There are three possible ways to negotiate bilateral air transport agreements between the EC and non-EC countries. The first is that individual Member States of the EC negotiate their own bilateral agreements with individual non-EC countries. However, the necessity of a common air transport policy, the avoidance of conflicts between Member States and a much stronger bargaining position will eventually lead Member States to seek to coordinate as a block in bilateral agreements with non-EC countries.

According to the second approach, the Community, through the Commission, negotiates with non-EC countries on behalf, and in the name of individual Member

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(1992) 29 Common Market L. Review 1107 at 1110-1128.

[204] The Commission was granted competence under 84(2) to negotiate an air transport agreement with Norway and Sweden. However, it is not clear whether this was a precedent or whether it was an expendient due to the urgency of these particular negotiations. See Tretheway, *supra* note 28 at 53.

[205] *Ibid.* at 54.

States: this would imply that the Community acts only as a "negotiation agent" and leaves the role of Member States as bilateral partners of non-EC countries intact.[206] The relevant Member State sits behind the table and instructs the EC negotiator what position to take. This would allow the EC negotiators to be tutored by their more experienced counterparts in the Member States.[207] Thus, it would solve one of the problems with the EC negotiating agreements; the Community has no expertise and no institutional memory for negotiating very complicated air transport agreements. Another advantage of this approach is that the EC negotiators would likely see a broader picture, as they would be sitting at the table for all bilateral negotiations involving any EC Member State. This would allow them to identify common problems and themes.[208]

According to the third approach, the Community negotiates on its own behalf and in its own name. This way implies that the power and responsibilities for negotiating bilateral air transport agreements with non-EC countries have been formally transferred from Member States to the Community.[209] However, this would pose basic problems of internal distribution of the traffic rights granted to Community carriers in the course

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[206] Weber, *supra* note 194 at 250.

[207] Tretheway, *supra* note 28 at 54.

[208] *Ibid.*

[209] Already the Commission has conducted negotiations with Norway/Sweden and EFTA. However, there was a practical need in those cases: SAS, the close relation between the EC and EFTA countries. Also, it is predicted that the Commission could be allowed to negotiate on special issues with non-EC countries such as US-cabotage rights, etc.

of negotiations. Also, the Union Treaty,[210] the so-called "Maastricht Treaty" includes the EC, the Economic and Monetary Union (EMU), Foreign & Security policy and Justice and Home affairs. Unanimity will apply in the Council in matters of foreign and security policy of the States, Justice and Home affairs and industry, while a qualified majority is valid for the protection of the consumers and trans-European networks such as transport and telecommunications. The unanimity rule for aviation policy toward countries outside the EC leaves national sovereignty unimpaired.[211]

In December 1992 the Danish Presidency of the community circulated a discussion paper proposing that a pragmatic approach to relations with third countries should be taken: existing bilateral air transport agreements should be respected; EC Member States could continue to negotiate bilaterals; and any Community negotiations should be individually mandated.[212] Member States do not appear willing to allow their sovereignty to be transferred to the Community in respect to aviation agreements with non-EC countries. At this point it is not at all clear what direction the EC is going to take in the near future. The second approach, discussed above, is likely to be the most realistic approach. However, as the Community is unified more in other aspects such

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[210] Treaty on European Union, European Document No. 1759/60, (opened for signature 7 February 1992, entered into force 1 November 1993). See, for details about the Treaty, Common Market Reporter, (Chicago: Commer Clearing House Inc., 1992) at 10,011-10,027.

[211] H.A. Wassenbergh, "The European Union" in Material for the Guest Lectures of Prof. H.A. Wassenbergh at McGill University, IASL, March 1993, 51 at 52.

[212] Haanappel, *supra* note 178 at 8.

as politics and the economy, in the long run the competence for air transport will be transferred from Member States to the Community.

III-2 EXTERNAL EFFECTS OF EXISTING COMMUNITY LEGISLATION

III-2-1 COUNCIL DECISION 69/94[213]

This Decision emphasizes the authorization and consultation procedure at a Community level and provides for Community negotiations. Negotiations relate to the commercial policy of the Community and shall be conducted by the Commission in consultation with the special committee appointed by the Council under Article 113 of the EEC Treaty[214] except in cases where Community negotiations under Article 113 prove to be impossible.[215] The Decision is not directly related to the air transport field. However, the Commission regards it as one of the important legal bases for its external competence.[216] Nevertheless, the procedure outlined in this decision had not been respected by Member States.[217]

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[213] EC, *Council Decision* 69/494 on the progressive standardisation of agreements concerning commercial relations between Member States and third countries and on the negotiation of Community agreements, O.J. Legislation (1969) No. L326/39 at 303.

[214] *Ibid.*, Art. 8.

[215] *Ibid.*, Art. 9.

[216] The Communication, *supra* note 162, paras. 51-52.

[217] Wassenbergh, *supra* note 203 at 47.

III-2-2 COUNCIL DECISION 80/50[218]

In 1979 the EC Council adopted the Decision which obliges Member States and the Commission to consult each other, at either's request, on air transport questions dealt with in international organizations and on aspects of air transport relationships between Member States and non-Member States. It is one of the earliest and least known actions of the Council related to air transport concerned precisely with the external aviation relations of the EEC.[219] However, because of its very general terms, it is of little practical importance.[220]

III-2-3 COMMUNICATION ON COMMUNITY RELATIONS WITH THIRD COUNTRIES IN AVIATION MATTERS[221]

In this communication the Commission states that the creation of the internal market has as a legal consequence for the outside world that the Community should be

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[218] EC, *Council Decision* 80/50 on setting up a consultation procedure on relations between Member States and third countries in the field of air transport and on action relating to such matters within international organizations, O.J. Legislation (1980) No. L.48 at 24.

[219] Haanappel, *supra* note 21 at 83.

[220] Cholmeley, *supra* note 33 at 13.

[221] Commission Communication, *supra* note 123.

considered as one entity and therefore as a cabotage area.[222] In order to reinforce the Community negotiating position vis-a-vis third countries and to avoid a situation in which third countries exploit the lack of Community unity, Community competence must be exercised without delay in such instances under Community procedures according to Article 113 of the EEC Treaty. Also, Member States are no longer competent to grant new fifth freedom rights to third countries. They will have to refer requests for such fifth freedom rights to the Commission for consideration.[223] Until now, this proposal has not been discussed by the Council.

III-2-4 COUNCIL REGULATION 2409/92 ON FARES AND RATES FOR AIR SERVICES[224]

Although this regulation does not generally apply to non-EC carriers, Article 3(3) prescribes that "only Community air carriers shall be entitled to introduce new products or lower fares than the ones existing for identical products". This obviously has implications for fifth freedom operations within the EC by non-EC carriers.

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[222] *Ibid.* paras. 37-42.

[223] *Ibid.*

[224] *Supra* note 100.

III-2-5 COMMUNICATION FROM THE COMMISSION TO THE COUNCIL[225]

In this communication, the Commission states that the establishment of the single market is likely to improve the competitive position of Community air carriers in relation to some of the very efficient carriers of third countries. However, it will be necessary to complement the internal market with a Community policy for the relations with third countries to allow them to make full use of the commercial opportunities.

The proposal for a Council Decision in this Communication replaces Council Decision 69/494 and amends the 1990 proposal for a Council Decision. It forces the creation of a regulatory framework for negotiations with third countries and provides for a transition period of six years (until 31 December 1998).

The Commission proposed that, as of 1993, the Community assume responsibility for all negotiations with third countries.[226] Several negotiations would take place at Community level,[227] whilst others would continue to be held at the level of individual

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[225] *Supra* note 162.

[226] *Ibid.* para. 54.

[227] *Ibid.*, para. 57. The Commission suggested several areas where the Community should assume its responsibilities without delay. Such areas are as follows: (a) negotiations on the Community level would give better economic results than negotiations at the Member State level; (b) the insistence on acceptance of Community principles such as non-discrimination on the grounds of nationality would place an individual Member State in an unacceptable situation; (c) relations with Eastern Europe and the successor states of the Soviet Union and Slovenia, Croatia and Bosnia - Herzegorvinia would be facilitated; (d) developments towards liberal multilateral agreements, possibility between groupings of countries could be accelerated; (e) common positions are expressed and Community interests are defended as a whole in international organizations such as ICAO

Member States but under Community supervision.[228] Community coordination would take place in order to safeguard the process as a whole and to assist the Commission and the Council. The Council should also establish an ad-hoc Aviation Committee.[229]

The Commission also proposed the establishment of a "Management Committee for Air Transport" for the implementation of the results of Community negotiations.[230] This Committee may handle, *inter alia*, the selection of Community air carriers to exercise the rights obtained in Community negotiations, i.e. the allocation of the routes and rights obtained by the Community from third States to Community air carriers:[231] The allocation of the rights obtained by the Community must be non-discriminatory and, according to the Commission, could be done by selling the rights to the highest bidder, or by a quota system based on actual performance (present market shares) or by a qualitative selection procedure which should normally be applied only to the allocation and of additional rights while taking into account the existing situation. The Commission favours the qualitative selection procedure.

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[228] *Ibid.*, paras. 58-59.

[229] *Ibid.*, paras. 60-64.

[230] *Ibid.*, para. 70.

[231] *Ibid.*, paras. 65-71.

On 7 December 1992, the Council held a preliminary exchange of views on this Communication, and instructed the Permanant Representatives Committee[232] to examine it with a view to preparing the Council's discussion at a forthcoming meeting.[233]

III-3 JURISPRUDENCE OF THE EUROPEAN COURT OF JUSTICE

A number of decisions of the European Court of Justice, especially in the field of competition law have functioned and continued to function as an impetus towards the adoption of a common air transport policy through legislative measures of the Council of the European Communities.

Of seven cases, which have significantly influenced the liberalization of air transport,[234] two are directly applicable to the relations with non-EC countries.

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[232] Each Member State has in Brussels, a Permanent Representative to the European Community with a staff of diplomats and official from the national civil services to assist them. This Committee consists of these representatives. For detail about the Committee, see Tretheway, *supra* note 28 at 17.

[233] Haanappel, *supra* note 183 at 8.

[234] Haanappel, *supra* note 21 at 71-79.

III-3-1 WOOD PULP CASE[235]

In this case two associations of wood pulp producers with registered offices outside the Community brought an action, under Article 177[236] of the EEC Treaty, for the annulment of a Commission decision which fined them for violating Article 85 of the EEC Treaty. The main significance of this case lies in the extraterritorial applicability of competition rules.[237] The implication of this rule for aviation is that "inter-airline agreements, particularly tariff agreements, covering prices and other conditions offered in the common market to air transport users for transport between Community and third countries" will fall under the Community common rules.[238]

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[235] Jointed cases 89,104,114,116,117,125-129/85: Ahlstrom Osakeyhtio and Others v. Commission, (1988) 4 CMLR 901.

[236] Article 177 of the EEC Treaty states: "The Court of Justice shall have jurisdiction to give preliminary rulings concerning: (a) the interpretation of this Treaty; (b) the valdity and interpretation of acts of the institutions of the Community; (c) the interpretation of the statutes...".

[237] S.A. Williams, "Internal Market and Common Market - the Single European Act v. the Treaty of Rome" at 12, in P.P.C. Haanappel, et al., *EEC Air Transport Policy and Regulation and their Implications for North America: proceedings of a Conference held at McGill University*, Montreal, Canada, September 1989, (Denventer: Kluwer, 1990).

[238] Haanappel, *supra* note 4 at 79.

III-3-2 AHMED SAEED CASE[239]

This case came before the Court by way of a referral by the German Federal Court of Justice, for a preliminary ruling under Article 177 of the EEC Treaty. The Court was asked three questions concerning certain practices connected with the fixing of tariffs applicable to scheduled passenger flights and their compatibility with the second paragraph of Article 5 and Articles 85, 86, 88, 89 and 90 of the Treaty:

(i) Were the agreements on the tariffs automatically void (Article 85(2)), even if the competition authorities had not acted under Article 88 or 89?

(ii) Does the exclusive application of such tariffs involve the abuse of a dominant position (Article 86)?

(iii) Would the approval of such tariffs by a Member State be incompatible with Community law (Articles 5(2) and 90) and thus be automatically void, even when the Community had not objected to such approval?

Although the actual situation presented by the *Saeed* case deals with airline tariffs, its implications go well beyond this. It can be argued that its reasoning applies equally to capacity and revenue sharing agreements.[240] The court noted, in ground 29 of the

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[239] Case 66/86, Ahmed Saeed Flugreisen et al. *v* Zentrale zur Bekapfung unlauteren Wett bewerbs e.v. (1990), 4 CMLR 102.

[240] Williams, *supra* note 238 at 13: For the detailed reasoning of the Court of this case, see G.L. Close, "Case 66/86 - Ahmed Saeed" in *European Air Law Association Conference Papers 1* edited by P.D. Dagtoglou (Athens: Ant. N. Sakkoulas Publishers, 1989) at 38-45.

judgement, that bilateral and multilateral agreements regarding tariffs applicable to flights between a Member State and a third country were automatically void under Article 85(2), but only if either national authorities - or the Commission acting under Article 88 or 89 - had ruled or recorded that the agreement is incompatible with Article 85. Furthermore, the court confirmed that since no exemption from Article 86 was available, the prohibition was fully applicable to all international air travel, whether confined to the EC or international in character.[241]

III-4 EC AIR TRANSPORT RELATIONS WITH NON-EC COUNTRIES

III-4-1 RELATIONS BETWEEN THE EC AND NON-EC COUNTRIES IN EUROPE

The community, through the Commission, using as a basis the negotiating directive issued by the Council, has concluded an air transport agreement with Norway and Sweden, which is in force.[242] This agreement permits the creation, in the area covered by the EC, Norway and Sweden, of a uniform system of rules concerning market access, airline capacity as well as price setting in the field of civil aviation. Due to the fact that SAS is jointly owned by Norway, Sweden and Denmark, while only

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[241] D.F. Hall, "Ahmed Saeed and the legal situation now", *ibid.* at 51.

[242] EC, *Council Decision* 92/384 concerning the conclusion of an agreement between the European Economic Community, the Kingdom of Norway and the Kingdom of Sweden on Civil Aviation, O.J. Legislation (1992) No. L.200 at 20.

Denmark is a Member State of the EC, negotiations were requested by Sweden and Norway in order to clarify the relationship of this carrier with the EC.

In April 1992, the important European Economic Area (EEA) agreement was formally signed.[243] It is a general economic association agreement between the twelve European Community States and the seven EFTA States. The EEA agreement envisages the creation of a trade area for the free flow of capital, goods, persons, and services, including air transport services. It would, amongst other things, extend the EC internal air transport market to the Member States of the EFTA. This would mean that the seven EFTA States associate themselves with, and voluntarily take over, most of the Community's liberalization, harmonization, and competition measures, so as to create one liberalized air transport zone composed of 19 European Countries.[244] Whereas the EC is among other things a customs union, the EEA will merely be a Free Trade Area. This has some practical consequences, amongst which are the following:[245] (a) EFTA countries might have their own individual external air transport policies, whereas EC countries will eventually have a common external air transport policy; and (b) although formalities might be reduced, border controls between the EC and EFTA countries will be maintained, whereas they are intended to be abolished between EC countries (first for customs, then for immigration).

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[243] Memorandum of IATA, *supra* note 181, paras. 1-1 and 1-2.

[244] Haanappel, *supra* note 7 at 218.

[245] P.P.C. Haanappel, "Europe 1992 and Airline (De)regulation" (1992) 17:1 Ann. Air & Sp. L. 271 at 279.

In a referendum held in December 1992, voters in Switzerland rejected that country's adoption of the multilateral EEA agreement. The Swiss vote has delayed the coming into force of the EEA, probably until the beginning of 1994.[246] Currently six EFTA countries are virtually certain to join the EEA: Austria, Finland, Iceland, Liechtenstein, Norway and Sweden. Switzerland is expected to negotiate a separate bilateral air transport agreement with the Community which would find its legal basis in the existing Alpine Transit Agreement between the EC and Switzerland.[247]

The Community signed three general association agreements, namely with former Czechoslovakia, Hungary, and Poland. These agreements provided that the conditions of mutual market access in air transport shall be dealt with by special transport agreements to be negotiated after the entry into force of the general association agreements.[248]

As mentioned above, air transport integration in "Great Europe", under the Community competence, has been smooth and steady. This means that the area, covered by the EC and the other European countries concluding aviation agreements with the EC countries, eventually will be ruled by a uniform aviation policy.

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[246] Haanappel, *supra* note 183 at 7.

[247] *Ibid.*

[248] Haanappel, *supra* note 7 at 220. Relating to the Eastern European Countries, Air transport to, from and over the Former Soviet Union is becoming increasingly important, both locally and for foreign air carriers, see Haanappel, *supra* note 183 at 9-15.

III-4-2 RELATIONS BETWEEN THE EC AND NON-EC COUNTRIES OUTSIDE EUROPE

The EC's external policy toward non-EC Countries outside Europe was not clear until recently. However, negotiation with the United States might be a high priority not only because the United States is a large market for the EC air carriers[249] but also because there is an imbalance of traffic rights between the EC and the United States. This imbalance can be illustrated as follows:[250]

EC/U.S. Market Comparison - August 1991

	EC carriers	U.S. carriers
- American gateways (in total 55)	22	54
- EC gateways (in total 28)	27	22
- Cabotage rights in the U.S. U.S. fifth freedom traffic rights within the EC	--	20
- Fifth freedom rights	10	33

[249] According to passenger revenue miles, the biggest air transport market is the U.S. domestic market; the second biggest, at around one third of the U.S. domestic market is the international trans-Atlantic market and then, close behind, comes the international North America-Asia/Pacific market. See, H.A. Wassenbergh, "The Globalization of International Air Transport" (1993) in material for the Guest Lectures of Prof. H.A. Wassenbergh at McGill University, IASL, March 1993 at 2.

[250] Commission Communication, *supra* note 162 at 11.

(intra-EC operation)		
- Number of routes operated between the U.S. and the EC	97	139*

* 276 advertised operations with 122 city pairs served under one flight number but with an aircraft charge

As the internal market is completed, it will be considered a cabotage area and fifth freedom rights within the Community will be considered a "Community asset". However, while the United States carriers enjoy fifth freedom rights within the Community, EC carriers do not have any similar rights within the United States. Therefore, the Community as a whole is likely to feel the necessity of amending its bilateral air transport agreements with the United States and then during the negotiations, the Community will have the competence, in close consultation with Member States, to conclude agreements; its bargaining power will be greater than the individual twelve negotiators. However, before showing up at the bargaining table, the Community must seek to solve a basic problem: the distribution of benefits among Member States, including acquired traffic rights of individual Member States in the United States.

One observer has suggested that it is more likely that the EC will conclude an agreement with Japan than with the United States. The reason given for this is that every EC member nation and carrier is constrained by current bilaterals with Japan in terms of both access to Japanese markets and the amount of capacity which can be offered.

Since everyone is more or less equally constrained, a new EC agreement would likely be of benefit to all.[251]

In the case of other countries, except the United States and Japan, their priorities will be decided on a case by case basis according to a basic criterion: How important and urgent is it to the interests of the Community?

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[251] Tretheway, *supra* note 28 at 56.

CHAPTER IV

IMPACT OF EC LIBERALIZATION ON AIR TRANSPORT IN KOREA

IV-1 BRIEF HISTORY OF AIR TRANSPORT IN KOREA

From 1948 to the year 1969, the Korean civil aviation industry was insignificant due to the Korean War, political turmoil and poor economic growth. During these years international air transport to and from Korea was serviced mainly by foreign carriers: Northwest Air, Japan Air and Cathay Pacific Air. However, since 1969 when Korean Air Lines (hereinafter KAL) was fully privatized, the Korean civil aviation industry has developed very rapidly thanks to the successful growth of the Korean economy and the active business of KAL.

During the twenty-year period between 1970 and 1990, the air transport market in Korea considerably expanded at an annual growth rate of 14.6% on domestic routes and 24.4% on international routes,[252] while the annual economic growth rate of Korea was only 8.7%. In the second half of 1980's, owing to the Seoul Olympic Games, the liberalization of overseas travel by the government, and the unprecedented economic

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[252] "Statistical Yearbook of Transportation" (Seoul: Ministry of Transportation of Korea, 1991) during the same period the operating revenue of KAL was increasing every year: 1.411 (1985), 1.643 (1986: 16.4%), 1.778 (1987: 8.2%), 1.927 (1988: 8.4%), 1.947 (1989: 1.0%), 2.098 (1990: 7.8%). Source: KAL; Unit: million U.S. dollar (1 US $ = 800 Korean won); % = annual growth rate.

boom, the air transport market grew at an annual rate of 34.1% domestically and 18.7% internationally.

The market share of Korean carriers on international routes was over 60% in the late 1980s, but it decreased to 52.8% in 1992 due to the increased frequencies offered by foreign carriers.[253]

Today, Korea ranks 11th in the world in overall ton-kilometer carriage including passengers, freight and mail, logging 4,540 million ton-kilometers carried on scheduled service. Also, according to ICAO Statistics for 1991,[254] Korea ranked 6th in freight carriage, logging 2,580 million freight ton-kilometers carried on scheduled service.

KAL also ranks as one of the fifteen biggest airlines in the world, with 27 jumbo jets, 14,000 employees, and 2.6 billion US dollars of operating revenue. This successful growth of KAL seems to have been based upon the government policy of privatization in the early stages, competition with foreign carriers on international routes, and the close-to-natural monopoly position it enjoyed in the Korean travel market.

As the demand for air transport increased 55 fold over the past twenty years, the civil aviation industry of Korea reached a major turning point in the late 1980's. In 1988

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[253] Against the background of increasing demand for air transport in Korea - Olympic games, economic booms, etc. - the number of foreign carriers to fly to Korea has been increasing every year; United Airlines, Swissair (1986); Delta Airlines (1987); All Nippon Airways, Japan Air System, British Airways (1988); Aeroflot, Continental Airways (1990); Phillippine Airlines, Evergreen Airways of Taiwan, Lauda Airline (1991); Vaspi Airways, Alitalia (1992). At the end of 1992, the number of foreign carriers to fly to Korea was twenty-five: Ministry of Transportation of Korea.

[254] ICAO, *Civil Aviation Statistics of the World* (1991) ICAO Doc. 9180.

the Korean government started to deregulate the air transport industry, and licensed the second carrier Asiana Air Lines (hereinafter AAR) to operate on domestic routes, the Korea-Japan route, and the Korea-U.S. transpacific route.

Since that time the aviation industry has been maintained as a two-airline system with one major carrier and the other relatively smaller one. The background[255] to this deregulation was, firstly, that the air transport market had become too big for a single airline to operate monopolistically. Secondly, the government had started to deregulate and liberalize all the sectors of the economy to promote efficiency. Thirdly, the government was influenced by the international trend toward airline deregulation, particularly in the United States. While there are nine other non-scheduled air service companies in Korea, their business has been negligible so far.[256]

The Korean domestic market is not profitable at all, because the air fares are strictly regulated by the government while the operating costs are very high due to the absence of enough mileage to operate and the consequent difficulty of aircraft utilization. Indeed, increased operation in the domestic market resulted in the accumulation of operating losses. Thus, the AAR sought to expend its network to the profitable Southeast Asian market and in October 1990 the Korean Ministry of Transport announced "The Guidance Rule for National Airlines' International Operation".

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[255] Yeong-Heok, Lee, "The Two Airline Policy In Korea: The Early Experience" (1992), Korea Maritime Institute [unpublished] at 2.

[256] Now, only one of the nine non-scheduled air service companies in Korea is conducting a point to point operation, "A Report for Aviation policy" (1992), Civil Aviation Bureau, Ministry of Transportation of Korea, at 24.

The rule permitted KAL to maintain its monopoly position on the long-haul international routes while giving priority to AAR on short-haul international routes, and allowed "a second designation"[257] on the densely travelled routes. Following this rule, AAR now conducts its international operations on 17 routes to Japan, Singapore, Taiwan, Hongkong, Bangkok as well as transpacific routes to the United States. KAL conducts its international operation on 56 routes throughout the world except Africa. AAR has a 35% domestic market share and its market share on international routes is 15% of KAL's.

IV-2 IMPACT OF THE EC LIBERALIZATION ON THE RELATIONSHIP BETWEEN THE EC AND KOREA

By adopting a common policy for air transport through liberalization measures the EC, as far as air transport is concerned, broke down the internal barriers between Member States and achieved a huge single market for 320 million inhabitants. While increased economic efficiencies brought about by market integration in general, and aviation liberalization in particular, will result in growth in air services to, from, and

[257] There are two criteria for double tracking on international routes: one is more than 150,000 passengers per year, the other is more than seven return flights per week and a load factor on those routes of more than 70%: Article 5 of the Guidance Rule for National Airlines' International operation.

within the EC, there are also a number of issues on the horizon which could impede progress.[258]

The first is constrained air traffic control facilities. Obviously, the air traffic system as organized at present is hopelessly inadequate.[259] There is no supranational European Civil aviation office, equivalent to the United States Federal Aviation Administration (FAA), to deal with Europe's critical air traffic congestion problems. All told, there are 42 air traffic control centres, more than twice the number in the continental United States which covers an area double the size of Europe. Those centres operating as individual units will need to be integrated as part of a central authority similar to the FAA. For instance, under the present procedures, a flight from Frankfurt to Madrid must be directed through eleven different air traffic control zones.[260]

During the 1988 summer season, air traffic delays throughout Europe reached epidemic proportions, resulting in lengthy delays for millions of travellers, and massive costs for the affected carriers. Many more measures to counteract this problem will be needed if current expectations materialize regarding the demand for air travel in the wake of "Euro-Deregulation".[261] If it were possible to free a greater portion of airspace

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[258] Joanne W. Young, "What will be the effects of EC market unification on intercontinental air services after 1992?" ICAO J. January 1992 at 27-28.

[259] Eugene Sochor, *The Politics of International Aviation* (London: MacMillan, 1991) at 197.

[260] *Ibid.*

[261] Young, *supra* note 258: To solve this problem, in April 1990, the ECAC (European Civil Aviation Conference) adopted a programme of ATC (Air Traffic Control) integration and harmonization. The ECAC's strategy includes two phases: (i)

dedicated to military operations for air carrier use, a significant contribution could be made to accommodating the infrastructure requirements of the growing demand for air travel.[262]

The second constraint is the limited ability of carriers to obtain additional access to the major airports of Europe in terms of landing slots, gates and terminal space. Some countries may be tempted to use congestion at certain airports as an excuse to keep foreign airlines out of the market[263] and to impede the creation of new entrant carriers. Indeed, the airport capacity shortage may prove to be devastating, preventing new entrants and competitors from ever developing frequencies and route networks. Incumbents may reap the benefits of protection from new competition at their existing hubs, where they already control sizeable blocks of slots, gates and terminal space.

In order to facilitate competition and to encourage entry into the market, the Council adopted Regulation No. 95/93 on common rules for the allocation of slots at Community airports.[264] It shall apply to the allocation of slots at Community airports

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the first extends until 1995 and is aimed at increasing the efficiency of the existing ATC systems. (ii) From 1995, the new ATC systems, which are more advanced and operate with greater harmony, will be introduced. Also, Eurocontrol is preparing to set up a Central Air Traffic Flow Management Unit (CFMU) to help reduce congestion to manageable levels. It will become fully operational by 1994, see Avianews International, February 1991 at 46.

[262] *Ibid.*

[263] Sochor, *supra* note 259.

[264] O.J. Legislation (1993) No. L.14 at 1-11.

except the airport of Gibralter.[265] A Member State may provide for any airport to be designated as a coordinated airport provided that certain principles of transparency, neutrality and non-discrimination are met:[266] (a) when air carriers representing more than half of the operations at an airport and/or the airport authority considers that capacity is insufficient for actual or planned operations at certain periods; or (b) when new entrants encounter serious problems in securing slots; or (c) when a Member State considers it necessary. The Member State responsible for the coordinated airport should ensure the appointment of a coordinator responsible for the allocation of slots[267] assisted by a coordination committee.[268] At an airport where slot allocation takes place, a slot pool, including newly created slots, unused slots and slots which have been given up by a carrier, shall be set up for each coordinated period.[269] Slots which are allocated to an air carrier for the operation of a scheduled service or a programmed non-scheduled service shall not entitle that air carrier to the same series of slots in the next equivalent period unless the air carrier can demonstrate to the satisfaction of the coordinator that they have been operated by that air carrier for at least 80% of the time

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[265] *Ibid.*, Art. 1.

[266] *Ibid.* Art. 3(2) and 3(3). For definitions of terms such as coordinated airports, transparency, neutrality, etc. see *ibid.*, at Art. 2 and introductory remarks.

[267] *Ibid.*, Art. 4.

[268] *Ibid.*, Art. 5.

[269] *Ibid.*, Art. 10(1).

during the period for which they have been allocated.[270] If the 80% usage of the series of slots cannot be demonstrated, all the slots constituting that series shall be placed in the slot pool unless the non-utilization can be justified[271] and then slots in the pools shall be distributed among applicant carriers. 50% of these slots shall be allocated to new entrants unless demand by new entrants constitutes less than 50%.[272]

Thirdly, once Europe's internal frontiers are dismantled it appears that duty-free shopping may no longer be offered to intra-Community air travellers, eliminating an important existing source of funding for airport operation and development. This phenomenon may result in the imposition of higher landing charges and ancillary airport user fees on air carriers, which in turn will put upward pressure on fares, thereby counteracting the other forces at work to promote greater demand for air travel.[273] In addition, the evaporation of this established source of airport funding will make it all the more difficult for airport infrastructure expansion plans to be successfully launched.

A final constraint is less flexibility in labor costs. In the United States deregulation prompted major cost-cutting measures among incumbents forced to match the low-fare-initiatives of non-unionized new entrants, including lower wage rates for newly-hired workers, pay freezes, give-backs for existing employees, and work rule

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[270] *Ibid.*, Art. 10(3).

[271] *Ibid.*, Art. 10(5).

[272] *Ibid.*, Art. 10(7).

[273] Young, *supra* note 258.

changes.[274] However, due to the existence of protective legislation and sharply different attitudes to labour relations, it will not be so easy to implement such savings among the European incumbent carriers.

The only possibility for a European incumbent is the formation of separate smaller airline companies, related to the parent company.[275] Companies such as Euro-Berlin, Lufthansa Berlin etc. have been established by Lufthansa because they are believed to enable higher productivity at lower cost.[276] However, the personnel cost issue will give new entrants and foreign carriers a meaningful advantage in their effort to compete against incumbents in the EC.

As mentioned above, the EC has its own problems in achieving an efficient internal market for air transport. However, from the non-EC carriers's perspective, the existence of a fortress block threatens them. In particular, many non-EC countries are concerned that the creation of an internal market may affect their traffic rights to, from and within the Community.[277] Even though their acquired rights are protected under Article 234 of the EEC Treaty,[278] non-EC countries which have agreements with

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[274] *Ibid.*

[275] European Air Law, *supra* note 47 at 57-58.

[276] *Ibid.*

[277] The Communication's Communication, *supra* note 162 at 22.

[278] Art. 234 of the EEC Treaty states: "The rights and obligations arising from agreements concluded before the entry into force of this Treaty between one or more Member States on the one hand, and one or more third countries on the other shall not affected by the provision of this Treaty."

individual Member States are understandably apprehensive about future negotiations with the Community on such sensitive issues as the designation of airlines to fly certain routes, the use of airports and fifth freedom routes in the EC. Korea is no exception.

From a practical standpoint, the unified Community makes it more difficult for non-EC countries to gain access to the European market because the air traffic rights within the Community are "Community assets". Therefore any negotiation on traffic rights for non-EC countries within the Community will be subject to a coordination of negotiating positions of the several Member States.

We will now turn to an analysis of the impact of EC liberalization on Korea as regards three subjects: bilateral agreements, extraterritorial application of EC competition law and fifth freedom rights, all of which are likely to influence directly the operation of Korea's air carriers in the EC.

IV-2-1 BILATERAL AGREEMENTS

Korea has seven bilateral agreements with EC Member States excluding Denmark, Greece, Ireland, Luxembourg and Portugal.[279] Regarding bilateral agreements between the EC and Korea, two issues will arise in the negotiation process: the "negotiating partner" issue and the "Community clause" issue.

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[279] Material concerning the present situation of Korea's Bilateral Air Transport Agreement with other countries, Ministry of Transport of Korea, 1992.

Even though Member States are not willing to allow their negotiation rights with non-EC countries to be transferred to the Community until the internal market has been completed and a common policy on non-EC countries has been determined, they will consider the interests of other Member States and will want to make full use of their enhanced bargaining position in the process of negotiating bilateral agreements. Therefore, negotiations with the Community are expected to involve the issues discussed before,[280] and the Community will probably act as a negotiation agent. Under public international law, non-EC countries cannot be legally required to recognize any transfer of tasks and powers to the Community as a negotiating partner.[281] However, there is no real benefit for Korea in rejecting the Community as a partner.

Another issue is the Community clause. The EC may request that Korea accept the Community clause instead of the nationality clause in the process of negotiating bilateral agreements. Denmark requested that Korea insert the Community clause instead of the nationality clause in the process of bilateral negotiations held in Copenhagen in May 1992. At that time, the countries did not reach a final agreement because of differences in opinions. One problem was precisely the community clause. Korea was reluctant to accept that concept. However, the Community clause will be a useful bargaining chip for Korea.[282]

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[280] *Supra* note 206.

[281] Weber, *supra* note 194 at 251.

[282] *Infra*, ch. IV-3-1.

IV-2-2 EXTRATERRITORIAL APPLICATION OF COMPETITION LAW

The attitude of governments towards their airlines has changed in recent years. In the past, the commercial interests of many national airlines were given special status. Indeed, most governments look on air transport as being distinct from other commercial undertakings. Although the reasons for this vary from one country to another, they can be summarized as follows:[283] air transport is a public service, promotes of foreign trade, is a source of income and foreign exchange, provides jobs and training for nationals, and adds to national prestige. Thus, in those States with well-defined competition laws, aviation law often supplanted the general competition law regime that applied to companies operating in other industries.[284] In the United States, airlines were until recently exempted from U.S. antitrust law for activities that might otherwise be unlawful, to the extent authorized by the Department of Transportation (and previously by the Civil Aeronautics Board). Similarly, in other countries where competition laws existed, these were not applied to air transport.

However, after the 1986 judgement of the ECJ in *Ministere Public* v. *Asjes* (commonly referred to as the "Nouvelles Frontières" case)[285] the air transport field of the EC was exposed to EC competition law. That judgement made clear that, despite the

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[283] G.K. Sletmo, "International Air Transport and National Interests" in Public International Law I edited by I.A. Vlasic for Lectures at McGill University, IASL, 1992 at 89-92.

[284] IATA White Paper, *supra* note 3 at 27.

[285] Case 209/84 3 CMLR (1986) at 173.

fact the Council had failed to adopt any implementing legislation applying the competition rules of the EEC Treaty to the air transport sector, it remained subject to the general rules of the EEC Treaty, including the competition rules.[286] The application of EC competition law to the air transport sector is highly complex and rapidly changing. No airline or company involved in aviation can afford to ignore recent developments because:[287]

- anti-competitive agreements or concerted practices which appreciably affect trade between Member States are *prohibited and void* unless an exemption is granted by the European Commission (Article 85 of the EEC Treaty); and
- the abusive exploitation of a dominant position by one or more undertakings in the Common market which may affect trade between Member States is *prohibited* (Article 86 of the EEC Treaty).

Infringement of Articles 85 and 86 can result in:

(i) the imposition of fines by the European Commission of up to 10 per cent of the annual worldwide turnover of the undertaking(s) concerned;

(ii) third party claims for damages; and

(iii) Commission action specifying remedial measures.

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[286] Trevor Soames, "Joint Ventures and Cooperation Agreements in the Air Transport Sector" in *European Air Law Association Conference Papers* 2 edited by P.D. Dagtoglou and T. Soames (Athens: Ant. N. Sakkoulas Publishers; 1990) at 73.

[287] *Ibid.* at 72.

According to the other cases of the ECJ,[288] Korea could also be affected, as any existing arrangements involving capacity, pooling or carrier fare setting could be disallowed by the EC competition law.

IV-2-3 FIFTH FREEDOM RIGHTS

The integration of the intra-Community air traffic market will affect the fifth freedom traffic rights between Member States and Korea. New intra-Community fifth freedom traffic rights for non-EC air carriers can no longer be freely negotiated as these rights are a "Community asset".[289] To provide a "balancing interest" in exchange of fifth freedom rights, a new guiding principle of negotiation is needed. Even though the acquired fifth freedom traffic rights will be respected by the Community, if Korea wants to get more fifth freedom rights within the EC, adequate reciprocity should be offered by Korea.

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[288] *Supra*, Wood Pulp case and Ahmed Saeed case in ch. II at 3-2.

[289] The Commission regards fifth freedom rights for non-EC countries in the EC as one of the important bargaining chips for the EC: Commission Communication, *supra* note 123, para. 41.

FIFTH FREEDOM RIGHTS FOR KOREA IN THE EC[290]

Pursuant to concluding a bilateral agreement with Korea	Rights granted
U.K. (London)	1 unspecified point in the EC or other continent
France (Paris)	1 unspecified point
Germany (Frankfurt) (Cologne)	3 unspecified points
Netherlands (Amsterdam)	1 unspecified point
Italy (Rome)	3 unspecified points
Spain (Madrid)	1 unspecified point

[290] Bilateral agreements between Member States of the EC and Korea (1992). Korea exerts only one fifth freedom right on the Amsterdam/Rome route once per week (December in 1992).

IV-3 STRATEGIES OF KOREA

From the Korean point of view, the unified external aviation policy of the EC may be unfavourable to Korea because the enhanced bargaining position of the EC as a block will place strong demands on Korea for a "balancing interest". Already, Korea has experienced limited bargaining power against the United States. In the post-war period there were great disparities in economic and political power which favored the United States in its relations with other countries. In addition, there was the special situation of the Korean War (1950-1953) in Korea. Under such circumstances, it was inevitable that air transport agreements between Korea and the United States would be concluded in such a way as to permit the United States almost free access, in terms of carriers, frequency and capacity, to the markets between the United States and Korea and beyond. The legacy of this period remains. Therefore, in order to gain more access to the United States, Korea has to offer a "balancing interest" to the United States.[291]

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[291] Whenever the bilateral agreement has been amended, the United States has requested from Korea a balancing interest for additional access for Korea to the United States. For example, in amending an agreement of 1991, Korea acquired 9 points in the United States and 3 beyond points. In return Korea permitted the U.S. to operate a CRS system in Korea, constructed an air cargo building for exclusive use by U.S. carriers and improved the customs procedure for air cargo for U.S. carriers.

PRESENT SITUATION BETWEEN KOREA AND THE U.S. - 1992

* Route Structure

  - Korea: points in Korea / intermediate points / 12 points in U.S. / 3 beyond points

  - U.S.: points in U.S. / intermediate points / unlimited points in Korea / unlimited beyond points

* Frequency and Kinds of Flight: unlimited

* Operation Situation

  - Korea: 2 air carriers, 10 routes, 69 flights per week

  - U.S.: 6 air carriers, 21 routes, 89 flights per week

However, Korea, which has a relatively small domestic market, has fewer bargaining tools to attract the EC carriers. Also, from the EC point of view, Korea is not an attractive aviation market at all because it has a relatively small population (about 45 million in South Korea) and only two international airports (Seoul and Busan). In addition, there are more attractive and lucrative aviation markets, Japan and China, on either side of Korea: Japan has a population of over 100 million and 15 international

airports;[292] China with a population of over 1 billion has a potentially enormous domestic market.[293]

Even though the Commission forecast that the Far East/Pacific market for EC carriers would increase 7.2% annually in 1989-2000,[294] it seems that its forecast focuses mainly on Japan and China. Therefore, the strategies of Korea towards the EC must start by recognizing these preconditions.

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[292] Regarding the International routes of Japan, five Japanese air carriers fly to 53 cities of 26 different foreign countries from twelve cities in Japan. Two Japanese airlines (Japan Air Lines and All Nippon Airline) were allowed double tracking on the three densely travelled three routes between Japan and Europe: London, Paris, Berlin (1991) and the domestic market of Japan was approximately 65 million in 1990. It is the third biggest market in the world behind the United States, and the CIS (Commonwealth of Independent States): Material for aviation policy (1992), Ministry of Transportation of Korea. According to IATA forecasting the international air transport market of Japan will be increasing 8.4% every year and in 2010 it will be 150 million (30 million in 1990) and especially European routes will be increasing 7.8% every year and be over 12 million in 2010 (2.6 million in 1990), Asia-Pacific Passenger Traffic Forecast-Travel Demand 1985-2010 (1991) IATA.

[293] In 1991 China had fifteen airlines and 452 routes (Domestic: 395, International: 49, Hongkong: 8). According to IATA forecasting, the international transport market of China will be increasing 11.0% every year and it will be 33 million in 2010 (4 million in 1990) and on European routes it will increase by 9.4%. The total number of passengers will be 1.4 million in 2010 (0.2 million in 1990), IATA. *Ibid.* Additionally, the growth rate of the economy (annually more than 10%) and a huge population makes it very difficult to predict the real air transport market of China.

[294] Commission's Communication, *supra* note 162 at 54.

IV-3-1 POSSIBLE BARGAINING TOOLS FOR KOREA

A. Acceptance of Community Ownership Requirement

Almost all bilateral agreements recognize the right to refuse its operating permission to a foreign designated airline that is not substantially owned and controlled by the designating State or its nationals. This is not compatible with the principle of non-discrimination on grounds of nationality within the Community and national ownership and control criteria for airlines are already replaced by Community criteria in order to make it possible for citizens of Community countries to establish airlines in other Community countries. Thus, the EC may request non-EC countries to replace the national ownership clause with the Community ownership clause in bilateral air transport agreements. However, a Community ownership requirement could have some peculiar consequences.[295] If Alitalia were not operating an authorized route from Italy to a point in Korea, another Community carrier, for example Lufthansa, could be allowed to operate the route. Thus, Korean carriers would be facing competition from Lufthansa not just on routes to Germany, but also on Italian and potentially other routes. Where Korean bilaterals have multiple designation provisions for the Community countries, there could be a significant increase in opportunities for the Community carriers to fly into Korea.

Nevertheless, if the EC were to request this change, Korea has no reason to reject it, not because the Community clause might be regarded as an irreversible trend but

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[295] Tretheway, *supra* note 28 at 76.

because Korea may be able to obtain concessions from the EC such as additional traffic rights, removal of frequency restrictions, additional fifth freedom rights and frequencies, etc. Furthermore, it may be possible for Korea to insist on a limited number of designated European carriers in exchange for acceptance of the community clause. Currently, five European carriers fly to Seoul. Given that European carriers will now be able to operate from any point in Europe, Korea might well insist on restricting the total number of designated European carriers, for example to four. On the other hand, if Japan follows the strategy, it might in fact be in Korea's interest to allow maximum designation of European carriers so as to favour the development of a hub airport in Korea. Korea might be better off to deal with the EC sooner rather than later: the EC is more likely to make generous concessions in its first few such negotiations rather than in its later negotiations.

B. A New Airport as a Hub for the Northeast Asia Region

If it were possible to operate economically with single seat aircraft, then all passengers could be served directly between their points of origin and destination, and at the desired time. There would be no need for passengers to transfer, and the phenomenon of hubbing would not arise.[296] As soon as aircraft size begins to offer economies of scale and to dictate a schedule, the situation changes fundamentally.[297]

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[296] A. Kanafani and A.A. Ghabrial, "Airline Hubbing - Some Implications for Airport Economics" (1985) 19A Transportation Research 15 at 15-16.

[297] *Ibid.*

The large traffic volumes to and from the large cities in a region encourage the use of larger aircraft. However, in the interest of maintaining the level of service, an airline wants to keep some lower limit on schedule frequency. Thus, the need to "fill" aircraft that fly to these cities arises and causes the airline to hub by reducing the direct service between smaller cities and by offering connecting flights at the hub. Already the efficiency of the hub and spoke system has been proven through the period of deregulation in the United States.[298] Whether airports becomes an international hub is determined by several factors: geographical location; economic status of the country where the airport belongs; bilateral air service agreements according to which the airlines can exercise the route rights; the airport charges which directly influence the cost structure of the carriers; international aviation and airport related policies of each country in the region; airport capacity, etc.

Korea has constructed a new international airport, temporarily called New Seoul Metropolitan Airport (hereinafter NSMA), for the air transport demand of the 21st century. It is expected to be a hub airport in Northeast Asia. Japan and Hong Kong also have constructed new airports. These two airport are also expected to create a hub in Northeast Asia. However, compared to these two airports, NSMA has some better points regarding scale.[299] In particular, NSMA would be suitable for supersonic

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[298] For the impact of the hub and spoke system on airline concentration in the United States see M. Brenner, "Airline Deregulation - A Case Study in Public Policy Failure" (1986) 16 Transport L.J. 179 at 186-191.

[299] Appendix III. Comparison of New Airports in Northeast Asia Region.

so-called next generation aircraft. Thus NSMA is expected to be a major hub. Regarding this point, Japan has been extremely worried that its new Kansas airport would become no more than a regional international airport serving the feeder airport of NSMA.[300] From Korea's perspective, this new airport will be a hub for sixth freedom traffic[301] on routes between the EC and Japan on the one hand and between South East Asia and the United States on the other. It could be that from the EC's point of view, NSMA might serve as a fifth freedom traffic hub between the EC on the one hand and Japan/China on the other.

IV-3-2 STRATEGIES OF KOREA

A. Regional Cooperation

Regional groups of countries sometimes adopt common air transport regulations in order to meet broader objectives such as economic integration, to boost trade, support economic and social development, expand and improve air services within their combined

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[300] The Daily Korea Times, 23 September 1993 at 10.

[301] Sixth freedom is defined as the right to fly into the territory of the grantor State and there discharge, or take on, traffic ostensibly coming from, or destined for, the flag State of the carrier which the carrier has either brought to the flag State from a third State on a different service or is carrying from the flag-State to a third State on a different service. For Freedoms of the Air, see Bin Cheng, *supra* note 1 at 9-18; Airlines such as KLM and Singapore Airlines with small national populations have successfully provided good connections with quality service for sixth freedom travellers. Sixth freedom traffic is regarded as one of the effective strategies of carriers. See Phillip Shearman, *Air Transport: Strategic Issues in Planning and Development* (London: Pitman Publishing, 1992) at 119.

territory, promote or defend their interests when negotiating with another group.[302] Perhaps regional cooperation among Asian countries would be a balancing force against the increasing pressure from the EC. The Asia/Pacific Conference of the Director General of the Civil Aviation Bureau, sponsored by the Asia/Pacific Regional Office of ICAO, has been held annually since 1961. Its primary purpose is the exchange of aviation technology and of opinions about formulating cooperative plans between participants. But it is informal and has no power to make any decisions that may restrict the participants. Therefore, it is almost impossible to expect regional cooperation through this Conference to act as a balancing force against the EC.

The common interest of the various countries in the Asia/Pacific region is less apparent than in Europe or North America or Latin America or even between the Arab Countries, although intra-industry trade and investment clearly are on the increase.[303] On the contrary, the Asia/Pacific region, according to its geographical peculiarity, will be divided into several groups such as the Association of South East Asian Nations (ASEAN), South-West, Middle-East and Pacific because small sub-regions have common political, economical and historical interests. Among them, only the six member States of ASEAN (Brunei, Indonesia, Malaysia, the Philippines, Thailand and Singapore) endorsed a plan to establish a free trade area within fifteen years. The mechanism to negotiate as a block already exists but as the timeframe for trade liberalization suggests,

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[302] "The torturous path to plurilateralism", The Avmark Aviation Economist, May 1992 at 17.

[303] Wassenberg, *supra* note 249 at 12.

the group seems far too fragmented at present to be able to agree on a common aviation policy.[304]

Unfortunately the Far-East Asia Region, including Korea, China, Japan and Taipei, will not be forming a block against the EC because the two big countries, China and Japan, do not need to do so: these two countries, respectively, probably have enough balancing power against the EC. So it is unlikely that Korea would be able to make use of regional cooperation as a counter block against the EC.

B. Access to the EC's Air Transport Market

Generally speaking, for an air carrier offering long-haul international services, the EC is a very important market, not only for point-to-point journeys, but in the context of its total network. The proportion of the EC market to the total international market of Korea is steadily increasing every year: 4.0% (1984), 4.9% (1988), 6.1% (1990), 6.2% (1991). According to "the Guidance Rule for National Airlines" AAR has restricted access to the EC and is not now flying to Europe. KAL conducts its 12 international operations weekly on five routes to the EC. EC carriers (BA, AF, KLM, LH, ALI) fly to Seoul eleven times per week.

Regarding market access to the EC, it is possible for Korea to contemplate two alternatives. The first is, if possible, to increase the points in the EC before April 1997 when cabotage within the EC is expected to be eliminated between EC carriers. The

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[304] The Avmark Aviation Economist, *ibid.* at 18.

breakdown of the barrier of cabotage, even though the negotiation rights with third countries are not totally transferred to the Community, will result in strong competition between EC carriers. They will, therefore, request the Community to protect their internal market from foreign carriers. The advantage of increasing points is that acquired traffic rights for third countries will be respected by the Community because an attempt to eliminate acquired rights will certainly produce an undesirable block-forming climate and provoke international tensions.

The greatest weakness of this approach is that adequate reciprocity should be provided to the EC carriers by Korea in bilateral agreements but Korea has fewer tools for negotiation. So, if Korea tries this approach, it should provide other economic benefits, not directly related to the aviation sector, to the EC carriers.

The second possibility is to develop its own hub-and-spoke networks by using the acquired points,[305] instead of seeking an increased number of points within the EC. Increased numbers of points, if any, will be pursued from a hub-and-spoke point of view because increasing points within the EC requires adequate reciprocity from Korea as well as the resolution of conflicts of interest between Member States.

However, this approach also has many problems:

- Points that Korea has already acquired are not sufficient to set up hub-and-spoke networks.

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[305] The alliance between carriers on both sides will be discussed in detail in the next Chapter. The strategies of Korea are not separate in nature. Korea will use all of its possible strategies with its bargaining chips in the negotiation of bilateral agreements or cooperation between carriers.

- A hub-and-spoke system will be less efficient than expected if stop-over rights with change of gauge are not acquired at the same time.

- Which points will play the role of the hub ?

Because of airport congestion at the EC airports which Korea wants to use as hubs, such use may not be possible. As mentioned above, neither alternative is obvious. Therefore, Korea must decide in advance, before entering into bilateral agreements, which form of access to the EC will be best for the Korean civil aviation industry.

C. Airline Alliances

There has been much talk in recent years of airline alliances. Alliances range from loose commitments to pursue joint marketing activities to the exchange of equity. American mega-carriers, having built up their corporate muscle in the competitive deregulated environment in the domestic market,[306] are forcing their entry to world markets and are expanding their networks toward globalization by exploiting their almost free vested rights.[307] This expansion of United States mega-carriers is the basic background of today's competitive environment in the world airline industry, and the cause for the swing toward airline alliances across borders as counter measures.

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[306] For air transport industry concentration in the United States, see J. M. Bruneau, "Concentration within the U.S. Airline Industry: A "Natural Phenomenon" or An "Ordinary" Monopoly/Oligopoly Resulting from the Behaviour of Competitors" (1992) Ann. Air & Sp. L. at 123-146.

[307] Susumu Yamaji, "Airline Cooperation in the New Competitive Environment" (1992) presentation at the sixth IATA High-Level Aviation Symposium held in September, 1992 in Paris at 3

There are some obvious advantages but also disadvantages to airline alliances.[308]

Advantages:

- increases marketing strength including possible CRS benefits;
- may deter predator-minded competitors;
- increases network synergy, provided the two networks are complementary;
- may enable economies of scale to be realised through such things as bulk purchases or joint negotiation of insurance rates;
- may provide for joint operations using one of the partner's aircraft to achieve cost savings;
- may provide slot sharing opportunities at congested airports.

Disadvantages:

- the image of one of the partners may be damaged as customers perceive that the lower quality of the second carrier may prevail;
- agreement on integrating schedules or on marketing tactics or on standards of service to be provided may prove difficult and time-consuming;
- management styles and company "cultures" may be different producing many disputes requiring resolution by top management;
- sharing costs of a joint service can lead to many disputes and much time spent resolving them;

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[308] Phillip Shearman, *supra* note 301 at 119-120.

- many alliances do not turn out to be equally beneficial for both parties, leading to disenchantment;

- the strategies of one partner may need to be abandoned or changed to accomodate the new strategies;

- governments may suspect collusion to reduce competition and increase fares, leading to action to control the alliance agreement.

Competitive pressure on airlines is likely to increase as governments reduce support and remove regulatory protection. Under such competitive circumstances, airline alliances are likely to continue to be the means by which carriers gain new market advantages, protection against competitors and cost saving benefits.[309]

Airline alliances could be classified into three categories according to the degree of alliance.[310] The first is corporate merger whether by airlines in various countries are merged them into a single corporate entity. From an operational point of view,

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[309] Some authors have argued that through the airline alliance a global airline network, capable of providing service to most large and medium-sized cities around the world, would be inevitable. Thus, to survive this situation it is suggested that Airlines in the world have to participate in this trend. They have pointed out some factors to support their arguments: creation of Open Skies Continental Blocks, Limited Knowledge of the Market, Time and Financial Resources, limits on Take-over and Foreign Ownership, and Limitation of Bilateral Agreement, etc. See T.H. Oum, A.J. Taylor, & Anming Zhang, "Strategic Airline policy in the Globalizing Airline Networks" (1992), Working Paper no. 92-TRA-010, Faculty of Commerce, the University of British Columbia, Vancouver, Canada.

[310] Michael W. Tretheway and Tae H. Oum, *Airline Economics: Foundations for Strategy and Policy* (Vancouver: Center for Transportation Studies, 1992) at 107-112.

outright merger is the most desirable form of consolidation. It allows full advantage to be taken of fleet and crew utilization possibilities, amasses purchasing and borrowing power, allows the adoption of a single consumer identity, etc. However, it has many political obstacles; limitation of foreign ownership of national carriers, desire to keep "flag carriers" etc. Therefore, while global mergers may be attractive from the airline's point of view, it seems to be an idea whose time has not yet come. The second is simple alliance. It involves marketing agreements such as frequent flyer participation, joint operation, code sharing, and joint scheduling etc.[311] between carriers of different countries for preferential exchange of traffic. While carrier agreements undoubtedly are effective, they are limited since they are easy to cancel. The third is a strong alliance involving equity swaps. Carriers of different countries maintain their own corporate identity, but they are affiliated in order to provide a global network service. The intent of these equity positions is not so much for one carrier to control another but rather to solidify an operating relationship. While strong alliances are popular among air carriers[312] they have their own limitations; in order to operate this way carriers should be privatized and sometimes foreign investment could be restricted by domestic law. The comparison of types of alliance could be summarized as follows:

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[311] Simple Alliance excludes traditional cooperation between carriers concerning technical and operational ground handling, refuelling and security services, handling of passangers, freight and baggage at airports and in-flight cartering, etc.

[312] For transfers of airlines, see *European Air Law*, *supra* note 50 at 61-65 and K.H. Lee ed., *The Structure and Strategy of Air Transport Industry* (Seoul: Park-Young-Sa, 1991) at 192.

Comparison of Types of Airline Alliance

Classification	Strong Point	Weak Point
Simple Alliance	- Relatively easy to form an alliance regardless of investment requirement - Independence of business	- Fragile solidarity and easy to cancel
Strong Alliance	- Easy to cooperate with partner carriers because of strong solidarity - Expectation of benefits from investment under the condition that partner's performance of business would be good	- Difficult to cancel - The business performance of one of the partners may affect the others - Foreign investment controls may restrict equity positions
Corporate Merger	- Enabled to use economies of scale - Reinforcement of market control and competitiveness through mega-carriers	- Losing brand recognization of individual airlines - Political obstacles because of principle of sovereignty - Possible huge deficit in case of economic recession and/or sudden rise of oil prices

The reason why Korea (or Korea's carriers) pursues airline alliances is that cooperation with EC carriers is the easiest and most practical way to overcome the barriers of the EC market without strong resistance from Member States of the EC. Through the alliance Korea would obtain the similar effects of setting up its own hub-

and-spoke system in the EC. Which type of alliance is best for Korea?[313] Taking into account their strong and weak points, it is likely that a strong alliance is preferable. However, a simple alliance could be introduced as the easier type.[314] Then, gradually, the degree of alliance would be enhanced to move toward close cooperation including equity swaps.

Which EC carriers should be the partners for Korean carriers? It can be said with a high degree of probability that within the territory of the EC approximately seven big airlines will dominate the market:[315] British Airways, Air France, Lufthansa, and medium-sized airlines such as Iberia, Alitalia, KLM, SAS - possibly with even closer cooperation than before liberalization, either among each other or with non-EC carriers.[316] The other carriers will have marketing opportunities - if they are not taken over - either as "satellites" of the largest carriers (albeit formally keeping their names)

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[313] KAL has concluded a commercial agreement with two EC carriers: Air France (Revenue Pool) and Lufthansa (Joint Operations).

[314] Even though the Korean Aviation Act permits 49 % ownership by foreigners, the Regulation on Foreign Investment, based on the Foreign Investment Act, practically restricts foreign investment in national carriers except when specific guidelines are met. See Article 6 of the Korean Aviation Act and Appendix 2 of the Regulations on Foreign Investment, Decree 93-3 of Ministry of Finance of Korea; Additionally, EC Major Carriers except British Airways are owned, partially or whole, by their governments. This fact may also affect adversely the process of exchange of equity between air carriers.

[315] European Air Law, *supra* note 50 at 67.

[316] Practically major EC carriers have closely cooperated with other carriers. See Appendix IV. Transnational Airline Alliances of major EC carriers.

or by finding a niche in the market (e.g. extension of inter-regional transport).[317] It is likely that non-EC carriers could use such smaller airlines as "Trojan horses" in the internal EC Market. Non-EC carriers do not need to operate to all European airports. Instead they operate to a few hubs and employ a European carrier which is not one of their competitors to operate feeder services. However, because such smaller airlines are closely related to the seven big carriers[318] it is unlikely that they will freely go against the will of the EC major carriers. Therefore, our analysis will concentrate on these seven carriers. We will have a close look at the competitive position of the EC's major carriers.[319]

- Air France (AF)

In 1990, Air France ranked third in world airline business. The French Government owned 99.38 of equity in 1991. Its route structure connected Paris to a wide range of destinations in Europe, Africa, Asia, and the Americas. In 1989, Air

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[317] European Air Law, *ibid.*

[318] *Ibid.* at 62-65 Figure 3 Transfers of Airlines all over the World.

[319] The three European Quality Allaince (EQA) airlines - Swissair, Austrian and SAS - and KLM were planning to create a single, integrated company called "Alcazar" (the Avmark Aviation Economic, April 1993). However, there were many obstacles to becoming a single entity, (ITA press 191, 16-31 May 1993). Thus, that deal was finally abandoned (The Financial Times, 22 November 1993). Source from Phillip Shearman, *supra* note 301 at 102-103; *Recent Trends of Air Transport in the World and Korean Air Line's Strategy* (Seoul: Korea Maritime Institute, 1992) at 195-198; Eric J. Vayle, "Swissair's Alliances" (1992) Harvard Business School No. 9-391-111 in material for Concordia University's MBA program at 2-8; *Airlinefinance Report 1990-1991* (London: Euromoney Publications, 1991) at 205-207 and 249-253; Airline Business February 1992 and August 1992; Aviation Daily 11 February 1993.

France acquired majority interests in UTA and Air Inter, competitors for domestic passengers and for traffic between France and other European countries. Combined, the three companies had revenues in 1989 of about $8 billion and controlled 9.2% of European traffic in 1990. Air France was not regarded as having superior in-flight service. After its purchases of UTA and Air Inter, Air France controlled more than 60 % of traffic at Paris's two major airports. In 1991, Air France was struggling to integrate its diverse acquisitions. France occupied a strong geographic, political and financial position in the EC and is a co-owner of Amadeus CRS.

- British Airways (BA)

In 1990, British Airways ranked fifth in world airline business. It was fully privatised in 1987. British Airways was the furthest-reaching international carrier in the world. In 1989, it carried almost 25 million passengers to destinations on every populated continent. It controlled 50% of traffic at its hub, London's Heathrow airport, and 15.5% of traffic in Europe in 1990. The carrier also used airports in Singapore, Bombay, and Kuwait as secondary, intermediate hubs for trips between London and the Pacific Rim. After privatization, it was also aggressive in pursuing strategic opportunities. In addition to interline agreements with Aeroflot, Interflug, Sabena, and United, the carrier's international partnerships included a meshed schedule arrangement with Delta through Dallas-FortWorth airport, and cargo service to the Far East in conjunction with Singapore Airlines. It also owned a 25% share in Covia, the partnership that ran the Apollo CRS. In 1987, it acquired its main domestic competitor,

British Caledonian, and in 1991 it was negotiating deals with the Belgian airline Sabena, and KLM. Also, it acquired 19.9% of total US Air equity in 1993. BA is a co-owner of Galileo CRS.

- Lufthansa (LH)

In 1990, Lufthansa ranked fourth in world airline business. The German Government, both federal and local, owned 59.16% equity in 1991. It carried passengers to 160 destinations on all continents. Lufthansa had hubs in both Frankfurt and Munich, and received about 45% of its revenues on flights among European countries. It carried 11.9% of European passengers in 1990. Flights to North America and Asia each generated about 20% of revenues. Luthansa was known in the international travel industry for two unique strengths. First, it was a leader in the international transport of cargo. The reasons for its strength in cargo transport included high technology support services and an international CRS agreement with Air France and Japan Airlines to reach cargo customers around the world. Lufthansa's second strength was its capability in maintenance. One-quarter of its employees were in maintenance. Since 1988, Lufthansa had been aggressively pursuing market share on many of its routes, especially travel between Eastern and Western Europe. Moreover, it was an investor or partner in over thirty European businesses. These included a German commuter airline, a charter carrier in Spain, and joint ventures in China and the USSR. Lufthansa is a co-owner of Amadeus CRS.

- KLM

In 1990, KLM ranked nineteenth in world airline business. The Netherlands government owned 38.2% equity of it in 1991. In 1989, KLM flew passengers between Amsterdam and 140 other destinations in 77 countries. Almost half of KLM's destinations were in Europe and it carried 4.2% of European travellers in 1990. The majority of its traffic flew between Amsterdam and North America or between Amsterdam and the Far East. KLM enjoyed a strong reputation for customer service. KLM has a money-losing equity investment in Northwest Airlines. U.S. regulations currently prohibit foreign carriers from owning more than 25% of one of its carriers. KLM is a co-owner of Galileo CRS.

- SAS

In 1990, SAS ranked twelfth in world airline business. It was controlled by three holding companies; ABA (Sweden, 42.9%), DDL (Denmark, 28.6%), DNL (Norway, 28.6%); each respective government owned 50% of equity of each company in 1991. SAS flew to 82 destinations in 36 countries in 1990. In Europe, SAS handled 8.8% of traffic. SAS signed a cooperation agreement which led to the formation of the European Quality Alliance with Austrian Airlines - Swissair and Finnair in October, 1989.[320] SAS also had an aggressive alliance strategy. This philosophy led SAS to take a large

[320] For a discussion of the failed Alcazar alliance, see *supra* note 319.

ownership stake in Continental Airlines and to form an alliance with Thai International and All Nippon Airways. SAS is a co-owner of Amadeus CRS.

- Alitalia (ALI)

In 1990, Alitalia ranked fifth in world airline business. The Italian government owned 84.9% equity. Its scheduled service network covered all continents. It derived 42% of its scheduled passenger revenue from Intra-European Services in 1989. It controlled 7.2% of European Traffic in 1992. Its restructuring programme continues with the objective of transforming a bureaucracy-ridden company into a commercially oriented airline with a streamlined management structure. The airline, preoccupied perhaps with internal problems, was comparatively slow to negotiate alliances with airlines in other countries. Alitalia agreed to a programme of commercial co-operation with Iberia. The two Airlines' route systems were to some extent complementary; Alitalia lacked coverage in some Latin American Markets, which Iberia could provide and Iberia did not serve the Far East, whereas Alitalia did. Alitalia is a co-owner of Galileo CRS.

- Iberia (IBE)

In 1990, Iberia ranked eighteenth in world airline business. It was wholly owned by the Spanish Government in 1991. It operated a broadly based network around the world. It derived 40% of its scheduled passenger revenue from European networks in 1989. It controlled 8.2% of European traffic in 1990. Much of the airline activity in

Spain was tourism-related. Iberia's competitive advantage was its strength in the Europe to Latin America market. Its goal has been to use Miami as a hub to reach key points in Latin America. Iberia is a co-owner of Amadeus CRS.

If the Korean carriers selected possible EC partners, the criteria could be as follows:[321]

(i) carriers which do not have an alliance with other Asia/Pacific carriers, especially Japan's carriers, which are in a competing position with Korean carriers;

(ii) carriers which have networks complementary to those of the Korean carriers for Eastern Europe or Africa, where Korean carriers do not fly;

(iii) carriers which have market-dominating power and a network in the EC and which are stable in financial and managerial terms;

(iv) carriers which have airports as hubs for Korean carriers and have enough landing slots in congested airports in the EC; and

(v) carriers which have a posssibility of a capital alliance with Korea's carriers.

According to the above-mentioned criteria, from the Korean carriers's perspective, the comparison of good and bad points of EC major carriers as possible partners could be summarized as follows:

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[321] Recent Trends of Air Transport in the world and Korean Air Lines Strategy, *ibid.* at 198.

Comparison of Good and Bad Points of EC Carriers

Criterion	AF	BA	IBE	KLM	ALI	LH	SAS
(i)	X	O	X	X	X	X	X
(ii)	O	X	X	X	O	O	O
(iii)	O	O	X	X	X	O	O
(iv)	O	O	O	O	O	O	X
(v)	X	O	X	O	X	O	O

O: positive; X: negative

AF, BA, LH and SAS could be possible partners for Korean carriers.[322] However, there are also possible obstacles to forming an alliance with these carriers. LH is a major competitor with KAL in the international air cargo market and is expanding its direct routes to Asia. BA already has an intermediate hub in Singapore and good networks in the Asia region. SAS already has cooperated with All Nippon Airways and Thai International Airways. AF has relatively less obstacles to forming an alliance but government ownership of AF prevents both sides from forming more advanced alliances including equity swaps. However, the plans are currently under way to privatize Air France. As of now, it is difficult to predict which EC carrier Korean carriers will cooperate with and to what degree. However, provided that an alliance is

[322] If we consider the global network, the possible EC partners might change depending on degree of alliance between U.S. mega-carriers and EC carriers. U.S. carriers' global strategy may affect the alliance strategy of Korean carriers with EC carriers.

the best way for Korea to overcome the intangible barriers of the EC air transport market, Korean carriers must seek the best method to cooperate with EC carriers as soon as possible. The application of EC competition law - a major legal problem in the process of forming an alliance - could be avoided with the help of EC carriers who are already exposed to competition law and have experience in dealing with that problem.

CONCLUSION

As of 1 January 1993, the EC broke down many internal barriers between Member States through gradual liberlization measures. Thus, as far as the air transport industry is concerned, it was integrated into a single market: all EC carriers are given free access to all intra-routes except for the limitation of domestic routes until April 1997; fares and rates within the EC may be freely set; any company satisfying certain basic requirements is granted an operating license; and the national ownership and control criteria for airlines are replaced by the Community criteria, which pave the way for full cross-border airline mergers and take-overs and also permit airlines from one Member State to set up operating subsidiaries in other Member States.

However, these changes in the EC may most significantly have affected the current international air transport legal system premised on individual sovereignty, nationality and bilateralism. In particular, the concepts of "Community air carrier" and "community cabotage area" are likely to be incompatible with the current system in many aspects: nationality of aircraft, cabotage, bilateral air transport agreements, and the function of IATA.

The liberalization in the EC will increase the competitiveness of the EC carriers and integration will enhance the bargaining power of the EC against the non-EC countries. However, despite the development in the EC of a common air transport policy aiming at a truly integrated internal market, there is as yet no common policy toward non-EC countries. Many non-EC countries are concerned that the creation of an internal

market may affect their traffic rights to, from and within the EC. For air carriers offering long-haul international service, the EC is a very important market, not only for point-to-point journeys, but in the context of a total network. Korea is no exception. However, Korea which has a relatively small domestic market is not an attractive principal market to EC carriers in northeastern Asia. Thus, for Korea it will be more difficult to protect and increase its rights in the EC than for Japan and China. Korea's possible strategies to overcome the competitive environment posed by EC air transport policy are regional cooperation as a counter block toward the EC, increasing the access to the EC market and airline alliances. However, there is a little possibility of regional cooperation, because of a lack of common interests between countries in northeastern Asia. There might be some opportunity for Korea to capitalize on its current leverage in bilateral negotiations over recognition of the "Community clause". Yet in the long run, if Korea wants additional access to the EC, it will be difficult to provide adequate reciprocity to EC carriers. Thus an airline alliance is the most practical way to overcome the barriers of the EC market without strong resistance from Member States of the EC. However, seeking partners is difficult. Therefore, the Korean Aviation authority and the Korean Aviation industry must cooperate together to produce the best comprehensive plan to deal with the EC air transport market as soon as possible.

Appendix I

ARTICLES OF THE UNION TREATY RELEVANT TO THIS THESIS

TITLE II - PROVISIONS AMENDING THE TREATY ESTABLISHING THE EUROPEAN ECONOMIC COMMUNITY WITH A VIEW TO ESTABLISHING THE EUROPEAN COMMUNITY

ART. G [Amendments to the Treaty of Rome]

G. The Treaty establishing the European Economic Community shall be amended in accordance with the provisions of this article in order to establish a European Community

G(A) Throughtout the Treaty:
The term "European Economic Community" shall be replaced by the term "European Community".

Article 2 shall be replace by the following:
"ART. 2 [Tasks of the Community]
The Community shall have as its take, by establishing a common market and an economic and monetary union and by implementing the common policies or activities referred to in article 3 and 3A, to promote throughout the Community a harmonious and balanced development of economic activities, sustainable and non-inflationary growth respecting the environment, a high degree of convergence of economic performance, a high level of employment and of social protection, the raising of the standard of living and quality of life, and economic and social cohesion and solidarity among member states."

Article 3 shall be replaced by the following:
"ART. 3 [Activities of the Community]
For the purposes set out in article 2, the activities of the Community shall include, as provided in this Treaty and in accordance with the timetable set out therein:
(a) the elimination, as between member states, of customs duties and quantitative restrictions on the import and export of goods, and of all other measures having equivalent effect;
(b) a common commercial policy;

(c) an internal market characterised by the abolition, as between member states, of obstacles to the free movement of goods, persons, services and capital;
(d) measures concerning the entry and movement of persons in the internal market as provided for in article 100C;
(e) a common policy in the sphere of agriculture and fisheries;
(f) a common policy in the sphere of transport;
(g) a system ensuring that competition in the internal market is not distorted;
(h) the approximation of the laws of member states to the extent required for the fuctioning of the common market;
(i) a policy in the social sphere comprising a European Social Fund;
(j) the strengthening of economic and social cohesion;
(k) a policy in the sphere of the environment;
(l) the strenthening of the competitiveness of Community industry;
(m) the promotion of research and technological development;
(n) encouragement for the establishment and development of trans-European networks;
(o) a contribution to the attainment of a high level of health protection;
(p) a contribution to education and training of quality and to the flowering of the cultures of the member states;
(q) a policy in the sphere of development co-operation;
(r) the association of the overseas countries and territories in order to increase trade and promote jointly economic and social development;
(s) a contribution to the strengthening of consumer protection;
(t) measures in the spheres of energy, civil protection and tourism."

The following article shall be inserted:
ART. 3A [Economic and monetary union]

The following article shall be inserted:
"ART. 3B [Principle of subsidiarity]
3B The Community shall act within the limits of the powers conferred upon it by this Treaty and of the objectives assigned to it therein.
In areas which do not fall within its exclusive competence, the Community shall take action, in accordance with the principle of subsidiarity, only if and in so far as the objectives of the proposed action cannot be sufficiently achieved by the member states and can therefore, by reason of the scale or effects of the proposed action, be better achieved by the Community.
Any action by the Community shall not go beyond what is necessary to achieve the objectives of this Treaty."

Article 6 shall be deleted and article 7 shall become article 6. Its second paragraph shall be replaced by the following:
"The Council, acting in accordance with the procedure referred to in article 189C, may adopt rules designed to prohibit such discrimination."

Article 75 shall be replaced by the following:
"ART.75 [Implementation of transport policy]
75(1) For the purpose of implementing article 74, and taking into account the distinctive features of transport, the Council shall, acting in accordance with the procedure referred to in article 189C and after consulting the Economic and Social Committee, lay down:
(a) common rules applicable to international transport to or from the territory of a member state or passing across the territory of one or more member states;
(b) the conditions under which non-resident carriers may operate transport services within a member state;
(c) measures to improve transport safety;
(d) any other appropraite provisions.
75(2) The provisions referred to in (a) and (b) of paragraph 1 shall be laid down during the transitional period.
75(3) By way of derogation from the procedure provided for in paragraph 1, where the application of provisions concerning the principles of the regulatory system for transport would be liable to have a serious effect on the standard of living and on employment in certain areas and on the operation of transport facilities, they shall be laid down by the Council acting unanimously on a proposal from the Commission, after consulting the European Parliament and the Economic and Social Committee. In so doing, the Council shall take into account the need for adaptation to the economic development which will result from establishing the common market."

In Title II of Part Three, the title of Chapter 4 shall be replaced by the following:
"Title VII - Common Commercial Policy"

Article 113 shall be replaced by the following:
"ART. 113 [Implementation of common commercial policy]
113(1) The common commercial policy shall be based on uniform principles, particularly in regard to changes in tariff rates, the conclusion of tariff and trade agreements, the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies.
113(2) The Commission shall submit proposals to the Council for implementing the common commercial policy.

113(3) Where agreements with one or more states or international organisations need to be negotiated, the Commission shall make recommendations to the Council, which shall authorise the Commission to open the necessary negotiations.
The Commission shall conduct these negotiations in consultation with a special committee appointed by the Council to assist the Commission in this task and within the framework of such directives as the Council may issue to it.
The relevant provisions of article 228 shall apply.
113(4) In exercising the powers conferred upon it by this article, the Council shall act by a qualified majority."
Article 114 shall be replaced.

Article 228 shall be replaced by the following:
"ART. 228 [Agreements with third countries and organisations]
228(1) Where this Treaty provides for the conclusion of agreements between the Community and one or more states or international organisations, the Commission shall make recommendations to the Council, which shall authorise the Commission to open the necessary negotiations. The Commission shall conduct these negotiations in consultation with special committees appointed by the Council to assist it in this task and within the framework of such directives as the Council may issue to it.
In exercising the powers conferred upon it by this paragraph, the council shall act by a qualified majority, except in the cases provided for in the second sentence of paragraph 2, for which it shall act unanimously.
228(2) Subject to the powers vested in the Commission in this field, the agreements shall be concluded by the Council, acting by a qualified majority on a proposal from the Commission. The Council shall act unanimously when the agreement covers a field for which unanimity is required for the adoption of internal rules, and for the agreements referred to in article 238.
228(3) The Council shall conclude agreements after consulting the European Parliament, except for the agreements referred to in article 113(3), including cases where the agreement covers a field for which the procedure referred to in article 189B or that referred to in article 189C is required for the adoption of internal rules. The European Parliament shall deliver its opinion within a time-limit which the Council may lay down according to the urgency of the matter. In the absence of an opinion within that time-limit, the Council may act.
By way of derogation from the previous subparagraph, agreements referred to in article 238, other agreements establishing a specific institutional framework by organising cooperation procedures, agreements having important budgetary implications for the Community and agreements entailing amendment of an act adopted under the procedure

referred to in article 189B shall be concluded after the assent of the European Parliament has been obtained.
The Council and the European Parliament may, in an urgent situation, agree upon a time limit for the assent.
228(4) When concluding an agreement, the Council may, by way of derogation from paragraph 2, empower the Commission to approve modifications on behalf of the Community where the agreement provides for them to be adopted by a simplified procedure or by a body set up by the agreement; it may attach specific conditions to such empowerment.
228(5) When the council envisages concluding an agreement which calls for amendments to this Treaty, the amendments must first be adopted in accordance with the procedure laid woen in article N of the Treaty on European Union.
228(6) The Council, the Commission or a member states may obtain the opinion of the Court of Justice as to whether an agreement envisaged is compatible with the provisions of this Treaty. Where the opinion of the Court of Justice is adverse, the agreement may enter into force only in accordance with article N of the Treaty of European Union.
228(7) Agreements concluded under the conditions set out in this article shall be binding on the institutions of the Community and on member states."

Appendix II

Comparison between Third and Second Package

Third Package	Second Package	Effects
Regulation on Licensing of Air Carriers Rules for economic and technical fitness of air carriers	Nothing	Very important
Entitlement for undertaking to be licensed as an air carrier when fitness criteria are respected		Will establish national monopolies.
National ownership rules are abolished and Community ownership criteria introduced.		Make easier to create new air carriers based on objective economic criteria.
Rules for leasing of aircraft to ensure that safety levels are respected and that dumping of aircraft from third countries will not take place.		The right of establishment will be given a real meanibg for civil aviation.
Regulation on Market Access Any Community air carrier may operate between two airports within the Community.	Receiving states obliged to accept a designated air carrier, subject to certain multiple desigantion traffic thresholds, but full discretionary powers for whether or not an air carrier would be designated by its own government.	The real introduction of the freedom to provide services throughout the Community.
Full fifth (and seventh) freedom	Limitations on fifth freedom and absence of seventh freedom rights.	Important for freedom to provide services.

Domestic services included but limitations may be applied for transitional period to domestic air carriers.	No domestic air services included.	Important inclusion but full effect not until 97.4.1.
Traffic rights cover also cabotage subject to a trasitional limitation until 97.4.1.	No cabotage	Freedom to provide services would not exist without cabotage.
Public service obligations	Public Service obligation but less developed.	Improvement in view of the inclusion of domestic services.
Safeguards in order to be able to deal with congestion prolblems allowing inter alia for intermodal coordination.	Simpler safeguards and no intermodal coordination	Ensures safety without losing flexibility
Operational and traffic distribution rules must be respected but possibility for Commission to intervene to avoid misuse.	Same rules but no role for the Commission	Guarantee for air carriers from other Member States
No bilateral capacity limitations.	Free capacity but only within a zone (60:40) and subject to approval of state of origin	Important in order to ensure that air carriers can take and implement commercial dicisions.
Capacity safeguards in order to deal with catastrophic economic develepments.	Same	
All air transport services included, both scheduled and non-scheduled.	Only scheduled air services	Important in order to ensure a level playing field where all air carriers are treated equally.

Air Fares and Rates Free pricing	Complicated mixture of nonal system, double disapproval and double approval for passeenger while free pricing for air cargo.	Allows commercial decison making of air carriersm.
Limited possibilities for Member States to intervene against exessive basic (ecnonomy) air fares or a catastrophic downwards price development	Replaces the zonal system etc.	Introduces considerable feedom for air carriers.
Same possibilities for Commission to intervene as for Member States (also for domestic services).	Limited possibilities for Commission to intervene.	Important in onder to ensure smae application rules throughout the Community.

Source: H.A. Wassenbergh, in material for the Guest Lectures of Prof. H.A. Wassenbergh at McGill University, IASL, March 1993 at 70-71.

Appendix III

Comparison of NSMA and Other New Airports in Northeast Asia Region

Description	NSMA	Japan's Kansai Airport	Hong Kong New Airport
Site Area	15.^{2} million m^2 (46.^{43} million m^2)	5.^{12} million m^2 (11.^{98} million m^2)	12.^{51} million m^2 (14.^{85} million m^2)
Runway	1 (4)	1 (3)	1 (2)
No. of Aircraft Operations	170,000 ops/yr (700,000 ops/yr)	160,000 ops/yr (260,000 ops/yr)	160,000 ops/yr (320,000) ops/yr
No. of Passengers	27 million pax/yr (100 million pax/yr)	25 million pax/yr (40 million pax/yr)	35 million pax/yr (87 million pax/yr)
Construction work period	1992-97 (2040)	1986-94 (unfixed)	1991-97 (2040)
Project Cost	$4.3 billion	$10.09 billion	$12.43 billion

Note: ( ) Ultimate Development

Source: Task Force for the New Airport of Ministry of Transportation of Korea, 1992

Appendix IV

Transnational Airline Alliances of Major EC Carriers

Airline	Partner	Share of Airline (%)	Share of Partner (%)	Kind of Cooperation
Air France	Air Inter	37		M
	Air Madagascar	3.48		
	Air Mauritius	12.77		R
	Austrian	1.5		
	Canadian AL			R
	Euro Berlin	51		
	Lufthansa			Coop, J
	R Air Maroc			M
	Thai Intl			RC
	UTA	54.8		
Alitalia	ATI	100		
	Canadian AL			R
	Iberia			M
	USAir			M
British AW	Air Mauritius	12.77		
	Air NZ			R
	Caledonian	100		
	Canadian AL			R*
	Delta			R
	GB Airways	49		
	Maersk			J
	SWA	20+		
	United			M
Iberia	Alitalia			M
	Aviaco	67		
	Japan AL			R
	R Air Maroc			M
	Viva	100		

Airline	Partner	Share of Airline (%)	Share of Partner (%)	Kind of Cooperation
KLM	Air UK	14.9		M
	ALM			M
	Garuda			R
	Martinair	29.8		
	Nippon Cargo			RC
	NLM	100		M
	Northwest	14.9		RC
	SWA	20+		
	SIA			RC
	Transavia	40		
	Viasa			R
Lufthansa	Aer Lingus			C
	Air France			Coop. J
	Air Mauritius			R
	Canadian AL			R
	Cargolux	24.5		
	Cathay			RC
	Condor	100		
	DHL Intl	5 (20*)		
	Euro Berlin	49		
	Garuda			R
	German Cargo	100		
SAS	AL of Britain	24.9		
	All Nipon			M
	Canadian AL			R
	Continental	9.9		M
	Finnair	≤ 10*	≤ 10*	M
	LAN-Chile	30		
	Linjeflyg	100		
	Scanair	100		
	Spanair	49		
	Swissair	7.5*	7.5*	M
	Thai Intl			M
	Varig			R

Explications:

•	To be planned
AL	Airlines
	Except permission
M	Marketing Agreement
R	Line Agreements
J	Joint venture
C	Cargo Agreements

Situation: November 1990
Source: European Air Law, *supra* note 50 at 62-65.

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