RECENT TRENDS IN EUROPEAN AIR TRANSPORT LAW AND POLICY WITH REFERENCE TO ROUTES, TARIFFS AND CAPACITY

by

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ABSTRACT

This thesis illustrates the trends towards eventual change of the regulatory system of air transport in Western Europe which is now based on bilateral air transport agreements and, in the case of non-scheduled services, on unilateral state authorization. The shortcomings of the present regulatory system and the factors hampering a change are discussed with reference to intra western European services.

Intra western European aviation is highly affected by and dependent on the traffic between the U.S. and Europe. A description of the situation over the North Atlantic is thus necessary.

The intra western European market is compared with the U.S. domestic market, to understand why the U.S. style deregulation can not be applied to intra European air services.

A survey of the work done by the European Civil Aviation Conference and the European Economic Community is made to assess whether an eventual regulatory change can be made within the framework of the activities of these institutions.

RESUME

Cette thèse illustre les tendances vers une modification éventuelle du système de réglementation régissant le transport aérien en Europe occidentale, lequel système se compose maintenant d'accords bilatéraux et, en ce qui concerne les vols non réguliers, de l'autorisation étatique unilatérale. Les failles du présent système de réglementation ainsi que les facteurs qui nuisent au changement sont étudiés tout en faisant référence aux services intérieurs d'Europe occidental.

Etant donné que ces services aériens sont largement affectés et dépendent du traffic entre les Etats-Unis et l'Europe, une étude de la situation sur l'Atlantique Nord s'avère nécessaire.

Une comparaison est faite entre le marché intérieur Ouest-Européen et le marché intérieur américain afin de voir pourquoi la déreglementation à l'Américaine ne pourrait être appliquée en Europe.

Un survol du travail fait par l'ECAC et la Communauté Economique Européenne est fait afin de voir si un changement éventuel de réglementation pourrait être accompli dans le cadre de ces institutions.

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TALBE OF CONTENTS

INTRODUCTION

The European continent consists of many relatively small states, each one too small a market for a large airline. To develop an air transport net in Europe, the European states are thus depended on each other.

International air transportation crosses national borders and thereby involves the concepts of sovereignty and jurisdiction. Since states are reluctant to surrender control over their territory, the attempts made to establish a multilateral convention on commercial air transport rights have all failed.

A worldwide system of bilateral agreements was created instead, ensuring the states would retain complete control over aviation activities in their respective territories. The system has worked well since 1946 when Bermuda I was concluded. Most bilateral agreements in the world are similar to Bermuda I which gives a verbal coherence to the system.

States are most concerned about the commercial aspects of air transport. These aspects are expressed in the basic concepts of bilateral agreements: capacity, routes and tariffs. Thus, it is important to describe these concepts and explain wy these are controlled and regulated. Each of the concepts is complicated and needs a thorough examination which has been done in the first chapters. It is necessary to know the basic commercial problems of bilateral agreements to better understand why most European states have adopted restrictive aviation

policies. It is not only the bilateral agreements that affect European air transport. Charter services are mainly governed by unilateral authorizations but carry 50% of all intra-European traffic. Consequently, how charter is regulated and the objects of European charter policy are described in Chapter 12. The full effects of the U.S. deregulation are not yet visible. However, since European and American aviation are closely related, e.g. the North Atlantic is the busiest market in the world - liberalizing trends have also emerged in Europe, exemplified by the liberal agreements concluded between the U.S. and the Federal Republic of Germany, Belgium, the Netherlands, and further, the Memorandum of Understanding 1982 on tariffs concluded between the U.S. and some European states.

A comparison between the U.S. and Europe is made to show the differences and similarities and why the U.S. deregulation can not be applied in the European market.

An interesting phenomenon in Europe is regional aviation. It is dependent on liberal governmental attitudes to be able to perform cross border services with prices lower than the national carriers charge. Regional aviation has not developed as much as its potential premises due to the restrictive policies of governments. Nevertheless, with emerging liberal trends in Europe, regional aviation is likely to have a future in the European air transport system. Within Europe, with its multitude of states and political, legal and economic systems, there

has been a definite trend towards closer forms of co-operation. These evolutionary forms of co-operation among states as well as among airlines have reached a level of intensity which may permit us to speak of air transport integration in a wider sense. An eventual deregulation must be organized and all European states and airlines must co-operate for the deregulation to be effective. It is suitable that deregulation is studied and, to some extent, carried out within the framework of ECAC and EEC. A survey of the result of their activities is made in Chapters 5 and 10.

At the present stage European states have restrictive air transport policies. However, there seems to be trends towards more liberalization of the air transport system. The best example is the draft Plurilateral Air Transport Agreement - PATA - presented in the conclusion. If it will be implemented, it will mean a substantial step forward on the path of liberalization.

CHAPTER 1: FREEDOM OF THE AIR

The Convention of International Civil Aviation of 1944 (the Chicago Convention), while it covers comprehensively the principles of public international law with respect to international air navigation, fails to cover the field of international air transport in a comprehensive fashion. The Convention covers technical and administrative matters relating to air transport, but is neutral as to the commercial aspects of international air transport.[1]

The assertion of the principle of sovereignty expressed in Article 1 of the Convention, is the antithesis of freedom of the air, and the Convention is, therefore, hampering the development of commercial international air transport. Article 1 also legitimizes the right of the states to protect their own airlines internationally as well as domestically. At the Chicago Conference in 1944, the states were, with few exceptions, not ready to surrender this aspect of their sovereignty.

The right of the contracting states to regulate international scheduled air services is also positively stated in Article 6 which reads as follows:[2]

> «No scheduled international air service may be operated over or into the territory of a contracting state, except with the special permission or other authorization of that state, and in accordance with the terms of such permission or authorization.»

As we can see and will discuss further in this thesis, states are most reluctant to let any other state or international organization govern commercial aviation activities in their respective territories. The effect of this has been that except for the limited exceptions made in Article 5 for non-scheduled services and the even more limited, but not true exceptions of the International Air Service Transit Agreement, the grant of commercial rights for international air transport has been performed by means of bilateral treaties, or in the case of non-scheduled commercial rights, generally by unilateral authorization.

While Article 5 of the Convention confers greater freedom for commercial aviation in the matter of non-scheduled traffic,[3] the scope of the article has been limited by a narrow interpretation. Under this article, all contracting parties grant airlines from other contracting states commercial rights for non-scheduled air services without prior permission. However, the rights granted are a chimera because they are subject to the grantor state's right to impose regulations, conditions or limitations that it considers desirable.

The practical implication is that all non-scheduled traffic rights are now governed by unilateral rules,[4] except in these few cases where bilateral agreements have been negotiated.

The rights of states to control international air services inside their territory is also reinforced by Art. 68 of the Convention, which gives states the right to designate the route to be followed and the airports to be used within its territory.

On the same day the Chicago Convention was opened for adherence[4], two other conventions were established to deal with the commercial problems of civil aviation: «The International Air Services Transit Agreement» or the so-called «Two Freedoms Agreement», and the «International Air Transport Agreement» or the «Five Freedoms Agreement». There are two types of overflight over a territory: operational and commercial.[5]

The operational flights are governed by the «Two Freedom Agreement» where the contracting states grant each other:

1) The privilege to fly across its territory without landing; and

2) the privilege to land for non-traffic purposes.

As of January 1981, this agreement had been ratified by 93 states. This implies that it is not difficult to give away non-commercial rights since they do not affect the grantor state's own traffic to any great extent.

The «Transit Agreement» does not require prior permission to enter the airspace of another state's territory. However, according to Shawcross and Beaumont's interpretation of ICAO Council's Advisory Opinion in 1951,[6] an airline or aircraft must ask for prior permission though, which the contracting state can not refuse without good reason.

The next three freedoms which are included only in the «Five Freedoms Agreement» are as follows:

- Freedom 3 - the privilege to put down passengers, mail and cargo taken on in the territory of the state whose nationality the aircraft possesses.

- Freedom 4 - the privilege to take on passengers, mail and cargo destined for the territory of the state whose nationality the aircraft possesses;

- Freedom 5 - the privilege to take on passengers, mail and cargo destined for the territory of any other contracting state and the privilege to put down passengers, mail and cargo coming from any such territory.

The sixth, seventh and eighth freedoms are not referred to in the «Five Freedoms Agreement». Freedom six and seven can be regarded as special types of fifth freedom traffic,[7] while the eighth freedom is cabotage and is regarded as domestic traffic. (See Art. 7 of the Chicago Convention) There exist distinctions which are worth pointing out. Cheng defines these three freedoms accordingly:[8]

- Freedom 6 - The sixth freedom is 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 either has 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.

- Freedom 7 - The seventh freedom is the right for a carrier operating entirely outside the territory of the flag-states, to fly into the territory of the grantor state and there discharge, or take on, traffic coming from, or destined for, a third state or states.

- Freedom 8 - The eighth freedom is cabotage and it is the right for a carrier to carry traffic from one point in the territory of a state to another point in the same state. Every state has the right to withhold cabotage rights according to Art. 7 of the Chicago Convention.

The limitation of the rights that are part of the concept of sovereignty recognized in Art. 1 of the Chicago Convention were far to extensive in the «Transport Agreement» for states to accept it. As of January 1981 only twelve states had ratified the «Transport Agreement» not including the U.S.A., and, thus, the agreement is a dead letter.

Consequently, all international scheduled traffic was left to be regulated by bilateral agreements. The adherence to the Transport Agreement would expose each country's airline to market forces and it would also limit their sovereign rights to control what is happening inside their borders.[9]

In these circumstances, only the strongest will win, which might imply that a country's whole air traffic would be carried by foreign carriers. Serious problems can then rise in times of war or other crisis. A state that has total or partial control over another state's air traffic, can neglect the latter state's national interests, which also might have the control over its economic activities limited.

In 1947, there was an attempt in Geneva to create a multilateral convention on scheduled traffic, but the attempt failed due to difficulties in reaching an agreement over the fifth freedom concept.

1.1 Scheduled and Non-Scheduled Traffic

The distinction between scheduled and non-scheduled traffic has during the last decade to some extent become blurred.

Charter traffic - which is classified as non-scheduled traffic - has been subject to numerous restrictions, because it could be carried at lower prices than scheduled traffic. Governments felt that they had to protect carriers of scheduled traffic. Examples of the types of restrictions placed on charter operations are:

1) Affinity Group Charter - the airline could only carry persons who had been members, for a period of six months or more, of an association not formed for purposes of travel; and

2) Inclusive Tour Charter (ITC) - These could only be sold if it was understood that the price of the ticket included hotel and associated facilities.

Later, more liberal forms of charters were permitted. The first of these was the Advanced Booking Charter - ABC - where the passangers had to buy the ticket in advance through a travel agency and usually had to travel to and from the destination with the same group of persons.

The liberalization of charter has now reached a point where the only difference between some types of charter and scheduled traffic is that a charter ticket has to be bought through a travel agency. The carrier itself can not sell charter tickets. As a result of the liberalization of this cheap way of travelling, charter traffic increased.

Airlines with scheduled traffic have taken counter measures though, especially over the North Atlantic, by introducing low fares such as the Advanced Purchase Excursion Fare (APEX) and stand-by fares. The scheduled airlines carrying traffic over

the North Atlantic are now offering many different kinds of cheap fares, so the passengers are now flying with them rather then by charter services, since they provide better service, e.g. in form of higher frequencies at competitive prices.

1.2 Bilateral Agreements

Since no multilateral agreement on scheduled traffic has been achieved, this traffic is governed by bilateral air transport agreements.

The main reasons for bilateral agreements to govern international aviation are: the recognition of the sovereignty of states and the consideration of this service as a phenomenon having important economic implications and being a mercantile activity.[10] A bilateral agreement also provides stability because the government and airline know that they are allowed to exercise traffic into the other country until the agreement is denounced. A bilateral agreement is usually terminated by one year's notice with the consequence that the airline has security for its investments in aircraft and ticket offices for a period in excess of a year. Since there are only two partners involved in a bilateral agreement, small ad hoc adjustments can easily be made. Its flexible nature is thus another advantage of a bilateral agreement.

Bilateral agreements have proven to be useful in developing international scheduled air transport. Many of them belong

to families inspired by standard agreements such as Bermuda I.[11]

There are three main groups of bilaterals: the Bermuda I group, the restrictive predetermination group and the liberal group of bilateral agreements, most of which have been concluded by the U.S.

The Bermuda I agreement, signed in Bermuda in 1946, between the U.S.A. and the U.K., was a compromise between the two governments, where the U.S. wanted freedom for the airlines, while the U.K. wanted restrictions. The U.S. had to give up their free pricing system which was left to an international body - IATA - and the U.K. compromised on its capacity predetermination principle.

The capacity offered by the carriers could not be predetermined by the governments but only controlled by an ex post facto review if there was an unduly large difference in the capacity provided.

It is disputed whether Bermuda I is a restrictive or liberal agreement. It depends on how it is interpreted. There are possibilities to interpret very strictly and practically have an agreement with predetermination of capacity.

The true predetermination agreements split the capacity offered usually on a 50/50 basis with reference to frequencies and amount of seats offered. The estimation of the capacity to be provided is generally calculated on a 60% to 75% load factor.[12]

At the end of the seventies, the U.S. started to negotiate very liberal agreements. The innovation of these agreements is the way in which tariffs are determined. A double disapproval or country-of-origin clause is used which in practice gives each airline freedom to decide what price they want to charge, as long as both governments do not disapprove of the fare. It is difficult to negotiate a bilateral agreement, since both parties want as much traffic as possible for their own airline, for reasons such as:[13]

1) the desire to earn as much money as possible;

2) national prestige. Airlines provide good publicity for national industry, «Trade follows flag»;

3) military and political interests and considerations; and

4) airlines provide a lot of job opportunities in a country and airlines are among many governments regarded as a public utility, so there is also a social aspect.

Most of the difficulties arise in the negotiations of the commercial rights, namely the last three freedoms, especially the fifth.

Freedom three and four are the primary objective of the negotiations and freedom five is the secondary objective. Third and fourth freedom traffic shall constitute the major traffic flow between the contracting states.

The purpose of the services operated under any agreement was primarily to serve third and fourth freedom traffic flows, and capacity carried was to be related primarily to these flows,

but capacity could be justified for fifth freedom traffic flows if there was an economic justification and the third and fourth freedom traffic flows of the other party (fifth freedom traffic of the first party) were not unduly affected.

The reason for these concepts of primary and secondary objectives is that each party has much better control over third and fourth freedom traffic, since this traffic originates in the contracting states. In third and fourth freedom negotiations they do not have to take into consideration what third countries do.[14] Hence, an increasing proportion of international traffic is being carried as third and fourth freedom traffic by the carriers of the countries to which that traffic is third and fourth freedom traffic.

Restrictive agreements deal preferably with third and fourth freedom traffic, which the Latin Americans and East European countries are known to favour.[15]

In negotiating a bilateral agreement, the states concerned have two objectives to think of:[16]

- the promotion of international air traffic for the benefit of the public; and
- the protection of their own national carriers.

Now, states can be divided into two categories: those that are stronger in term of traffic resources and equipment and those that are not strong.[17] For the stronger airlines it is easy to take a liberal position and promote international traffic, because they are strong enough to compete in a free

market which is supposed to be to the benefit of the public.

All states want an airline, but not all of them can establish one in a competitive situation, so the weaker states must take protective measures insisting on equal sharing of traffic.[18] The airlines of the weaker countries do not always possess the capacity and the possibility to serve the whole public. And since it is sometimes difficult for a nation to accept second position in the competition,[19] it will not give away more traffic and capacity to another nation than it can provide itself. Splitting traffic like this on a 50/50 basis with equal shares for the two carriers is to deprive the passengers of a free choice.

Within limits, a state must thus accept being in an inferior position in a bilateral agreement, which, as a matter of fact, is current transport practice.[20] Since Bermuda I was concluded in which generally fifth freedom traffic rights were granted on a generous state, there seems to be more and more restrictions imposed on the right to carry fifth freedom traffic. Hence, an increasing proportion of international traffic is being carried as third and fourth freedom traffic. The countries that started this trend in the sixties were the socialist countries and some Arab countries.[21]

This trend is also confirmed by the previous director of SAS, Carl Nilsson who states that the freedom of the air is not expanding. On the contrary, for example, the SAS fifth freedom

traffic has in ten years declined from 22% to 10% of its total traffic.[22]

These practices are indulged in foremost by countries that, rightly or wrongly, have little confidence in the competitive position of their airlines.[23] But obviously, if these countries continue with their restrictive attitude, the other countries are bond to follow sooner or later whether they wish to or not.

CHAPTER 1: FOOTNOTES

1. H. Wassenbergh, Post-War International Civil Aviation Policy, The Hague 1957, p. 40. Hereinafter cited as "Post-War"

2. Whitney Gilliland, "Bilateral Agreements », from Bradley/McWhinney Freedom of the Air, p. 141.

3. Post-War, p. 31.

4. Interview with Mr. Gustaf Zetterstrom, Department of Transport, Sweden.

5. Paul de Dongo, Progress Toward the Multilateral Exchange of Commercial Air Transport Rights, Thesis McGill Univ., Montreal 1954, p. 248.

6. ICAO Doc. 7107-12, C 1823-12 and 55.

7. Bo Johnson, Suveranitet i havet och luftrummet Stockholm 1972, p. 211.

8. Bin Cheng, The Law of International Air Transport, London 1962, p. 15.

9. De Dongo, ibid, p. 254.

10. F. Escalada, Aeronautical Law, The Netherlands 1979 p. 471.

11. Supra, p. 471.

12. Supra, p. 476.

13. ITA Bulletin Nr. 7/8 1966, p. 215.

14. For further details on primary and secondary objectives, see Escalada, p. 453, De Dongo, p. 266, "Post-War, p. 24, H. Wassenbergh, Aspects of Air Law and Civil Air Policy in the Seventies, The Hague 1970 p. 33f.

    O. Lissitzyn, Bilateral Agreements on Air Transport JALC 1964, p. 251.

15. G. Besse and R. Mathieu, "Ten Years of Commercial Aviation", ITA Studies 65/8-E 1965, p. 47 and 49.

16. Wassenbergh, Aspects of..., p. 17.

    Frank Loy, Bilateral Air Transport Agreements: Some Problems of Finding a Fair Route Exchange from Bradley/McWhinney, p. 175.

17. ITA Bulletin Nr. 7/8 1966, p. 214.

18. Bin Cheng, ibid, p. 240.

19. F. Loy, ibid, p. 176.

20. Supra, p. 176.

21. F. Déak, "The Balance Sheet of Bilateralism", from Bradley/McWhinney, p. 164.

22. American Aviation Week, September 1967, p. 13.

23. F. Déak, ibid, p. 164.

CHAPTER 2: ROUTES

2.1 Origin and Destination

In negotiations for fifth freedom traffic rights, the origin and destination of the traffic play an important role when determining or reviewing the capacity of the carriers. For the states to decide what capacity may be provided by each of the airlines, they must have information about the traffic volume on the routes in question, i.e. data concerning the flow of traffic from its true origin to its true destination.[1] Thus, the larger traffic volume, the larger is the capacity that the states will grant each other.

At first glance it appears to be an easy task to decide the two places and this is so if the traffic is carried between two points and all trips started at one point and terminate at the other.

However, generally it is not possible to define a market by the traffic generated at a single point, since a trip often consists of a series of successive stages. Traffic on a route can have its origin and destination anywhere in the world. Most international routes should, therefore, be considered as an integrated part of a worldwide route pattern of all airline air services.[2] The concept of a passenger trip must, therefore, be defined. This has been done by a panel in ICAO for the purpose of collection of statistics.[3]

The panel had to consider different concepts of origin and destination when trying to solve the problem in defining

the two concepts. Among those considered were:

- «effective» origin and destination, which would take into account ground transport at the beginning and end of an air trip;
- «purpose» origin and destination, which would reflect the main intent of the passenger;
- «stop-over» origin and destination, which would distinguish those points which a passenger has an intention to visit, as distinct from merely changing aircraft;
- «line» origin and destination and «routes» origin and destination, which would refer to points of embarkation and disembarkation on services or on routes specified in a bilateral agreement.

There was no practical possibility of using any of the above concepts, so the panel decided to define the passenger trip in terms of the information given on the ticket.

Relevant concepts for determining origin and destination according to ICAO panel are as follows:

1) ground transport before or after the trip, is excluded;
2) more than one ticket can be issued and in that case they are treated as one ticket;
3) information on one ticket coupon concerning other stages on the trip may not be used for statistics on other stages on the route since the passenger can change his itinerary en route;
4) a directional trip in one statistical period may apply in part to a different statistical period;
5) no splitting of a dual directional trip into two separate directional trips due to some loss of information.

On the basis of the consequences mentioned above the panel established the following definitions of origin and destination.[4]

TOD - Ticket origin and Destination

The first and last points on a whole passenger ticket.

DOD - Directional Origin and Destination

The first and last points on a one-way ticket and the first and last points on each of the two directional parts of a «round-trip».

SOD - On System Origin and Destination

The points at which the passenger enters and leaves the system on a trip.

COD - Coupon Origin and Destination

The points of embarkation and disembarkation covered by one flight coupon.

Routing

A listing of sequence of cities of two or more COD's appearing in a single ticket and also in conjunction with TOD, DOD, SOD where two or more coupons are involved.

Wassenbergh argues that the ticket should not be the criterion for determing the origin and destination of traffic. The ticket is both a ticket and a voucher and as a voucher it makes the determination of the origin and destination of the passenger impossible.[5]

2.2 Different Concepts in Route Negotiations

In all types of trade negotiations, the parties try to achieve an equitable exchange of values and benefits. A nation will be reluctant to suffer any disadvantage from the outcome of an agreement. Thus, in overall trade negotiations, dissimilar products may be subject to the trade; e.g. the grant of a right of free entry of wheat from X country in exchange for X country granting the right of free entry for steel.

The same can be true in the negotiations for air transport routes, there can be a trade of air transport rights in exchange for political or other non-commercial benefits or commercial benefits of another nature.

A more common approach in bilateral air transport negotiations is the use of visual reciprocity where both parties have the right to carry the same amount of traffic on each route, the so-called «double-tracking». Another way of bargaining is to use the «most favoured nation clause» i.e. where state A gets the same benefits as state B has given state C in another bilateral agreement.

Loy expressed the then official U.S. view that there is a fair deal in the route exchange when both parties gained an equitable exchange of economic benefits.[6]

Wassenbergh's view[7] is that the economic benefits derived from a route is not solely dependent on what kind of route the airline has. Other factors such as effective management affect

the economic result of the airline. A fair route exchange exists where there is equal access in practice to a market.

Reciprocity is the principle that governs the present system of bilateralism,[8] meaning in the view of some states, in short, the same amount of frequencies for both airlines on all routes between the two contracting states. However, since both parties are supposed to have about the same amount of traffic on a route, the state with the weakest airline will not give more frequencies to the other state, than its own airline manages to operate. The weakest airline will, thereby, set the limit for both airlines, which will not provide the public with the most extensive service possible.[9]

Where the two carriers are of different strengths, there can be a system of compensation instead. The stronger carrier compensates the weaker for eventual losses on the route.[10] This «royalty» system is used by some countries under various disguises and in rare cases openly.[11] The similarities with pool-agreements are striking and the problem is normally solved through a pool-agreement between the airlines and a 50/50 sharing of revenues.[12] The solution is only possible with a predetermination of capacity or an ex post facto review.

2.3 Exchange of Routes

The two elements that determine the actual formation of the routes and thus the geographical scope of the agreements, are the pattern of the air services and the route structure.

Together with the routes specified there must also be operating rights granted.

For political and economic reasons, both parties attempt to exercise control over the whole, or part of the route, even outside their own territory. The extent and details of the route exchange are determined by the consideration mentioned in part 2.2.

The attempts of the parties to control as much as possible of the routes is exemplified by a rigid route pattern. Usually all points at which traffic rights may be exercised are indicated in the agreement, including intermediate points in third countries. The points may only be altered by agreement between the contracting parties.[13]

This system can severely limit the flexibility of the airlines, since they can not change their services whenever the economic circumstances so require. To avoid this, a sufficient number of intermediate points should be allowed for, so the airlines are able to change the routes when traffic so demands.[14]

It has been argued that a carrier can decide to fly on a route and to points not mentioned in the agreement. Wassenbergh submits that the other party should not be able to prevent the carrier from trying to improve his service by flying to points not mentioned in the agreement, the so-called «blind sector». It is difficult to interpret existing bilaterals as excluding blind sectors according to Wassenbergh. They are permitted as a matter of course.[15]

The contrast to a rigid route pattern is an entirely free route structure with the complete freedom to chose routes between the contracting states. Such types of agreements are very rare.

Other more restricted, but common and useful type of systems are the flexible and semi-flexible route structures. An agreement with a flexible route structure usually mentions a continent, a country or a group of countries where traffic rights can be granted. The route in question usually should «constitute a reasonable direct line out from and back to the homeland of the state whose nationality the aircraft posses» as it is expressed in the International Air Transport Agreement.

In an agreement with a semi-flexible route structure, there is a number of predeterminated points which the operator may chose between. Bermuda I introduced this formula, and it is expressed with the sentence «any one or more of the following». The carrier must give notice to the other state about any change.[16]

Airlines are only interested in flying between points that generate a lot of traffic, i.e. the big cities. This makes it important for the airlines to be granted traffic rights to such cities.

There has been a longstanding dispute between Europe and the U.S. over the sixth freedom issue.

Since there are so many independent states in Europe, it is easy for the European carriers to exercise sixth freedom

traffic rights to and from the U.S. For example, Air France brings traffic from FRG to France and from France to the U.S., which takes traffic away from the FRG and the U.S. market. The U.S. might then retaliate by not granting the right to Air France to fly to New York but, e.g. to Washington instead, which would not have the same value to Air France. From the European carriers point of view, the U.S. carriers have access to a larger market, namely the whole U.S. and thus, the European carriers want to equate Europe with the U.S. Otherwise, U.S. carriers can carry third and fourth freedom traffic from a point in the U.S. to all of the European countries, while the European carries would only have access to a limited number of points in the U.S. from their home country. The U.S. can create a large hub on the east coast and then let American carriers take the passengers to their final destination in the U.S.

This «port-of-entry» philosophy was not accepted by Europe. If U.S. carriers had access to the whole European market, European airlines wanted the possibility to operate to the whole U.S. market.

The solution is, as usual, somewhere in between. The U.S. must grant, as they do, rights to foreign carriers to fly to some of the bigger cities in the U.S.[17]

As for the sixth freedom issue, a widespread solution might be that the passengers must make a stop-over at least 12 hours, for to be considered third and fourth freedom traffic and not sixth freedom traffic.

2.4 Pattern of Air Services

The aim of each signatory is to obtain the right to participate in scheduled traffic and achieve the greatest possible advantage in the network of international routes. For to achieve this aim there must be room for fifth freedom traffic.

If traffic on a route is only carried between two points, the service is called a terminating service. Technical and other non-traffic stops are irrelevant. The traffic streams are then only third and fourth freedom traffic, although there may also be sixth freedom traffic rights involved. To give room for fifth freedom traffic, the parties have to agree on a terminating service with intermediate points located in other states.

When beyond rights are granted on a through service there is also created a fifth freedom traffic stream, namely traffic carried from the territory of the other party by the airline of the first party to points beyond.

At first, the U.S. regarded itself as a terminating point and did not grant any beyond rights for foreign carriers. With the introduction of long-haul jets, foreign operators were granted rights beyond the U.S.[18]

If both states are parties to the International Transit Agreement, the carrier should not be restricted in extending its route to a point beyond, so long as no traffic rights are

exercised and so long as there is no prohibition in the bilateral[19] agreement. If the same through service is operated by the carrier from the granting state it is called a preternational service or sixth freedom traffic. This is generally considered as a special benefit but it should be seen as a result of geographic characteristics and technical and economical needs of air transport according to Escalada.[20]

A very rare kind of traffic stream is the extra national service, or the seventh freedom, where the airline operates totally outside its home state without even using it as an intermediate point.[21]

To sum up the different kinds of traffic streams corresponding to the pattern of bilaterally agreed routes, Cheng classifies five main groups of traffic streams:[22]

1) Total Route Traffic: includes all the traffic and is the sum of all the different traffic streams listed below;

2) Inter Parts Traffic: is a stream only between the two contracting parties in terminating services, i.e. third and fourth freedom traffic;

3) National Traffic: consists of all traffic between the two contracting states, not only third and fourth freedom traffic. It can be subdivided into:

   a) inter partes traffic as specified above;
   b) anterior national third country traffic, which is traffic between the flag state and anterior points in a third state, i.e. sixth freedom traffic;

c) intermediate point national third country traffic: traffic from flag state via intermediate points in third state, i.e. fifth freedom traffic;
d) beyond point national third country traffic: traffic beyond the grantor state, i.e. fifth freedom traffic;

National traffic is the principle of a state's «own» traffic being essentially third freedom traffic, but extended to fourth, fifth and sixth freedom traffic due to the structure of the international route network and the fact that traffic rights are exchanged between states of unequal traffic volume and geographical position. The principle benefits countries that generate a large volume of traffic. But it is contrary to Bermuda I principles and can not be regarded as a principle of international law. It is also difficult to apply in practice to international air services while it offers possibilities to the public of going everywhere in the world at many different kind of tariffs.[23]

4) Grantors Traffic: The grantors traffic consists of all traffic goint to, from and through the grantor state. Thus, there are so many types of grantors traffic as there are freedoms of the air, including cabotage;

5) Third Country Traffic: will be offered whenever a route pattern includes anterior, intermediate or beyond points in third states. Third country traffic can be subdivided into three categories:

a) national third country traffic which is traffic between the flag state and third states that are anterior, intermediate or beyond points;
b) extra partes third country traffic is traffic between any of the third countries on an agreed route. This traffic does neither originate nor is destined for either of the contracting states;
c) fifth freedom third country traffic consists of all traffic between the other contracting state and third countries on an agreed route. This is the core of the bilaterals and contains three types of traffic: (i) anterior point; (ii) intermediate point; (iii) beyond point fifth freedom traffic.

CHAPTER 2: FOOTNOTES

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21. Cheng, pp. 399-403.

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CHAPTER 3: TARIFFS

A public utility is, in the interest of the public, often regulated by governmental authorities. A well functioning transport system is vital for the development of the society. Without air transport, the economic and social activities would suffer great harm, and that is why air transport is regarded as a quasi public utility.[1] Why then is air transport not regarded as a complete public utility?

A public utility is under the obligation to provide reasonable adequate and stable services to all who apply. It falls within the class of industries whose services form a «common necessity» for the public. The services like gas, water, electricity are usually provided totally by the government and excluded from market forces.

Air transportation is performed by private, partly private and governmental owned companies that have to compete with other airlines. Nevertheless, airline activities are controlled by governments through different kind of regulations due to the public's interest in a regular and cheap air transportation and assured uniformity and equality in treatment.

The general economic argument in favour of controlling airline fares and rates is on one hand to protect the public against abuse from the airlines due to thier protected position under a system of controlled entry, and on the other hand, to ensure the long-term economic stability of the airline industry by preventing cut-throat price wars.[2] International tariffs

are controlled through bilaterals between states. The expression «tariff» does not only mean price of the ticket. It also includes all conditions and provisions that affect passenger fares, routing guides, rating and charges.[3]

There are international attempts to unify the establishments of tariffs.

In 1967 ICAO worked out the «International Agreement on the Procedure for the Establishment of Tariffs for Scheduled Air Services».[4] It applies when there is no bilateral between two states or if the bilateral does not contain a tariff clause, see art. 1.a.i,ii.

The definition of «tariff» is expressed in art. 2.1:

> «the prices to be paid for the carriage of passengers baggage and freight and the conditions under which those prices apply, including pricing and conditions for agency and other auxiliary services, but excluding renumeration or conditions for the carriage of mail.»

The agreement is a codification of existing articles used in most of the present bilaterals.

Another result of ICAO activities is the adoption by the ICAO Council of a «Standard Bilateral Tariff Clause». The Clause is used to guide member states when concluding bilaterals. The Clause resembles the Tariff Agreement, e.g. the definition of «tariff» is practically the same. There are important differences.

First, the Clause is drafted in a way to include non-scheduled traffic and second, there is no explicit reference to IATA, but rather an implicit one.

The ECAC's achievement in the tariff area is the establishment of «The International Agreement on the Procedure for the Establishment of Tariffs for Scheduled Air Services» 1967, and also a Memorandum of Understanding 1982, between some ECAC states and the U.S.A. about tariffs over the North Atlantic. I will refer to these two agreements in Chapter 5.

3.1 Governing Principles in Tariff Negotiations

Cheng enumerates four factors of governing principles in the bilateral tariff negotiations:[6]

1) Economic operation;
2) Reasonable profit;
3) Characteristics of service;
4) Tariffs charged by any other operator on the same route.

Bermuda I was first to establish that tariffs shall be connected with the cost of operation, reasonable profit and with the tariffs of other airlines on the same routes. In other words, the prices must not be too high to turn away passengers. The result would be that the airlines go bankrupt or have to rely on governmental subsidies, which ultimately means that the taxpayers have to pay. Furthermore, even if air transport can be regarded as a quasi public utility, it is only a small proportion of the taxpayers who use aviation.

The prices can not be too low, since the airlines must show a reasonable profit for two reasons; the airline must be able to invest for the future and also continue to attract private investors to those airlines that are private or partly private owned.[7]

The rates must be the cheapest consistent with sound economic principles.[8]

To decide the actual level of the prices is a very difficult problem and there exist many different opinions. I will deal with this question later in this chapter.

Bilaterals provide a procedure for the establishment of the tariffs which, in general, can be divided into three phases:[9]

1) agreement between the airlines;

2) consultation between other airlines on the same route in seeking the agreement;

3) approval by the contracting states.

The agreements contain, with some exceptions, provisions that the rate fixing between the airlines shall be exercised in accordance with thie IATA rate fixing machinery - the so-called «Bermuda rate clause».[10] The references to IATA can be expressly mentioned, impliedly mentioned or not mentioned at all. In the cases where IATA is mentioned expressly, the use of its machinery is, nevertheless, not mandatory[11] for several reasons.

First, the contracting states may not be members of ICAO and hence the airline can not be a member of IATA. This is a

highly unlikely reason though, since practically all states in the world are members of ICAO.

Second, an airline of a contracting state may not wish to be a member of IATA.

Third, IATA may not have reached a tariff agreement.

Fourth, IATA's machinery may not for some other reason be available.[12]

When IATA is impliedly mentioned, it is referred to with wordings like «an association of air carriers» or «an international air transport association» when both carriers are members of IATA. When only one carrier is member of IATA, wordings like «such tariffs shall not differ from those valid and internationally enforced on the same route» or «tariffs shall be fixed by the usual procedures adopted by airlines» are used. Other examples of phrases are: «in accordance with usual practice in the international air services»[13] or reference to the «usual procedures adopted».[14]

Nevertheless, there is no doubt that there is a reference to the IATA rate fixing machinery in all cases.

Parties to an agreement that does not refer to IATA at all, usually fix rates in accordance with the IATA resolutions anyway.

3.2 The Government Role in Tariff Agreements

All tariff agreements are subject to governmental approval. The procedures preceding approval can take different forms.

If the airlines do not agree, the matter is taken up for negotiations between the governments involved or the aeronautical authorities.

In the negotiations there are three different ways of establishing a new tariff. The agreement can contain a:

1) double disapproval clause as in the U.S.-Belgium[15] Air Transport Agreement - ATA;

2) double approval clause as in the Bermuda II ATA;

3) country-of-origin approval clause as in the U.S.-New Zealand[16] ATA.

In recent years, steps have been taken to move away from multilateral - i.e. IATA resolutions on tariffs.

Bermuda II was the starting point with an innovative individual tariff proposal[17] and a double approval clause. The tariff is here subject to airline approval and if not agreement can be reached between them there must be an approval from both the governments concerned. If one of them disapproves of the new tariff proposed, the old tariff applies. Each state has thus a veto.

A much more liberal clause is the double disapproval clause where both parties must disapprove a new tariff, for it not to be applied.

Furthermore, the liberal U.S.-Belgium ATA does not contain any arbitration clause, so the only thing the disapproving state can do if denied to confer about its will, is to terminate the whole agreement.

The clause gives the opportunity for an airline to take a dominant position on a route and be a price leader. This type of agreement will undoubtly only be signed between states with equally strong airlines. A dominant position on a route by one airline could have negative consequences for the consumers, since the price leading airline can charge too high prices due to its dominant position. Prices can also be artificially low due to subsidies from the government. In short, the double disapproval clause gives the airlines the opportunity to set the prices they want and thereby have price wars.

Whether an unrestricted price war is good for consumers in the long run is disputed. I will refer to this problem later, so I will only mention that most authors - at least the European - doubt that tariffs established entirely according to market forces are good in the long run for the consumers.

Another bilateral agreement with a liberal tariff clause is the U.S.-Netherlands ATA. It introduces a concept of «rules of origin pricing». This «country-of-origin» clause removes the requirement for approval of tariffs from the state of destination.[18] It is a little more restrictive than the double disapproval clause though, since the tariff must be approved by a specific state, the country of origin, while under an agreement with a double disapproval clause, any one of the two states can approve the new tariff.

The concept was extended even further in the U.S.-Israel[19] ATA where the tariff clause removes the requirement of approval

from any of the two governments.

Government action is only provided in the event of mutual disapproval.[20] However, the U.S. have lately - with their agreement with New Zealand - changed their policy to a more restrictive view and stopped the «perfect market approach». The U.S.-New Zealand agreement is different from earlier agreements with «country-of-origin» clauses.

This agreement establishes criteria for setting of prices. Prices are to be cost based. This is a reversion to the Bermuda II agreement.

Under the country-of-origin policy each party establishes the fare for outbound traffic. This includes both one way and round trip journey originating in a country.

The prices set by the outbound country can be matched by the other party, and on fifth freedom routes, all the third carriers are entitled to match the country of origin's fare, provided they allow the contracting parties to match the fares in their home market.

The fault with this provision is that there can be differences in frequency of traffic. If that is so, an airline can then have a higher price, but more traffic attracted by the better service which results in the customers chosing that airline. The prices can also be set in many different ways.[21]

3.3 Time Limits

Time limits are usually specified for filing of tariffs. Usually the new tariff or any other change of fares must be filed with the authorities 30-45 days before it can come into force.

In country-of-origin agreements the tariff proposal has to be filed for approval with the country-of-origin. In the case of double disapproval it has to be filed with the aviation authorities of each contracting party and if both parties are dissatisfied with the tariff they must negotiate. Likewise in the case of double approval agreements the proposals must be filed with both parties. In the case of double disapproval agreements if the parties cannot agree, the disputed tariff comes into force. In the case of double approval agreements, usually if a party disapproves of the new tariff proposal, the existing tariff will continue to apply.

3.4 Enforcement of Tariffs

ICAO made in 1980 a survey about the state practice in enforcement of tariffs.[22] The result of the survey indicated that tariff enforcement has been actively pursued in a large number of states. The enforcement has taken form of government involvement in the airlines or extended authority for civil aviation authorities. This enforcement and control machinery is generally not referred to in the agreements.[23]

The survey shows an apparent trend towards an ever increasing governmental control over the international civil air transport business. Violations of the tariffs have declined due to the fact that the bilateral agreements have lately given the airlines possibility to introduce innovative tariffs which have enabled them to respond better to market needs without having to violate approved tariffs.

As regards the tariff enforcement activity of IATA, some significant developments have taken place in recent years. The proliferation of IATA fares, the increased complexity of rules and regulations associated with these fares, and the increased incidence of open rates situations made it necessary for IATA to review its approach on tariff enforcement among its member airlines. IATA now emphasizes preventive actions rather than punitive measures.[24]

3.5 The Actual Price Level

The previous part explained the procedure for setting the tariffs. A far more difficult problem is to decide the level of the tariffs, i.e. the price the passengers shall pay.

There is a vast number of opinions about pricing and the reasons for the present poor state of the airline industry and also opinions about how to solve this problem. I will give a brief survey of the core of the problem, since price policy is a separate science.

The goal of the airline industry is to provide as good transport facilities as possible to as many people as possible.

Like Escalada, we must define the problem as economic and the appropriate mechanism to deal with the matter is IATA. Assuming aviation to be a quasi public utility, Escalada believes that states have the right and duty to intervene in this problem.[25]

For consumers low prices are the best form of fares. However, cut throat price competition is not suitable. Reduction in fares is justified only if it will increase traffic and the reduction will not jeopardize the operation of the carrier.

It must be noted that a price reduction combined with a reduced service is not a true price reduction.[26] An example of this is the Laker Skytrain service. Compared to consumer prices in the last decades, fare levels have declined substantially. However, costs have also increased substantially, due to the oil crises.[27] At present about 45% of the airline expenditures is referrable to gasoline. Hence, the operating profits are down. These circumstances have to be taken into account when prices are decided upon.

Since tariffs are set, with very few exceptions, through IATA's rate fixing machinery and, therefore, are similar all over the world, an airline has to attract customers by offering a better service than other airlines. This benefits the public for it gets better service, but the catch is that it is

difficult for the airlines to differentiate between themselves in the long run. Short term advantages can be gained, as for instance was the case with the introduction of jet planes, which were of a great advantage to the airlines that first introduced them.

Nevertheless, the only way for an airline to differ from the others is to try to improve service through wasteful competition; wasteful because a product differentiation of this type costs a lot of money, and often the aggregate increase in traffic, resulting from the product differentiation is less than which would have resulted from the application of the same amount of money to fare reductions.

For example, a 15% of all expenditures on product differentiation activities must result in additional traffic than would result from a 15% reduction in fares. Furthermore, the passenger market is an elastic one, and passenger traffic is very sensitive to price changes, even if the traffic does not respond to price changes under special circumstances such as high income growth.[28] The solution to wasteful competition would be a standardization of service and a threat of return to price competition.[29]

Starting with Bermuda II, states have taken unilaterally actions concerning tariffs. This is especially true with the U.S. As mentioned above, Bermuda II commenced with the adoption of innovative individual tariff proposals which were the result not of multilateral negotiations of fares and rates but were agreed bilaterally.

These actions are totally outside the international framework and there can perhaps be short-term advantages for the specific country taking the action, but in the long-run, international aviation will suffer from these activities.

The type of traffic that has been most affected by this new concept is charter traffic. Charter traffic - or non-scheduled traffic - is not included in bilaterals, but generally left to unilateral regulation. It is even so in Europe despite the 1956 Paris Convention on non-scheduled traffic[30] which is dealt with in Chapter 5.

A new type of charter traffic that has emerged lately (prorata programmed charter services), has made the concepts of scheduled and non-scheduled traffic vanish. The charter traffic steadily increased over the North Atlantic until 1977, thereafter, the share declined but it may now be recovering.[31]

Without a base for the tariff structure, bilaterals for non-scheduled traffic have been increasingly difficult to achieve.[32] Hammarskjold argues consequently for a system where bilaterals cover all international air traffic.[33] First, the system is flexible in itself. The agreements allow for small ad hoc adjustments.

Second, the IATA Traffic Conference system has the function of a linking element. It has provided a multilateral fare mechanism to balance the needs and aspirations of bilateral partners.[34]

CHAPTER 3: FOOTNOTES

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CHAPTER 4: CAPACITY

In creating an aviation industry, nations are caught between two poles:[1]

1) promoting the economy by expanding the network of air services for the benefit of the public; and

2) protect their flag carriers so that they will get a fair opportunity to compete for business.

It is difficult to achieve these two goals with the same course of action. Practically all countries have emphasized the second notion.[2]

Many reasons have been advanced for a state having its own national operator, other than it is required for the benefit of the travelling public, irrespective of whether it is governmentally or privately owned. Without a well functioning net of transport, a nation can not develop economically. Therefore, a communication system is important as a public utility.

However, air transport can not be regarded as a public utility since it does not have a natural monopoly, but it is an industry of real public importance and that is why many governments have treated the industry as if it is a true public utility.[3]

A public utility - a quasi public utility is a better description of air transport - must function and exist whether it is profitable or not. This means that the government has to subsidize the system or control it or both if it is having losses.

Due to these reasons, airlines are not always run on a strict commercial basis. There is no problem when there is only one airline operating on domestic routes. But when the protected airline starts operating abroad, problems arise in implementing such a policy because in international air transport a state does not have the complete control that it has in relation to domestic air transport.

To foster and promote its objectives, it has, within the framework of the treaties which it makes, to negotiate appropriate terms. The terms the state seeks to negotiate reflect its conception of the role of air transport. Thus, one can have diametrically opposed policies on capacity regulation.

4.1 Capacity Clauses in Bilateral Agreements

States which take a rigid position must assure themselves of a sufficient share of traffic in the bilateral negotiations. This leads us to the important capacity clauses in bilateral agreements.

States are in different positions when negotiationg capacity with regard to geographic position.[4] Further, some states, like the U.S. generate a lot more traffic than others. The advantage of this for them is that they can demand a large portion of the traffic as the U.S. does over the North Atlantic and Japan over the Pacific.[5] Other states with the advantage of a favourable geographic position like Belgium can use it

for connecting traffic from different parts of the world, i.e. sixth freedom traffic.

One view is that countries that generate a small amount of traffic ought to be liberal in granting traffic rights since they have nothing to give in return and thus nothing to lose.[6]

Whatever their position is, most of the states are for different reasons in favour of strict regulation of capacity. Only the U.S. has, until recently, been in favour of non-regulation of capacity but instead has desired free competition for the benefit of the public and the U.S. while it had the carriers best suited to benefit from free competition.

A compromise between these two standpoints was made with the first Bermuda agreement signed by the U.S. and the U.K. in 1946, where the U.K. stood for the rigid position with strict regulation of capacity fares and routes, while the U.S. wanted total freedom in all areas. In general, the U.K. had to abandon their demand for predetermination of capacity and the U.S. had to agree to tariff control by the governments and IATA.

4.2 Predetermination

The U.K.'s view in the Bermuda I negotiations was that a sort of formula had to be worked out which would control capacity and frequency of operation of any airline.[7] The normal formula would be a 50/50 split of the traffic between carriers

from the contracting parties. There must be room for a certain flexibility though, since a state can temporarily be unable to take care of his share of the traffic. The other carrier must in that case have the possibility to provide this service to the public.[8]

The Latin American countries have supported this view of predetermination and strict control of traffic. It was advanced by E.A. Ferreira in 1946 and was called the «Ferreira doctrine».

The fundamental thought behind this is that each country «owns» the traffic that originated in or is destined to its territory, whatever the nationality of the passengers. The contracting parties are, therefore, entitled to share this traffic[9] on a 50/50 basis, regardless which of the two states originates most of the traffic. The fact that a person is travelling from one nation to another, gives equal importance to both nations. It does not necessarily have to be a strict equal split of capacity. There can be room for some competition if the amount of traffic permits it.[10]

The above discussion is applicable to third and fourth freedom traffic.

The Ferreira doctrine gives hardly any recognition to or entitlement for fifth freedom traffic. This traffic will only be allowed when third and fourth freedom traffic flows are insufficient to meet the traffic demand on the route in question.

Wassenbergh opposes the doctrine that each state «owns» its traffic, and argues that a market is not a static phenomenon referable to a specific state and controlled by that state. The market is practically all the worlds traffic.[11] A person travelling from Asia via Europe and Brazil to the U.S.A. is not solely a part of Brazil's market when he passes through Rio de Janeiro, but a part of the market consisting of the traffic between - in this case Asia, Europe, South America and the U.S.A.

The Ferreira principle is basically mercantalist and eliminates all competition between airlines and thus provides a strong incentive to them to abolish all competition and establish a sort of commercial pooling agreement.[12]

In recent years there have been a decline in passenger traffic, so there is an excess of capacity with wasteful use of resources. The aim of the Bermuda II ATA was to prevent this waste by regulating capacity but also avoiding predetermination.[13]

4.3 Ex Post Facto Review

The U.S. had the complete opposite position in their aviation policy. They wanted freedom for the airlines to compete for the traffic. Predetermination is contrary to liberal development of international air transport and an ex post facto review usually provides an adequate safeguard.[14] Ex post facto review of capacity was first introduced with

Bermuda I ATA. Under agreements containing this principle the airlines are given the possibility of free competition in the provision of capacity for third and fourth freedom traffic with adjustments made afterwards if there is to big a difference in the traffic carried by the airlines involved.[15]

An airline's operation must not affect unduly the services of the other airline on the same route. This concept is mentioned in provision no. 5 in the Final Act of the Bermuda I ATA.

The ex post facto position implies that there must be a close relationship between the capacity provided and the requirements for transportation.[16] The purpose of this provision - which in Bermuda I is stated in Clause 3 of the Final Act - is to prevent a carrier from operating at unnecessarily low load factors to the detriment of the other airlines serving the route.[17] The meaning of this concept is that the operator shall provide about the same amount of capacity as there is travelling public. It is not possible for an operator to always have a load factor of 100%. He would then have to turn away prospective passengers.[18]

The U.S. did not wish to gear capacity too closely to immediate demands, since it would not give any room for competition, better service and traffic development.[19] A load factor of about 65-70% would, therefore, be appropriate.

A problem with the ex post facto review concept is that it is only suitable for countries with equally strong airlines.

A weak airline can not get as much traffic as a strong airline by competing with it so the weaker airline has to ensure for itself a sufficient amount of traffic in another way.

In the review of the traffic carried by the two airlines, the airline with the lowest amount of traffic carried, can insist that the other airline reduce its share of the traffic in the future. Hence, the weaker airline will set the amount of traffic at a level where it is able itself to handle the traffic volume. The stronger airline has to lower its capacity with the result that the total capacity offered on the route is lower than the demand. The weaker airline must, therefore, accept its inferior place in the competition in order to give the travelling public what they need.[20]

4.4 Definition of Capacity

A very small number of bilaterals concluded contain a definition of capacity. It seems, therefore, not necessary to define it, but for the sake of clarification, the most common definition of capacity is:

> «The term 'capacity' in relation to an aircraft means the payload of that aircraft avialable on the route or section of a route.»
>
> «The term 'capacity' in relation to a specified air service means the capacity of the aircraft used on such service, multiplied by the frequency operated by such aircraft over a given period and route or section of a route.»

This definition is, for example, used in the bilateral ATA's between Belgium-Pakistan and Afghanistan-Pakistan.[21]

4.5 Traffic Measure

When deciding upon capacity, the question arises what kind of traffic should be measured. Is the capacity supposed to be measured only on traffic following between the contracting parties or shall it be measured on the total amount of traffic that passes through each of the states, or in some other way?

Often, the decision is made on the basis of a mixture of the different traffic flows, but some types of traffic are considered more important than others. These types are included in the primary capacity criterion, which in most cases is third and fourth freedom traffic.[22] There are three types of traffic flows included in the primary capacity criterion.[23]

1) Total route traffic;
2) Inter-partes traffic;
3) National traffic.

Total route traffic includes all traffic on a given route. Hence, it is the most liberal criterion since capacity entitlement will be related to all traffic.

Traffic between the contracting states in a direct terminating service constitutes inter-partes traffic. This is the most restrictive criterion and omits all the other types of traffic.[24]

The most common criterion is the national traffic concept, which was first introduced in Bermuda I Clause 6 of the Final Act. It denotes traffic to or from the flag state of the carrier.

In Clause no. 6 of Bermuda I, the criterion is formulated as -/«traffic demands between the country of which such air carrier is a national and the country of ultimate destination of the traffic». Capacity is thus related to all traffic that is coming out from or going to the state of the carrier. Only a few bilaterals have other kinds of traffic as primary capacity criterion. When the primary capacity criterion contains inter partes and national traffic, there are usually provisions about how to divide the rest of the traffic not included in the primary capacity criterion, i.e. third country traffic. But not national third country traffic which already is included in the primary capacity criterion. The provisions about third country traffic are included in the so-called supplementary capacity criterion and consists mostly of fifth freedom traffic.[25]

The different kinds of traffic that are included in the supplementary criterion are fifth freedom third country traffic and extra partes third country traffic.[26]

In Bermuda I ATA, the supplementary criterion is stated as follows in Clause 6 of the Final Act:

> «The right to embark or disembark on such services international traffic destined for and coming from third countries at a point or points on the routes specified in the Annex to the Agreement shall be applied in accordance with the general principles of orderly development to which both governments subscribe and shall be subject to the general principle that capacity should be related:

a) to traffic requirements between the country of origin and countries of destination;

b) to the requirements of through airline operation; and

c) to the traffic requirements of the area through which the airline passes after taking account of local and regional services.»

It is thus third country traffic and it is clearly specified to what the capacity should be related to in sub-paragraphs a-c.

The variations of the supplementary criterion are more numerous than the primary criterion and sometimes the supplementary criterion is omitted completely in restricted bilaterals.

4.6 Fair and Equal Opportunity

In constrast to predetermination of capacity, Bermuda I introduced a regime of controlled competition. Airlines of the contracting parties have now a «fair and equal opportunity» to operate on any route between the territories of the contracting parties, clause no. 4 of the Final Act. The purpose of the paragraph was to ensure that each nation had the right to offer the services within the limits set out in the agreement.[27]

The concept of fair and equal opportunity can only be applied on routes where there actually is competition. If one of the carriers does not want to fully use its opportunities to operate in the market, it will not be able to restrict the operation of the other carrier in an ex post facto review.[28]

Critical voices mean that the weaker airline will be out of business unless there is a handicap placed on the stronger one.[29] But one must emphasize the expression «opportunity to operate». The weaker airline still has the same right and possibility to operate. Furthermore, Clause no. 5 in Bermuda I sets a limit on permissible competition. Both carriers shall take the interest of the other carrier into consideration so as not to affect unduly the services of the latter on the same route. The purpose of this Clause is to give protection against unfair trade practices.[30]

The problem of how free the competition is supposed to be is solved with the conclusion that both carriers shall have a fair chance to show the public what kind of service they have, but purely destructive cut-throat competition in the sense of striving for monopoly is not allowed.[31] The Clause revives the old slogan «live and let live».

Another problem is to decide whether in fact there is a fair and equal opportunity to operate.

A liberal reading of the concept implies that one carrier is allowed to fly all routes flown by the other carrier, but such an interpretation would clearly be inconsistent with the grant of specific routes.[32] The U.S. interprets equal opportunity to operate by putting the opportunities on a level with the benefits derived from them. Also Prof. M. Bradley argues that actual and potential revenues might be factors that determine balance.[33]

However, different revenues can depend on other factors, such as bad management or not enough resources. Hence, an equal opportunity is not always an equal benefit. Wassenbergh, therefore, suggests that equal opportunity should be interpreted as meaning equal access in practice to the market. Whether for reasons mentioned above, the airlines make use of their opportunity or not, is up to them.[34]

CHAPTER 4: FOOTNOTES

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3. S. Wheatcroft, ibid, p. 46 f; see also beginning of Chapter 3.
4. Stoeffel, p. 265.
5. AWST Aug. 23, 1976, p. 24.
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21. ICAO Circ 72-AT/9 Montreal 1965.

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25. Martono, p. 152.

26. Cheng, p. 406 ff.

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28. Wassenbergh, Air Law in a New Era, p. 41.

29. J. McCarroll from JALC 1963, p. 119.

30. G. Baker, ibid, p. 254.

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32. J. McCarroll, ibid, p. 118.

33. Report to ICC Doc. 310/223 24/4/1968.

CHAPTER 5: ECAC

After World War II there followed fast technical development in the western world. Combined with prestige, national defence and economic growth it paved the way for the development of civil aviation in Europe.

There existed many other factors typical for Europe which restricted the development of international aviation in Europe.

The European continent consists of many small or intermediate nations, all of them having the desire to exercise the concept of «complete and exclusive sovereignty» over their territories. This hampered international civil aviation in Europe. Domestic aviation played a minor role due to their geography.

The sovereignty doctrine had the consequence that fifth freedom traffic rights were very difficult to obtain, with the result that the operators had to depend on the third and fourth freedom traffic. Hence, a constant overlapping of services and wasteful competition resulted.[1] Every country wanted its own airline to have as much traffic as possible.[2]

Goedhuis analysed the above mentioned political reasons and the question why aviation was to be considered as an instrument of national policy and why non-economic considerations govern the formation of aviation policy.

Aviation in its political and strategic aspects can not be considered independently from general international relations.

Between the two world wars, there was growth of general economic nationalism which affected the development of aviation so that it became a restricted and controlled industry in practically all European countries.[3] When examining the aviation development in Europe, a natural thing is to compare it with the situation in the U.S. The most significant reason for the different evolution in aviation on these two continents, is that the U.S. is only one country with one big market, while Europe consists of many countries each having an insufficient market to develop a large airline.

The large number of countries implies a multitude of formalities, procedures and permits of economic, legal and monetary nature,[4] e.g. immigration and custom rules and competition in the aircraft industry etc.[5] In the U.S. it is generally considered that a route of less than 500km is uneconomic.[6]

In Europe not only are the distances very small in general, but furthermore, the market is concentrated between Glasgow, Barcelona, Milano and Stockholm. The shorter the routes are, the higher are the costs due to more engine wear, fuel consumption in take-off and landing and waste of aircraft utilization etc.[7]

Further, establishment expenses are high in proportion to revenue. In view of this high establishment expense, it is difficult to set suitable prices especially for short-range

travel, owing to the little gain in time this kind of travel provides. The prices must be fairly low to give the public an incentive to travel by air instead of using another mode of transport.

Europe has also an excellent system of subsidized railways which compete to a high degree with aviation. The inconsiderable gain in time forces the airlines to have a high frequency of services and, therefore, use smaller aircrafts, which has a negative effect on the ton/km production compared to bigger aircraft.[8] The labour market is also different from the U.S. where salaries can be cut and people laid-off if an airline is showing poor results.

Airlines in Europe have much higher labour costs, and there is an overall common European policy, partly due to strong labour organizations, to see to the well-being of the employees as well as the travelling public. The states and airlines in Europe have felt that the solution to these problems in European aviation industry is co-operation on both governmental and airline level, motivated by economic considerations often stimulated by political reasons.[9]

So, as early as 1951, these matters were discussed in the Council of Europe and three plans were submitted.

Firstly, the Sforza Plan envisaged a complete unification of all European aviation activities, with one single European air medium and a supra national air transport authority.

Secondly, the Bonnefous Plan argued the same way and advocated an aviation authority with supra national powers, and one single European airline.[10]

These two plans envisaged a neofunctionalist approach and since the functionalists were in majority in the Council, the plan found little support. The functionalists promoted co-operative solutions within a «sector-by-sector» approach and further rejected «supra national solutions».[11]

The third proposal, the van der Kieft Plan found more support since it was more pragmatic. It advocated the formation of a European airline consortium and the convocation of an intergovernmental conference on air transport in Europe.[12] Even if this plan did not find full support it was the only one that provided a basis for action.[13] The Consultative Assembly of the Council of Europe recommended to the Committee of Ministers[14] an association of airline companies in Europe and a conference of governmental experts or other methods of improving coordination in this field.

After two years of discussion, the Committee of Ministers agreed to recommend such a conference, with the reservation that ICAO should convene the conference, which it did.[15] As a result, the «Conference on Coordination of Air Transport in Europe» - CATE - was convened, upon invitation of ICAO in Strasbourg in 1954.

A number of resolutions were adopted concerning the facilitation of European air transport. CATE's most important

recommendation envisaged a European Civil Aviation Conference should only be advisory, since the European states were not willing to leave the decisions regarding air routes through their territories to an international body.[17]

Their solution accorded exactly to the functionalist scheme; only a forum for co-operation was created without the states giving up any part of their sovereignty in air transport matters.[18]

The European Civil Aviation Conference held its first meeting in the fall of 1955 and the first problem it had to solve was the constitution and status of ECAC.[19] As for its relationship with ICAO it was decided that ECAC should neither be subordinate to a regional body of ICAO, nor completely independent, but have an intermediate status.[20]

An international organization has the legal status and powers given to it by its constitutive instrument. ECAC's constitutive instruments is the «Constitution of the European Civil Aviation Conference» revised and changed in 1968. The legal status and powers are expressed in the first resolution and the decisions adopted at ECAC's sixth session 1967. Article 1 of the Constitution reads in part as follows:

> §1 The objects of the European Civil Aviation Conference shall be to
>
> a) review generally the development of European air transport in order to promote the coordination, the better utilization and the orderly development of such air transport; and

b) consider any special problem that may arise in this field.

§3 The function of the Conference shall be consultative and its resolutions, recommendations or other conclusions shall be subject to the approval of governments.

The Constitution shows clearly a tendency to make ECAC more than a periodical forum, but a permanent, well-structured organization. It is further clarified in Art. 4 where permanent bodies are set up, such as the Directors General of Civil Aviation, which is a kind of Council of ECAC.

Moreover, in certain limited aspects, ECAC has acquired considerable influence and even quasi obligatory recommendatory powers, mainly in the field of non-scheduled traffic over the North Atlantic. The work in this field is done by the Economic II committee.[21]

It was feared in the beginning that ECAC would duplicate the work and tasks of ICAO and become a European ICAO. The Chicago Convention permits the contracting states to enter into any arrangement not inconsistent with the Convention, Art. 83. Since there has been no protests from ICAO, and ECAC has continued to exist, we must assume that ECAC is not inconsistent with the Chicago Convention. Verploeg argues, however, that some rules in the Chicago Convention with its annexes are not consistent with ECAC activities.[22] Verploeg's view is that ECAC is not in compliance with the international rules set forth in the Chicago Convention, but «rather is a result of failure of the Chicago Conference to establish world order in aviation».

The possibility of conflicts between actions taken by ECAC and actions of other bodies of civil aviation have increased. As the number of treaties concerning and affecting international aviation increase, so does the possibility of conflicts.[23]

An important treaty, for European aviation, is the «Treaty establishing the European Economic Community», the Rome Treaty signed and ratified in Rome 1957.[24] The purpose of the treaty is to promote, throughout the community, a harmonious development of economic activities, a continuous and balanced expansion, by establishing a common market and unifying the economic policies of the member states, Art. 2. Whether this general policy includes air transport as well, has been disputed for a long time. The only paragraph that gives some guidance is the ambiguous Art. 84 of the EECT:

> 1) The provisions of this title (IV) shall apply to transport by rail, road and inland waterway; and
>
> 2) The Council may, acting unanimously, decide whether to what extent, and by what procedure appropriate provisions may be laid down for sea and air transport.

Does this article exclude maritime and air transport from the EECT? The question, being of some importance for air transport, was finally settled by the European Court of Justice 1974 in the French Seamen Case.[25] The effect of the decision was that the Treaty was applicable to sea and air transport so long as it promoted the attainment of the

EECT.[26] Problems may arise when a decision concerning aviation is taken by the Council of Ministers under Art. 84 that is incompatible with an ECAC action.

First of all, a member of the Council of Ministers who fears that a proposal is in conflict with an ECAC action, can vote against the proposal. No decision can then be reached, because the Council can only act if there is unanimity.[27] In second place where there are conflicting decisions the application of the principle of «lex specialis» may solve the problem.

The EECT is a convention that promotes economic activities in general while ECAC is a specialized organization with the purpose of facilitating European air transport. Any conflict between the two conventions should thus be solved according to the principle «Lex specialis outrule lex generalis».

If states adhere to two different treaties it could, thus, lead to legal conflicts, which e.g. is true with the respect to the rules of establishment and competition in the EECT. A strict application of the «national treatment rule» in Art. 52 EECT, creates problems for an airline in an EEC country that wants to establish itself in other EEC countries. The article will come in conflict with the «national ownership and control» clauses in bilaterals, as well as with aircraft registration provisions in the air navigation codes of member states.[28]

Since bilaterals and treaties like EECT, European Free Trade Association - EFTA, EUROCONTROL, ECAC, General Agreement on Tariffs and Trade— GATT, etc are expresssions of European

co-operation, in many areas, the potential problems will certainly have to be solved by political goodwill.

5.1 Work Done by ECAC

As mentioned above, the principal task of ECAC is to facilitate air transportation in Europe and to liberalize the granting of traffic rights among member states. The liberalization efforts have, however, been very modest especially in matters of scheduled services where there are practically no results.

The concept of «scheduled service» and how to regulate it has though been discussed a lot, starting with the CATE conference. At that conference an obstacle arose immediately. Most of the states in Northern Europe - having more developed airlines and thus seeking traffic outside their territories - favoured complete freedom, while most of the southern states - with weaker airlines - favoured a cautious approach with safeguards against excessive competition.[29]

Hence, there were many different proposals on how to regulate scheduled services. They ranged from plurilateralism, partial multilateralism and complete freedom to proposals for more restrictive development of air transport. All multilateral solutions were, however, criticized due to the danger involved of less liberalization than existed under the present bilateral system. Reference was also made to the International Air Transport Agreement which had become a dead letter.[30]

The result of the work of CATE was recommendations to the governments to co-operate in technical and administrative fields and further to exhort airlines to co-operate through, e.g. pooling.

Some conventions have, nevertheless, been agreed upon: The Multilateral Agreement Relating to Certificates of Air Worthiness for Imported Aircraft from 1960,[31] facilitating import of aircraft within Europe, and the International Agreement on the Procedure for the Establishment of Tariffs for Scheduled Air Services 1967. The latter established the administrative procedure when deciding upon the tariffs, which shall be established through IATA rate fixing machinery. In the field of scheduled services where the states could not agree on a common action, ECAC has, at present, limited its activities to merely following the existing situation.[32]

An example of this is the result of the Ninth Triennial Session of ECAC 1976, where one of the standing committees of ECAC, the Economic Committee I - ECOI - was urged to conduct an investigation of the possibility of developing an improved pattern of air services which would better satisfy the public demand on an economic basis, to «undertake a critical survey of the structure and level of air fares» and to seek promotion of co-operation between airlines to -

1) satisfy adequately public demand; and

2) reduce costs.

As a consequence of this session, ECAC formulated its main principles of future policy with respect to European scheduled air services:

1) Support for the multilateral fare - and rate fixing process provided by IATA; promotion of harmonisation of procedures among governments under the 1967 Multilateral Agreement for Establishment of Tariffs;

2) the need to ensure the economic viability of scheduled air services while safeguarding the interest of the travelling public;

3) the need to establish and maintain a closer relationship between air fares and the cost of providing air services;

4) the need for a simpler and marketable fares structure; and

5) the need for some reasonable relationship between the lowest scheduled fares and charter rates.

This policy was affirmed in the Ninth Intermediate Session 1977 where directives were given to the ECOI for its future work which can be summarized as follows:[33] the national administrators must look more to the public interest of air transport and have a more market oriented view on services and level of fares. Hence, ECAC should try to see that the public was offered adequate services at the lowest costs possible and at a reasonable rate of return for operators. In order to achieve this long-term objective, the aviation system should satisfy the requirements of -

1) an adequate air route system with adequate air services;

2) operational and economical efficiency of the airspace, airport, airline and flight safety systems; and

3) the environment.

Whether this policy will lead to more liberal aviation regulation among the different European states and an emphasis on the interest of all the travelling public will be left for the future to tell.

5.2 Memorandum of Understanding, 1982, on Tariffs

One of the latest results of ECAC's work is a Memorandum of Understanding with the U.S. concerning tariffs over the North Atlantic, signed 2 May 1982 and valid from the 1 July 1982 for a period of six months with the possibility of renewal.

The understanding mainly covers two areas: tariff scales and the authority for signatory countries to take part in multilateral tariff coordination while the arrangement is still in force.

The scales include five main fare levels: first class, business class, economy class, discount and deep discount. Every level has its price zone in which tariffs are automatically approved by the aviation authorities of the contracting states, Art. 3. Fares outside the zones will continue to be dealt with under existing bilaterals, Art. 4.

The U.S. sees the understanding as a confirmation of its fares policy, which is a key to deregulation, and the European

countries consider this approach as reflecting a measure of solidarity which is the aim of ECAC as an institution.[34]

The agreement provides that economy fares with the possibility to range 20% above or below the specified reference fare levels set forth in the agreement. The discount fares can be set 30% below the economy level and the deep discount fares are permitted down to 40% of the economy level.

The wide range of possibilities for the airlines to set fares, automatically approved by the aviation authorities in the contracting states, provide a flexibility called for in today's international market.[35] The MOU is unique in the history of international aviation. The airlines will have greater freedom to make responsible marketing decisions. Hence, the MOU provides a framework for the airlines to give more considerations to the needs of the travelling public, which will contribute to a more viable air transport system on the North Atlantic.[36]

5.3. The 1956 Paris Convention on Non-Scheduled Traffic

Article 5 of the Chicago Convention was established to facilitate non-scheduled traffic, but the second paragraph contains severe limitations. Contracting states can according to Art. 5.2 «impose such regulations, conditions or limitations as it may consider desirable». It implies that there is practically no difference between scheduled and non-scheduled traffic insofar

as prior permission for services is concerned, since the grantor state can impose any kind of rules to be followed by the foreign non-scheduled carrier.

There was a general agreement among the European states that some special measures should be taken to liberalize this form of activity in Europe. It was felt that non-scheduled services could be granted greater freedom inside Europe if such services did not compete with established scheduled services.[37]

The «Multilateral Agreement on the Commercial Rights of Non-Scheduled Air Services in Europe» Paris 1956, distinguishes between three categories of flights that do not harm scheduled traffic, Art. 2.3: those flights that by nature do not offer any real threat for scheduled traffic such as taxi flights; flights for emergency situations and flights with aircraft entirely chartered without resale of space and also isolated flights, Art. 2.1.

Article 2.2 gives the same treatment to freight transport and to transport of passengers between regions which have no reasonable direct connection by scheduled services.

Other kinds of non-scheduled traffic are subject to the restrictions that can be imposed under Art. 5 of the Chicago Convention.

The very limited type of flights in the first category and the possibility for the grantor state to impose restrictions on the second category of flights, if it deems them to affect

the scheduled traffic in the area, reduces the importance of the Agreement to a minimum.[38]

The non-scheduled traffic is entirely subject to unilateral decisions,[39] and the practice and general consent among contracting states were that they were granting permission to this kind of flights.[40] The importance of the Agreement should not be under-estimated. One of the more substantial effects of it is that there has been a considerable rise in the Inclusive Tour Charter traffic, ITC,[41] i.e. North Europeans going to the south of Europe.

It is also the first time the states sat down together since the Chicago Convention and worked out an agreement on commercial rights.[42] Furthermore, it is the first time a complete system for granting commercial rights on any basis, has been worked out rationally.

5.4 Memorandum of Understanding 1975 on Non-Scheduled Traffic

Another large achievement of ECAC in the field of non-scheduled traffic is the arrangement between ECAC and the U.S. on non-scheduled traffic over the North Atlantic.

In 1972, ECAC, the U.S. and Canada agreed on a common statement of principles, the «Ottawa Declaration». It was the first attempt to set up a regulatory regime for transatlantic charter on a multilateral basis.[43] It introduces the non-affinity concept for the North Atlantic charters. The concept was based on the advanced booking requirements, which had the

result that ABC traffic increased enormously over the North Atlantic.[44]

Further results from ECAC negotiations with Canada and the U.S. was the Memorandum of Understanding from 1975 which expressed a common policy and principles that should govern ECAC state's bilaterals with the U.S. or Canada on the subject of charter services. The policy aimed to regulate both prices and capacity in the transatlantic charter traffic. The ECAC policy is to:

1) Establish charter prices at reasonable levels, due regard being paid to all relevant factors, including:

   a) reasonable profit;
   b) seasonal variations;
   c) economically sound cost of operation;
   d) the relationship between scheduled fares and rates and charter prices;
   e) the impact on transatlantic air transportation as a whole; and
   f) the characteristics of the various categories of charter flights.

2) Adapt capacity to the need:

   a) to avoid unduly affecting scheduled services;
   b) to maintain a close relationship between charter capacity and demand, while,
   c) respecting the principle of fair and equal opportunity for the carriers of each pair of states concerned by a given traffic flow.

3) In regard of both prices and capacity, ECAC has stressed the need for periodic multilateral discussion and consultation, including exchange of traffic figures and forecasts.[45]

No multilateral agreement has though been concluded between the U.S. and ECAC concerning transatlantic charter.

The Ninth Intermediate Session 1977 introduced a «One day charter flights open to the public» which is to be used only where no harm is done to scheduled traffic and special conditions are met.

The Association of European Airlines, AEA, proposed a closer relationship between AEA and ECAC at this session.[46]

In recent years, ECAC member states have also started to adopt a common policy on intra-European scheduled services.[47]

CHAPTER 5: FOOTNOTES

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2. Dan Goedhuis, The Role of Air Transport in European Integration, JALC 1957, p. 274.
3. Supra, p. 274.
4. Matte, p. 267 and L. Weber, European Integration and Air Transport, Thesis McGill 1976, p. 23.
5. Stage, p. 11.
6. Supra, p. 32, footnote 72.
7. Supra, p. 32 For a more thorough discussion, see Chapter 7.
8. Goedhuis, ibid, p. 276.
9. Stage, p. 33 and 57 and Weber p. 37 and 53.
10. Matte, p. 267.
11. Weber, p. 46.
12. Matte, p. 267.
13. Weber, p. 49.
14. Res. 12 1951 of the Consultative Assembly of the Council of Europe, See Recommendation and Resolution of Assembly, Session 51/52, p. 48.
15. Matte, p. 268.
16. Weber, p. 52.
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18. Weber, p. 53.
19. Stage, p. 19.
20. ICAO Doc. 7676-ECAC-1 Resolution nr. 1.

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22. E.A.G. Verploeg, The Road Toward a European Common Air Market, Thesis McGill 1963, p. 155. In Verploegs opinion annex 9 is not consistent with ECAC activities.

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26. L. Weber, Die Zivilluftfahrt im Europaishen Gemeinschaftsrecht, Springet Verlag 1980, p. 373 and Weber, European Integration, pp. 124-131.

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44. Matte, p. 272.

45. For more details about the work of ECAC, see Arif Cavdar, Regionalization in International Civil Aviation, Thesis McGill pp. 62-73.

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CHAPTER 6: CO-OPERATION BETWEEN AIRLINES

At the beginning the airline industry was very individual. However, it was soon evident that there was a need for co-operation between airlines and between governments, mainly for the purpose of performing in a more efficient way in their business. Pooling was due in large part to the poor financial situation of many airlines. Todays airlines have large expenditures, especially on aircraft purchase and maintenance side. The incentive to reduce costs is, therefore, very high.

Verploeg has made a survey over the most common types of co-operation between airlines as follows:[1]

1) Common representation and maintenance. Co-operation in ticket sale, advertising, fueling, catering, etc.;
2) Coordination of schedules;
3) Hire, charter, interchange, dry and wet lease and blocked space agreements;
4) Interchange of routes;
5) Pools;
6) Consortias, like SAS; and
7) International companies

For the co-operation to work in the most efficient way it is important that the governments stay out of the business. The reason is that the most efficient way of doing business is to use the contract with its flexibility, which allows it to be changed in accordance with circumstances.[2] If the governments

are involved, there usually has to be rules and laws established which are very difficult and time consuming to change. The purpose of co-operation between airlines is to conduct business more effectively. An effective and cheap air transport system will undoubtedly also benefit the customers.

6.1 International Co-operation Between Airlines

Chapter XVI of the Chicago Convention «Joint Operating Organization and Pooled Services», expressly permits airlines to constitute joint air transport operating organizations or international operating agencies and to pool their air services on any routes or in regions, Art. 77. Pooling is, thus, legal so long it is subject to the provisions of the Chicago Convention. The Convention does not deal with the commercial aspects of air transport due to the fact that the states did not want to have a commercial multilateral air transport agreement, but left it entirely to bilateral and unilateral actions. Hence, Chapter XVI must be considered neutral towards airline pools. Thus, it does not give any guidance on whether, e.g. pool arrangement is good for airline industry and the travelling public. The Convention simply confirms their legality.

A recent step by ICAO to facilitate co-operation between airlines is the adoption of Art. 83 bis as follows

> «a) Notwithstanding the provisions of article 12, 31 and 32a of this Convention, when an aircraft registered in a contracting state is

operated pursuant to an agreement for the lease, charter or interchange of the aircraft, or any similar arrangement by an operator who has his principal place of business or, if he has no such place of business, his permanent residence in another contracting State, the State of registry may, by agreement with such other State, transfer to it, all or parts of its functions and duties as State of registry in respect of that aircraft under articles 12, 31, and 32a of this convention. The state of registry shall be relieved of responsibility in respect of the functions and duties transferred;

b) The transfer shall not have effect in respect of other contracting States before the agreement between States in which it is embodied has been registered and made public pursuant to article 83 or directly communicated to the other State or States concerned by a State party to the agreement.»

Due to the high costs of maintenance and purchase of aircraft, lease, interchange and charter of aircraft have become more common.

The state of registry has many duties concerning the aircraft and crew under the Chicago Convention. If the temporary operator of the aircraft is a national of another state, it might be a problem for the state of registry to control the aircraft and fulfill its duties under the Chicago Convention and also under the «Convention on Damage Caused by Foreign Aircraft to Third Parties on the Surface», Rome 1952, and the «Convention on Offences and Certain Other Acts Committed on Board Aircraft», Tokyo 1963.

Article 83 bis was adopted at the 23rd Session of the ICAO Assembly 1980 by a overwhelming majority.[3] The article will come into effect after two-thirds of the contracting states have ratified it.

In short, the state of registry does not have to fulfill its duty according to Art. 12,31 and 32a. The duty can now be transferred to the state of the operator. It will make it easier for the state of registry to have somebody from another state operating their aircraft.

In 1967, ICAO made a «Summary of Material Collected on Co-operative Agreements and Arrangements».[4] The states that answered showed what kinds of co-operation are common between the airlines. The different types of co-operation ranged from common arrangements in the handling of traffic, to leave and interchange of routes and aircraft.

There is reason to believe that co-operative activities among airlines have not declined due to the present poor financial situation of the airlines.

Increasing co-operation in European air transport is an expression of a European policy[5] that gives room for more co-operation in all areas through different organizations.[6] For example, EEC, ECAC and EFTA concerning trade in general and more specialized organizations like KSSU (KLM, Swissair, SAS, UTA) and ATLAS (Air France, Lufthansa, SABENA, Alitalia, Iberia) which are two organizations for maintenance and overhaul of aircraft.

The first, and so far the most successful co-operation between airlines is the Scandinavian Airlines System, SAS, which is a consortium of three airlines from Denmark DDL, Norway DNL, and Sweden ABA. ABA has 3/7 shares and the other two have 2/7 shares each in the assets.

Another similar arrangement is Air Afrique. At the 24th Assembly of ICAO in the fall of 1983, a resolution[7] was adopted that facilitates and encourages co-operative arrangements.

Most countries are dependent upon reliable air transport service for their economic and social development. This is particularly true for developing countries dependent on tourism. Such countries must be assured that there exist carriers which have an obligation to serve them in all circumstances.

However, due to economic realities relating to the establishment of a national airline, the high capital costs involved and the technological and managerial parameters of all airline operations, many small developing countries can not afford to have their own airline. One solution is, therefore, a form of co-operation-a single airline serving and owned by a number of countries. Another solution is that a state can designate an airline totally owned and controlled by another state.

In most bilateral ATA, though, the carrier designated by one contracting state must be substantially owned and effectively controlled by the government or nationals of that country.

To solve this, the resolution established a new concept. The real and substantial connection existing between developing

countries, members of a regional economic grouping, provides a genuine link which justifies the recognition of this community of interest as an acceptable alternative to substantive ownership and effective control.

The states rocognize, therefore, the concept of community of interest within regional economic grouping. On this basis, a developing state would have the possibility of designating an airline substantially owned and effectively controlled by another developing state or states in the same regional economic grouping.

For the concept to be valid certain conditions have to be fulfilled:

1) there must be a genuine regional community of interest between or among the developing states concerned;

2) the state making the designation must itself be a developing state within the regional economic grouping;

3) the airline being designated will have to be substantially owned and effectively controlled by another state or states or its or their nationals within the regional grouping;

4) the rights exercised would not be greater than the individual rights of the developing states concerned unless otherwise agreed by the accepting state or states;

5) the terms and conditions for use of rights exchanged in this manner must be mutually acceptable to the states concerned; and

6) in view of 1-5 above there are adequate safeguards to avoid «flag of convenience» operations.

An example of a region of this kind is the Carribean states which sponsored the resolution together with Mauritius, Belgium, Australia, and the U.S.A.

6.2 The Pools

Co-operation is not limited to developing states. European carriers use pooling more than any other carriers, and almost all intra European routes are pooled.[8] An example of a standard pool agreement is shown in the above-mentioned ICAO Circular in Appendix 12 on page 111.

The three areas where co-operation is best suited are: fares, regional services and special freight[9] and the pooling concept can be used in all three of them.

In large there are two kinds of pooling: technical and commercial. The technical pools try to rationalize the scheduling patterns, centralization of operations and reservations, interchangeablitity of tickets, joint promotion of sales, co-ordination of technical facilities and services by the participating airlines.[10] The purpose of the technical pools is to allow the airlines to perform more effectively.

The commercial pools, in most cases, provide for a sharing of revenues. The definition of a commercial pool agreement is an agreement between two airlines for the operations of an air route or air routes where the revenues derived from the services are put together and then split according to a predetermined

formula.[11] What kind of formula there is to be used is exemplified in Amer Sharifs report from the Arab air carriers organization «The Mathematics of Pool Agreements».[12]

The formula to be used depends on factors like types of aircraft used, system of «aircraft coefficients» or that of ceilings on the revenue or capacity pooled.[13] Exactly how the revenues are shared or what the pool arrangement look like, is often difficult to find out, since pool agreements often are confidential, unless they are provided for in the official bilateral.[14]

There is rarely a pure split.

The limit of how much of the revenue shall go into the pool, is often set on 70%. Then there is a limit within the pool depending on how much traffic the different carriers have. If one carrier has 40% of the traffic, he gets 40% of the pooled[15] revenues. The rest of the revenues, 30%, are left to competition, which gives the airlines an incentive to earn more. There is a lot of different reasons for establishing a commercial pool. One of the airlines might not be as well established in the market as the other one, and since it is very difficult to start operating on a new route, the airlines agree to pool their revenues until the weaker airline is able to compete properly.[16] In a market with a low density of traffic, the air transport agreement may contain provision for a pool, since there is not enough traffic for both airlines.[17] In such a case, it is no doubt a restrictive bilateral agreement with

some kind of predetermination of capacity that regulates the traffic. Thus, the airlines have to make the best of the situation. They can co-ordinate their schedules, so there will be services at all times, not only at peak seasons and peak hours. This must be considered as an advantage to the customers, since this arrangement will imply higher load factors followed by lower prices.[18]

Until the late 1970s, there was no possibility for price competition, since prices were fixed by the government and IATA. Restrictive bilateral agreements do not allow much competition with the result that it does not matter if one airline can offer a better and cheaper service than the other one. It will still not secure any more traffic. It should be pointed out that even if there was competition with the result that one airline discontinues service, the monopoly then achieved will not benefit consumers.[19] However, an airline in a monopoly position can not charge any kind of price, since the public can reroute,[20] and if the prices are too high, there is always room for another airline to operate.

Bermuda I was supposed to be a liberal agreement, and at least the U.S. has interpreted it that way, since it benefits it to have competition between airlines. Contrary to the broad U.S. interpretation, the Bermuda I principles can be interpreted in a most restrictive fashion. This is the case with intra European Bermuda type bilateral agreements, where, as mentioned, pooling agreements control capacity and flight frequencies.[21]

An essential part of all commercial pool agreements is capacity regulation.[22] In other words, a kind of predetermination of capacity through a back door on a non-governmental but inter airline level.[23] Furthermore, the purpose of pooling is much the same as for capacity agreements, elimination of wasteful competition, efficiency of operations and optional use of available aircraft.[24]

Even if the pool agreement between the airlines is confidential, the governments concerned must at least acquiesce, which is true for both private and government-owned airlines, and this is why the difference between capacity predetermination and pooling agreements is relatively insignificant.

A major difference does exist though. The pool agreements restrict competition even more than capacity agreements do which is examplified by Wassenbergh as follows:[26] first, there is a risk of unduly high artificial load factors due to the restrictions in the capacity offered. The airlines have then to turn away passengers that want to travel on a specific flight. In addition thereto, service standards may be in jeopardy.

When the prices are fixed through IATA's price fixing machinery and the capacity and frequencies are fixed through the capacity agreement, the only way for the airlines to compete then, is to provide the best service.

In a pooling agreement it is usually insignificant what airline the passenger is taking, since the revenue will be split, so the airlines might as well agree on a common service.

There is, however, still room for some competition, since usually all of the revenues are not split. Usually, about 30% is left for the airlines to compete about.

Another difference is that a strict division of traffic volume on a strict economic quid pro quo under an exchange of third and fourth freedom traffic can only be done through predetermination or an ex post facto review. However, in practice, the problem is solved through a pool agreement between the airlines with a sharing of revenues.

Pooling is used as a means for achieving reciprocity on a route segment. When it is reciprocity on a route segment, the airlines involved have recieved the same opportunities to operate, and at present that is the motive of bilaterals in Europe.

Reciprocal opportunities and benefits can only be agreed upon bilaterally or multilaterally, hence these concepts are subjective notions.[27]

Unfortunately, reciprocity implies much more than pooling. Reciprocity leads states to anomalies as equal bilateral exchange of economic aviation benefits, imposition of traffic quotas, discriminatory ground handling monopolies. In short, it is a bilateral protectionism and it contains all kind of measures to limit the access of a foreign airline from a third country.[28]

To sum up, the purpose of pooling seems to be that the airlines want to secure themselves of a way to exercise business that is to their advantage in the sence of more effective

performance. It could also be that they just want to be sure that they get as big a share and as much benefit from the market as the other airlines.

We shall also have a look at whether pooling also is an advantage to the travelling public, or if the fact could be that pooling is anti-competitive and restrict the consumers possibility to chose the best and cheapest airline. If the pool is a technical one and the result of it is more effective and cheaper operation of the airlines, the consumers will gain from it through better services and cheaper prices. There are different opinions, however, whether a purely commercial pool with revenue sharing is always the benefit of the public.

Since pooling is mostly used on low density markets and partically always in combination with schedule coordination to raise load factors and provide daily services to the consumers, it reduces wasteful competition, according to Mr. Bob Tole, Manager Business Centre Administration, Air Canada. However, he indicates that there may be some lessening of the «healthy» competition. It seems to be verified by the fact that, e.g. CP Air wanted a pool with KLM, because they felt they were weaker than KLM.[30]

Pools might also be anti-competitive due to the fact that they are prohibited in the U.S., since the Americans are of the opinion that pools restrict competition. Pools are only granted in the U.S. if they are of «national interest».[31]

It looks to me that pooling to a certain limit is good, which is shown in a clear way by the International Chambers of Commerce (ICC), which made a statement at the 24th Assembly meeting of ICAO 1983. In its pooling statement it argues that pooling of all kind is good to reduce trading obstacles, which will benefit the public. It is also good for developing countries as mentioned above. But, it should not be used to support protective governments and it must not frustrate consumers choice.[32]

Finally, IATA has not taken any official position, since it represents all airlines and thus wants to be neutral.[33]

CHAPTER 6: FOOTNOTES

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18. Mr. Bob Tole and S. Wheatcroft, The Influence of Operational and Technical Factors on Air Transport Regulation, from Aeronautical Journal, Aug. 1970, p. 623.

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26. Wassenbergh, Air Law in a New Era, p. 20.

27. Wassenbergh, International Air Transport a «trade in services». Address to the 4th Lloyd's Conference in International Civil Aviation, New York 11-12/6 1982, p. 4.

28. Supra, p. 4.

29. Interview with Mr. Bob Tole, ibid.

30. Canadian Air Transport, p. 619 and Canada-The Netherlands ATA Art.

31. Burton Landy, p. 577.

32. ICAO Doc. A24-WP/59 EC12 21/9/83.

33. Mr. Louis Haeck, ibid.

CHAPTER 7: THE COSTS OF AIRLINE OPERATIONS

7.1 Different Kinds of Costs

It is often alleged that intra-European air fares are too high. The «evidence» shown is the lower domestic U.S. fares. Confronted with these obvious facts, the public wants the European governments and airlines to take measures to lower fares. The politicians claim that the public support their call for lower fares, which puts the airlines in a financial squeeze. If you want to advocate lower fares, you must, however, be aware of the whole financial situation of the airlines and also look at the costs. To put matters in a proper prospective, IATA made in 1980 a survey of the cost and fare situation in the U.S. and Europe. The survey shows that Europe and American carriers have very different operating conditions with the implications that European carriers charge higher prices but also that they have higher costs. The higher costs reflect the wide diversity of political and regulatory environment in which the airlines must operate. About one-third of the costs can be controlled by the airlines in Europe. These costs are related to administration and management and they are the same in both the U.S. and Europe. The costs that cannot be controlled, about 65%-70%, are unmistakebly higher in Europe.[1]

The IATA study lists ten specific areas in which costs are higher as a result of individual government regulations

due to national sovereignty or long-established customs:

1) Fuel costs are much higher in Europe;

2) Air navigation charges. There is a considerable duplication of air navigation facilities in the densely crowded European airspace. Air navigation on higher altitudes is exercised by EUROCONTROL which in 1981 costs over a billion dollars;

3) Higher route detours in Europe. Restrictions in the European airspace force planes to take roundabout routes which consumes extra fuel. Average route detour is 15% in Europe and 3%-4% in the U.S.;[2]

4) Landing fees. The owners and administrators of international airports are always the governments. They impose all the costs of airport operations on the airlines. But, they also include costs for safety, security, health, custom and immigration services. These services have nothing to do with the operation of the airlines and shoud, hence, be paid by the national treasury. Charges for commercial services such as handling charges should be set in line with the economic environment in which the airlines operate.[3] For example, the landing fees on Arlanda airport in Stockholm are nearly ten times higher for a Boeing 747 than certain airports in the U.S. like Miami and Houston. This is despite the fact that Arlanda airport has lowered its fees by a half between the years of 1980 and 1982.[4]

5) Delays and crowded, inadequate airport ground facilities at European airports;

6) Security measures are higher in Europe;

7) Route density/economies of scale. A European equivalent of the American high-density transcontinental service does not exist;

8) Labour costs. The actual wages are about the same in Europe and the U.S., but on top of that the European carriers have to pay obligatory social charges. These largely invisible costs often average 50% of an individual's salary, compared to only 20%-25% in the U.S.;

9) Inefficient use of labour. European carriers have not the same possibility as the U.S. carriers to lay off employees to adjust to changed conditions;

10) Lower aircraft utilization in Europe for a variety of reasons. Europe has more restrictive airport airflows than the U.S. and distances are shorter in Europe. Proportionately more time is spent on the ground for refueling, servicing, loading and unloading. The daily utilization of aircraft, mostly Boeing 737 and 727 and DC-9, in Europe is about six hours or about half the utilization achieved on intercontinental services with long-range wide-bodied aircraft.

The Association of European Airlines - AEA - also conducted an investigation in 1982 about the costs of European carriers.[5] European officials believe that the airlines should fulfill a public mission. The mission include providing service on unprofitable routes, providing employment and encouraging tourism and foreign currency exchange. The airlines are often required to provide service where load factors are so low, that average operating costs per passenger km. has increased. Operating on non-profitable low-density implies cross subsidization from the high-density routes. Passengers on high-density routes are, therefore, paying a part of the ticket for passengers on the low-density routes.[6]

Marketing costs are also higher in Europe because of variety of languages, cultures and different currencies. The depreciation in Europe is also 65% higher.[7]

All of the above-mentioned factors are out of the airlines control. But they all add to costs which must ultimately be

paid by the travellers. Without taking these factors into account, a comparison between European and American fares cannot be fair.

7.2 Ways of Reducing Costs

The costs that can not be controlled by the airlines are in most cases controlled by the governments. Hence, the governments can also lower them; but unilateral actions are not suitable.[8]

International air transport overrides national, and bloc, interests. All European states are integrated in one air transport system, so there is a need for co-operation between the governments, to lower the costs for the airlines.

The European states seem to have the same kind of problems. Economic, social, operational and political factors have a habit of interaction which would make it difficult to isolate one, or even a number, of states from the wide concept of international air transport. The problems of Europe in the field of international air transport should thus best be dealt with by the ECAC and the EEC.[9]

The areas where government co-operation is suitable is first of all the bilateral agreements. They usually regulate commercial operations very strictly by limiting allowances of capacity and authorized landings. The European states should simultaneously liberalize the bilateral agreements to obtain a

more flexible system for the airlines to operate in. I will deal with this matter in the conclusion.

To simplify market entry and administrative procedures, all laws and regulations in the European states should be similar and harmonized. The governments should, furthermore, where it is possible, try to lower the costs for the airlines, e.g. try reducing the landing fees.

In short, a lot of restrictions in Europe, with following extra costs for the airlines, depend on the facts that there are many different countries in Europe. A solution would, therefore, be a network unhampered by national barriers.[10] I will deal with the measures taken by ECAC and EEC to facilitate co-operation among European states in Chapter 10.

Not only the governments ought to co-operate to lower the costs for the airlines, naturally, the airlines themselves must try to reduce their costs. They can co-operate in different manners for the purpose of reducing costs. In Chapter 5, I mentioned two organizations, ATLAS and KSSU, that are facilitating the maintenance and overhaul of aircraft, and thereby, making it cheaper for the airlines involved to repair their aircrafts.

The largest form of airline co-operation is IATA. Its most prominent task is to coordinate inernational tariffs, but it has also contributed to the facilitation of ticket handling, baggage checking, inter-lining and setting of service standards, all measures which have helped to reduce costs.

Another major airline organization is AEA, formed in 1973. It has much in common with IATA and its main objectives are:[11]

> «to contribute to the improvement and development of commercial air transport in Europe in the interest of the travelling public and the member airlines, by advancing the co-operation between the European airlines, by harmonizing their commercial, technical, and administrative policies and by anticipating and meeting such economic, commercial, social, technical and regional developments as may affect air transport and develop forward plans and innovative ideas.»

Hopefully, this objective will contribute to more effective and cost saving performances by the European airlines.

With inter-lining, a passenger can buy one ticket and use different airlines on the various route segments. There is a problem, however, with inter-lining connected with the introduction of airline deregulation and following low fare structures. When a fare is low for a segment of a flight, there is a dilution of the fare for the whole flight and, therefore, in the amount of the fare divided among the carriers involved. The solution is that a common policy or standard must apply in these situations so there can be an equitable division of the fare.[12]

Another form of airline co-operation is a joint air company similar to the SAS consortium. Roy Watts from British Airways pushed the idea of having a joint European air company consistent of British Airways, KLM, SABENA, Aer Lingus and Air France and operating between London, Dublin, Paris, Brussels and

Amsterdam with jointly owned aircraft in shuttle traffic. The shuttle would overcome the enormous no-show and change-of-booking problem which bedevils each of these business routes. On the London-Brussels route, for instance, only 30% of the passengers actually travel on the flight they originally booked. The problems of loss of airline identity, the giving up of national sovereignty and the sixth-freedom issue made this idea unrealistic.[13]

To effectivate the use of aircraft, airlines can co-operate by interchanging routes. For example, British Airways operates London-Paris and London-Amsterdam, Air France operates Paris-London and Paris-Amsterdam and KLM operates Amsterdam-London and Amsterdam-Paris. Through an interchange of routes, all three of these companies would be able to operate the route London-Paris-Amsterdam in either direction. Their respective governments must then agree on extensive fifth freedom rights which they will do only if the other governments will do it. A plurilateral or multilateral solution is thus suitable.

A similar way of co-operation is the «banalization» of aircraft, where an airline can «borrow» an aircraft from another airline at a time when the latter has no use for it. Representation agreements are another form of possible co-operation. Here companies would agree to represent each other in certain states or airports by, e.g. selling tickets for each other.

Moreover, there is the coordination and rationalization of timetables and also of handling agreements, viz, assistance during landing operations.[14]

The EEC does not believe that they can force the airlines to reduce their costs and become more efficient. But one way to increase efficiency is to allow some competition as a spur to efficiency. The airlines would then become more cost conscious.

A widely used type of co-operation by the European carriers is pooling (see Chapter 6). The ECAC has made a study over the extent of capacity restrictions and pooling agreements in European air services.[15] It shows that 75%-80% of the ton km. performed on intra-European flights are handled under pooling agreements which include some form of revenue or cost sharing. It is impossible though to deduce this from the official documents since there usually are confidential supplements to the bilateral agreement.

Pooling agreements often require the airlines to agree on capacity, fares to be charged, fare conditions, class and variety of services offered, schedules to be operated and they also restrict the routes that can be served. The basic purpose is, thus, to reduce the degree of competition in the provision of capacity.[16]

Clearly there exists cost saving aspects in the pool concept. Ten to fifteen per cent of the pooling agreements involve cost sharing and the agreements enable the airlines to make cost savings which they could not have done if they operated independently.

Pooling also helps the airlines to improve load factors. Furthermore, AEA argues that airlines participating in pools generally agree to spread their departure times throughout the day instead of having all flights at the profitable periods. The pools are intended to compensate the airlines for flying on less desirable times. Without the pools the European airline services will be less convenient, an AEA official says.[17]

The disadvantages with pooling between airlines from a passengers point of view is the fact that, e.g. sharing of costs puts less pressure on the pool partners to reduce the costs with high prices as a result.

The conclusion of the ECAC study was that pool arrangements generally protect the established airlines from excess competition and allow them to make long-term plans more effectively but the study also concluded that pooling agreements discriminate against more efficient carriers and against airlines that would like to enter markets.

The states that usually insist on a pooling agreement are those with a weak airline[18] and so long as there are differences of competitive ability among the European states, the less likely it is that liberal bilateral agreements can be introduced.[19]

Airline industry officials say, however, that there has been a slight reduction in the number of pool arrangements. Factors affecting this reduction of pools include the move of governments toward more «open sky» policies and pressure from charter airlines.

Another difficulty with pool agreements is the fact that some agreements provide that if the load factor or passenger share of one airline exceed a set level, it receives a larger share of the pool revenues. The stronger airline thus tries to negotiate lower levels at which their share increases, and the less successful naturally oppose this. To sum up, pooling and other kind of cooperations are, from the travellers point of view, good, where they help the airlines reduce their costs. Unfortunately, pooling has also a tendency to restrict competition and give cause for higher fares. The tendency ought to be stopped by implementing more liberal bilateral agreements. Airline cooperation as a means to reduce costs is important, but as mentioned above, the largest part of the costs can not be controlled by the airlines. If they lower their controllable costs by 20%, it still would result in saving only 1%-2% of the total costs, according to AEA.[20]

7.2.1 Other Aspects on Cost Reductions

Another aspect of cost reductions is that the airlines might be tempted to reduce safety measures since they cost money without contributing to the economic performance of the airline. The Air Line Pilot Association, ALPA warns[21] that to reduce costs, pilots, especially those not protected by an ALPA contract, are pressed to perform the operation under minimum or marginal conditions. Furthermore, bad times for airlines and the attempts to reduce costs, have forced some

airlines to cancel orders for new, safer and more efficient aircraft and instead continue to fly old aircraft that should be replaced. The large growth in the number of airlines in the U.S. have had, as a result, that the American Federal Aviation Administration - FAA - now has difficulties in controlling the security aspects of airline activities such as the flight performance and maintenance procedures. No proof exists though that shows a connection between accidents which have occured and the attempts by airlines to reduce costs by reducing safety measures.

CHAPTER 7: FOOTNOTES

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10. ATW Oct. 1980, p. 38.

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21. AWST July 11, 1983, p. 35.

CHAPTER 8: PRESENT STAGE OF EUROPEAN FARES CAPACITY AND ROUTES

8.1 European Fares

The table in Annex 1 shows the differences between U.S. domestic fares and intra-European fares and also the different fares available over the North Atlantic as of January 1984. Only one U.S. route is shown, New York-Dallas/Fort Worth, but fares are similar all over the U.S. for the same distances with similar traffic volume. In general, prices on normal economy fares are lower in the U.S. with a few exceptions. The difference between economy fares and discount fares is not as large in the U.S. and the same is true for the European airlines that charge low economy fares. The higher economy fare, the bigger difference between economy and discount fares.

Fares in Europe are not so homogenus as in the U.S. There is a substantial difference between some European fares for the same distance which makes room for competition, since travellers can reroute trying to achieve the lowest possible fare. They can use the economy fare only on one route segment and discount or charter fares on another route sigment. Italy seems to be very restrictive in their price policy. However, the most expensive country is Sweden. It is more expensive than Denmark despite the fact that it is the same air company, SAS, that is designated by both states. For example, Stockholm-London costs 460$US and Copenhagen-London costs 350$US, Stockholm-Zurich costs 393$US and Copenhagen-Zurich costs 279$US.

The liberal agreements concluded between the U.S. and Federal Republic of Germany,[1] Belgium, the Netherlands ought to have lowered the prices over the North Atlantic. This is true in the case of the Netherlands and Belgium but not in the case of FRG. The answer to this could be that the ATA between the U.S. and FRG refers to the rate fixing machinery of IATA, while the agreements between U.S.-Belgium and U.S.-the Netherlands do not do that. Hence, airlines from these countries have more freedom to compete with prices. Another argument could be that Lufthansa taking care of the largest part of the traffic between the U.S. and FRG is the price leader on the route and the other airlines follow because it is profitable to do so.

The cheapest fare over the North Atlantic is 150$US charged by People Express. According to Bermuda II, ATA fares must be cost related but despite the low price charged by People Express it is still cost related since the company has managed to reduce their costs substantially.

The prices shown in the table say nothing about service, losses or profits. SAS, for example, has chosen to improve service to attract business poeple and other people that are not price sensitive. These customers constitute a more secure source of income for the company. Moreover, the Belgium national carrier, SABENA, which had been making losses for over twenty years, recently managed to return into profitability as a result of wage cuts and an early retirement program.

To attract those people that can not afford normal economy fares, the European states have introduced a number of discount fares. At the moment there is about 350 different types of discount fares in Europe. There exists all kinds of restrictions on the purchase and use of these low-fare tickets. Examples of restrictions are limited validity, limited stay, only a certain category of customers can buy the ticket, e.g. students and ticket must be purchased a certain time in advance.

8.1.1 Reasons for High European Fares

In Chapter 7, I emphasized that airline costs are much higher in Europe than in the U.S. as the main reason for higher European fares.

Airline Users Committee - AUC - has conducted a survey over European fares which shows other reasons for high European fares, than high costs.

The price level in Europe is due to several factors:

1) the many decision centres, which run counter to greater efficiency and good coordination;

2) first class fares are maintained at an inadequate level;

3) the losses due to revenue sharing rules in the case of non-European passengers on inter-continent trips with one or more intermediate stops in Europe; and

4) the serious dilusion of revenues (about 30%) due to the existence of reduced fares.[2]

Most of intra-European routes are served only by two carriers carrying third and fourth freedom traffic. The basic reason is that there is usually not room for more than one carrier on these routes, but another reason is that the routes are carefully protected by the governments. On these routes where there, thus, exists an effective duopol, there usually also exists a revenue sharing pool with the result that carriers involved are in a position to extract monopoly profits. They have done this by effectively controlling the provision of capacity and by controlling fare levels through IATA Traffic Conferences. In practice this has meant unusually high fare levels.[3]

Furthermore, it must be remembered that virtually all European air services are operated by airlines owned or controlled by their national government, implying no price competition since they are regulated and controlled by the governments. In the absence of pressure from consumers, there is no incentive for either governments or airlines in Europe to reduce costs and/or fares.[4] And even if one government is willing to reduce fares, the attempt can be stopped by other governments, usually by those with a weak airline.

Intra-European passengers are subsidizing the European carriers on their intercontinental routes where competition is fiercer. Normal economy class travellers are further subsidizing all other kinds of fares on intra-European air services.[5]

In Chapter 3 I mentioned the 1967 Agreement on Establishing of Tariffs in Europe which contains the traditional administrative procedures for establishing tariffs. Even if the agreement facilitates the administrative procedures, it also hampers innovative proposals that would liberalize tariff procedures. Hence, the problem must be solved through unified actions with all the states involved. It is, thus, best dealt with in the framework of EEC[6] and ECAC.

8.1.2 Discount Fares

To meet the low price competition from charter carriers, scheduled carriers, with British Airways in a leading position, started in the mid-70s, to introduce different kinds of discount fares. As we can see in Part 8.1., the number of discount fares has grown considerably. The result was an increase in scheduled traffic, since passengers chose the more convenient services provided by the scheduled carriers.[7]

About 25% of all passengers on intra-European routes are paying normal economy fares, 25% are using discount fares and 50% are travelling by charter.[8] The amount of discount fares available is about the same in the U.S. and they are used in the same extent as in Europe.

There are relatively fewer travellers using reduced fares on short haul routes than on long haul routes.[9] The big increase in charter and discount fares have been recognized in the new liberal bilateral agreements concluded between the U.S.

and Belgium, the Netherlands ~~and~~ FRG. Fares in the normal Bermuda I type agreements are related to costs. In the new liberal agreements, fares, rates and prices shall be set by each designated airline, based primarily on commercial considerations. Government intervention should be limited to prevention of predatory and discriminatory practices, protection of consumers from the abuse of monopoly power and protection of airlines from prices that are artificially low due to direct or indirect governmental support or subsidies. The agreements between the U.S.-Belgium and the U.S.-the Netherlands do not refer to IATA rate fixing machinery, which is another step towards a liberal fare policy. All the new liberal agreements concluded by the U.S., including Bermuda II, also recognize the charter concept and the need for its development.

The problem with discount fares is that they are often too encumbered with restrictions that do not always reflect costs. The restriction imply poorer service which means that in practice the fares might not be so low as they appear to be.

As mentioned in Part 8.1.1, passengers paying normal economy fare are usually subsidizing passengers travelling on discount fares. The most serious case of such cross-subsidization can occur where low-rated traffic forms a large proportion of traffic on a given route. The regulatory authorities have here a responsibility towards the full-fare traveller, who may bear any residual costs not covered by the low-rated passengers.

Discount fares must, thus, be cost related since the normal fares are required to be cost related. However, airlines can relate their fares to the costs of the most efficient airline in the same market. Aviation authorities, therefore, can not force airlines, that, for whatever reason, can not match the costs of the most efficient airline, to charge higher prices than their competitors against the judgement of their management.[10]

If international air transport was controlled in a free market, airlines could cross subsidize discount fares so long as passengers travelling on economy fare are willing to pay an excessive amount of money. However, fares in international air transport are regulated by governments. They have, therefore, a responsibility to see that such an unfair situation does not arise.

8.1.3 Regulation of tariffs

A much disputed question is whether international tariffs should be regulated by governments and IATA or if there should be a liberalization of tariff regulations in Europe or if the international tariff system should be organized in some other way. There is a lot of different opinions in the matter amongst authors and politicians. It is, therefore, impossible to give a definite solution to the problem so I will refer to some views in the matter, that represent the present international discussions.

No serious proposal advocates a complete deregulation of international fares. The European states will not surrender their control over fares. Wheatcroft, for example, believes[11] that there is a need to regulate airline fares. It is a central feature of the whole system of economic regulation which is necessary to secure the primary objectives of public policy in air transport development. The disadvantage with fare regulation is though that there will be a wasteful competition when trying to improve service to attract passengers.

The CAA in the U.K. has taken a similar view and established some principles on international tariff policy.[12]

1) prices should not exceed the cost level plus a fair return on capital investment;

2) every price charged should be related to costs;

3) fare regulations should be simple, rational, and enforceable;

4) air transport supply should be able to meet all demand from categories representative of the population; and

5) regulations should be maintained of the minimum level required to meet the preceding objectives.

However, this policy is aimed at sound management of airlines and efficiency of operators, but there is no concern for the users. The policy implies that passengers have to meet costs they are not responsible for. On the other hand, the policy gives no room for cross subsidization between routes. But one might argue that those benefitting from more favourable

conditions should participate in maintaining unprofitable routes.[13]

International tariffs have always been established through the IATA tariff conferences. In recent years IATA has changed its position a little. The Association favours the 1982 Memorandum of Understanding on tariffs between the U.S. and some European states. The agreement will, according to Sir Adam Thompson, Chairman of BCAL, transfer the tariff fixing responsibility to the governments. IATA's role should merely be to coordinate rates and act as a holding company for safety and technical areas and inter-line facilitation like ticketing.[14]

Furthermore, IATA proposed an arrangement similar to the MOU in matter of establishing international fares. Three objectives should govern the setting of international tariffs:[15]

1) fare zones should be established. Proposed fares that are inside these zones should be approved automatically by the governments;

2) the amount of zones should be limited to 4 or 5; and

3) prices should be related to costs.

The role of IATA as a tariff co-ordinator is also advocated by Wassenbergh.[16] Inter-lining is essential for the development of international air transportation. Agreed tariffs must, therefore, allow for such inter-lining. The best solution is multilateral tariff co-ordination and not tariff deregulation as the U.S. proposes, nor tariff regulation, nor tariff discrimination as practiced by some states in their tariff policies.

Whatever the tariff policy is, it can not be separated from the policy of capacity access and regulation of market entry. Where there is capacity control and route fixing, a free pricing system would be nullified as traffic is properly divided anyway. Free pricing can only be applicable where there is a free market. It will otherwise lead to subsidies since states will never let their airlines go bankrupt. However, some markets are more price elastic than other which implies a more liberal price and capacity policy and a liberal entry system. If there was strict price fixing on a price elastic market, it would protect the high cost carrier, normally through capacity control. A static market always contains price control which is the logical compliment of a carrier-oriented capacity control systems.[17]

To sum up, most authors and governments agree that there must be some regulation of international tariffs. The dispute concerns mainly the extent of the regulation and in what form.[18] The aim of tariff deregulation is to give room for some competition with lower prices as a result. But we must remember that it is very difficult to lower prices in Europe due to the high costs. Airlines want to liberalize fares but they can not do that because of higher costs and personnel policies.

Naturally there exists opinions advocating total freedom in Europe, but they are usually not well argued.[19]

8.2 Capacity

In bilateral air transport agreements similar to the Bermuda I, the primary objective is that capacity provided by each airline should be related to the traffic demand between the two contracting parties, i.e. third and fourth freedom services. Capacity provided for fifth freedom traffic is a subsidiary objective.[20] Furthermore, there must be a fair and equal opportunity for both carriers to operate, and an eventual imbalance in the capacity provided is connected in an ex post facto review.

In the bilateral agreements between U.S.-Belgium (Art. 11) U.S.-the Netherlands (Art. 5) and U.S.-FRG (Art. 5) there is no capacity regulation. Only the «fair and equal opportunity» concept is left. It provides that each party shall take into consideration the interests of the other party and its designated airlines so as not to affect unduly the opportunities for the airlines of the other party when exercising their rights. However, the opportunity to operate is not the same for all airlines.

For example, the pricing opportunity is not the same for the European airlines as for the American airlines since costs are much higher in Europe. European airlines have also the duty to serve low density routes meaning that they have to subsidize them from the profitable routes. Hence, they have not the same opportunity to compete with U.S. carriers on the profitable routes.[21]

A liberal bilateral agreement has not yet been concluded between two European states so practically all intra-European agreements are similar to Bermuda I. The agreements, directly or indirectly, limit the capacity to be provided. The ECAC study mentioned in Chapter 7.2 showed that there are capacity limitations on 90% of all the routes among ECAC states. To liberalize the capacity provisions and give opportunity for the airlines to compete, the task force of ECAC proposed zones for capacity regulation. One zone would be for capacity on existing routes. If an airline wants to provide more capacity on an existing route, the state of the airline is permitted more capacity, provided that the airline has done well in the past and is able to carry more traffic. The capacity offered by each airline shall not exceed the zone limit though. The limit should always be set over 50% of the total capacity provided on the route.

The other capacity zone is for route creation. Any additional route is permitted automatically if certain conditions are fulfilled: it must be adequate demand on the route, the new service must not affect the traffic on other routes and the service may be withdrawn if an ex post facto review shows that inadequate demand exists. With a strict interpretation, these conditions can severely hamper any new route creation.

8.3 Routes

The longer the distance of a journey is the more favourable it is to travel by air. For example, the advantages of travelling

by air on a journey of 2,500 miles or more, are so great compared with surface transport that aviation has little to fear of competition from that transport medium. However, a significant portion of European flights cover distances less than 2000 miles and many flights cover distances less than 500 miles.[22]

A large majority of European routes are low density routes. Only the routes London-Paris, London-Amsterdam and London-Frankfurt have sufficient traffic for more than one carrier.[23] These two factors combined with the fact that most traffic in Europe is third and fourth freedom traffic implies low utilization of aircraft and, thus, expensive operations for the carriers.

Furthermore, there is a trend in Europe towards more restrictive route schedules. Most European bilateral agreements grant fifth freedom traffic rights.[24] But some bilateral agreements concluded in the end of the seventies only grant third and fourth freedom traffic rights[25] with some minor exceptions. The ATA between the U.K. and Italy[26] grants the Italian carrier fifth freedom traffic rights but only to Hong Kong which is regarded as British territory. There are also some fifth freedom traffic rights granted in the ATA 1979 between Sweden and the U.K., but this is mainly due to the fact that the Swedish airline SAS, is also designated by Norway and Denmark.

The solution to the problem of better aircraft utilization is liberalization of the European route structure through co-operation. The European airlines must be allowed to develop a system of services with freedom to move their places of departure and arrival easily and redesign schedules and network.[27] Thus, more fifth freedom traffic rights must be granted so the airlines can use their aircraft in the most efficient way. If all European states, preferably within the framework of ECAC, agreed on extensive fifth freedom traffic rights, it would theoretically allow an airline certificated in one of the states, to serve all other ECAC states. With fifth freedom traffic rights granted, the airlines would have the opportunity to interchange routes and change their schedules according to traffic demand.

CHAPTER 8: FOOTNOTES

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2. ITA Bulletin Nr. 21, 1978, p. 508.
3. Rigas Doganis, Air Transport, A Case Study in International Regulation, Journal of Transport Economics and Policy Vol. III, nr. 2, May 1973, p. 115.
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6. Gary Heillbronn, Regulating the Setting of Scheduled International Air Fares, Thesis Monash Univ. 1983, p. 158.
7. AWST Oct. 9, 1978, p. 30.
8. Airport forum April 2, 1981, p. 31.
9. ITA Bulletin nr. 21, 1978, p. 510.
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11. Steven Wheatcroft, Aeronautical Journal Aug. 1970, ibid.
12. Supra, footnote 10, p. 9.
13. ITA Bulletin, nr. 21 1978, p. 512.
14. ATW Dec. 1983, p. 25.
15. ITA Bulletin nr. 3, 1982, pp. 51-56.
16. Henri Wassenbergh, Reflections on Sixth Freedom Questions, from International Air Transport in the Eighties, ed. by Wassenbergh and Fenema, The Netherlands 1981, p. 195.
17. For further details, see: ITA Bulletins nr. 35, 1979, p. 796.
18. See, for example, Airport Forum April 1981, p. 31.
19. See, for example, The Economist 4-10 Dec. 1982, p. 48.

20. Clause 6 Final Act of Bermuda I.

21. ITA Bulletin nr. 11, 1981, p. 265 and nr. 25 1981, p. 617.

22. Aerospace June/July 1975, p. 21.

23. ATW January 1979; p. 48a

24. See, for example, Sweden-FRG ATA from 1957.

25. See ATA between U.K.-Austria, U.K.-Sweden, U.K.-Italy. It shall also be kept in mind that the U.K. is supposed to be one of the most liberal states in Europe.

26. Agreement between the U.K. and Italy for air services between their respective territories, 1976.

27. ATW Oct. 80, p. 44.

CHAPTER 9: DEREGULATION OF EUROPEAN AIR TRANSPORT

9.1 Governments Attitude To, and Their Involvement In, Airline Activities

When discussing the regulatory system of international air transport, certain political and economic realities can not be ignored. Compared with other commercial activities, aviation is unique in matter of trade and in communications. Aircraft can easily cross national borders which raise the issue of sovereignty, jurisdiction and defence.

Air transport is distinguished from traditional trade commodities, which is a reason for regulating air transport in a different way from normal international trade. Aircraft seats are a perishable commodity. They can not be stock-filed. The «market» is immobile and can not be transferred to another country. Air transport is also one of the few commodities traded by all nations. Aviation is a communication system and it is, therefore, regarded as a quasi-public utility with certain obligations.[1]

A very important task for European airlines is to create job opportunities which gives us a social aspect of European air transport.[2] All these factors have to be taken into account to understand why European governments are regulating international air transport.

The European states have succeeded in their goal of each having its own airline.

State intervention in airline activities has, however, been to the detriment of the consumers. All major commercial air transport activity depends on state intervention, sometimes unilaterally, but mostly bilaterally. This leads to the introduction of non-economic elements into the system, with negative effects on the effectivity, as for instance:

- rigidity of the exchange of traffic rights on a purely bilateral «do ut des» - basis, deprimental to the network;
- the predominance of the request of market shares for the national carriers irrespective of their productivity; and
- unilateral restrictions on charter services.

The result is strong concentration of traffic of the main airports, a very little chance of market entry and as to the scheduled services, the pool arrangements and the way of setting fares have lead to a tendency of high fares. However, the «public service» concept adapted by the European governments has been to an advantage for business travellers and holiday makers.[3] It is also a need for the airlines to be financially healthy since the governments will never let their airlines go out of business. If there would be totally free competition some airlines are bound to get into financial difficulties. Hence, subsidy wars will ensue.[4] In the beginning of airline activities, they were subsidized by governments due to the heavy financial burdens. In the last twenty years, official subsidies have gradually disappeared and today they are exceptions.

However, the system of direct subsidies have been replaced by a system of indirect state aid that may be more harmful than its earlier forms. This indirect aid is based on government aviation policies.

There still exists a couple of direct subsidies though. A special circumstance often requires financial aid from the government. An example is the introduction of the Concorde.

The government may want the national carrier to use a specific airport even if it is not economical for the carrier to use it. The government will, thus, compensate the carrier for its losses.

More common, though, are indirect subsidies such as the following:

Cross subsidation between markets: Tariffs on routes to and from developing countries are often high so the weak airlines from the developing countries have the opportunity to develop. This means that the more effective airline from the developed country is making a high profit which is used to compensate for losses on other markets such as the North Atlantic.

Other examples of indirect subsidies are mandatory use of flag carrier by civil servants, assistance to aircraft manufacturing industry resulting in cheaper purchase prices or the airlines, preferential funding arrangements, etc.

When a low-cost operator, such as People Express, starts a new service, it will only operate on the profitable routes

and during peak hours. With its lower prices, it will take away traffic from the flag carrier. The flag carrier, therefore, needs financial support to be able to serve the low-density and unprofitable routes. Under such circumstances it can be argued that it is the low fare airline that is the cause of the subsidy.[5]

When discussing the regulatory system in Europe we must, thus, have in mind that the European governments will never surrender control over airline activities if the result would be poorer service to their country or their airline would go bankrupt.

9.2 The Influence of U.S. Deregulation on European Air Transport

In 1978, President Carter signed the «Airline Deregulation Act». The Act is intended to remove government control over air carriers, their market entry and their pricing. The result is that a lot of new airlines have emerged. They do not have the same costs as the large, established airlines, with the result that they are charging much lower prices. To provide a similar kind of service at much lower prices is a sign of efficiency. The large airlines are bound to follow this path, otherwise, they will lose traffic.[6]

Encouraged by its domestic deregulation, the U.S. decided to deregulate also the international air transport system. The American positions can be summarized as follows:

«The goal of effectively deregulating international aviation and maximizing carrier latitude on entry, pricing and service conditions is basic to U.S. policy.»[7]

It was in 1978 the new policy objectives were announced by President Carter[8] as follows:

1) Creation of new and greater opportunities for innovative and competitive pricing that will encourage and permit the use of new price and service options to meet the needs of different travellers and shippers;

2) liberalization of charter rules and elimination of restrictions on charter operations;

3) expansion of scheduled service through elimination of restrictions on capacity, frequency, and route and operating rights;

4) elimination of discrimination of unfair competitive practices faced by U.S. airlines in international transportation;

5) flexibility to designate multiple U.S. airlines in international air markets;

6) encouragement of maximum traveller and shipper access to international markets by authorizing more cities for non-stop or direct service, and by improving the integration of domestic and international airline services; and

7) flexibility to permit the development and facilitation of competitive air cargo services.

Simultaneous with this policy statement, the U.S. government tried to reach bilateral agreements that would:

1) permit garanteed multiple designation;

2) establishment of free pricing mechanism through adoption of a country-of-origin pricing system; and

3) liberalization charter rules so the country-of-origin system could apply.

In exchange for the acceptance of these rights by foreign trading partners, the U.S. was willing to grant major route concessions as consideration.[9]

This policy of the U.S. is an attempt to promote competition internationally. The U.S. has been accused of imposing unilateralism and trying to alter the international regime without multilateral consultation.[10]

In their attempt to impose this liberal policy, the U.S. has signed a number of liberal agreements.[11] They are more or less expressions of the above-mentioned policy and they have completely removed the capacity clauses. Only the «fair and equal opportunity» is left. Moreover, charter is liberalized and prices are generally lower than on similar routes governed by other more restrictive agreements. This is due to the fact that the fares are now based more on market considerations and do not have to be related to costs. The main provision is though the route allocation with extensive fifth freedom rights granted. The most important provisions from the liberal U.S. agreements can, thus, be summarized as follows:

- Unlimited designation;
- multiple and optional routes;
- no capacity clause but provisions for ensuring fair and equal opportunity for competition;
- no distinction between charter and scheduled pricing. Country-of-origin and double disapproval clauses;
- price matching. Automatically approved fare if it is substantial similar to other prices on the same route;

- government interference only where there is price abuse; and
- charter and scheduled services are negotiated together.[12]

Airlines from those European states that have signed this kind of liberal agreements with the U.S.-Belgium, FRG, and the Netherlands are now forced to be more effective. However, the problem is that if they fail to operate profitably, the result will likely be subsidization. Furthermore, this liberal trend in international protectionism is opposed by states with weaker airlines or which do not want a liberalization of international aviation for some other reason.[13] There has been strong opposition to the liberal trends, started by the U.S., FRG firmly opposes the extension of tariff liberalization.[14] This is despite the fact that the tariff clauses in Art. 6 of the U.S.-FRG ATA is more restrictive compared to the other liberal agreements like the others, tariffs are based on commercial considerations, but unlike the other agreements the U.S.-FRG ATA refers to IATA's rate fixing machinery and it also contains a double approval clause in the case the airlines from both contracting states have agreed on an IATA tariff. If they do not agree, the country-of-origin clause applies. See Art. 6d of the U.S.-FRG ATA.

9.3 European Deregulation

An analysis of the present European regulatory system reveals that the system is not different from systems in other

markets. The system is based on bilateral agreements, or, in the case of non-scheduled operations, unilateral permits, apart from a number of specific activities regulated by the 1956 Agreement on non-scheduled traffic concluded in the framework of ECAC (see Chapter 5).

The bilateral system in Europe includes both the classic categories of bilaterals: Bermuda I type and pre-determination agreements. Very few cases of multiple designation are to be found. The tariffs are concluded through IATA Tariff Conferences.[15] The agreements grant third and fourth freedom traffic in virtually all cases. The route structure is very restricted so the carriers can only operate to major hubs in each state. Fifth freedom traffic rights are granted in 75% of the agreements, but fifth freedom traffic account for only 1% of all intra-European traffic. The bilateral agreements provide for multiple designation, but practically all European states have only one flag carrier. Hence, nearly all routes in Europe are operated by two carriers. Ninety per cent of the agreements in Europe regulate capacity through predetermination or ex post facto review. There are, in addition, a large number of inter airline commercial agreements. Seventy-five to eighty per cent of all km. performed in Europe are under pooling and all of them are revenue sharing and 15% of them provide for sharing of expenses.[16]

The question is now whether this system is best for future development of European air transport. As we can see,

the system is highly regulated to the benefit of the national carriers. One of the reasons is that a basic policy of each European government is to have its own national carrier. Other policies of the European states can be summarized as follows:

1) states want to ensure that the network of services offered to the public generally has a reasonable constancy and durability;

2) states want their airlines to be profitable;

3) states want to serve other national interests outside air transport, such as tourism, the balance of payments, defence, all of which may be dependent on the existence of air traffic into their territory; and

4) states want to offer their travelling public low fares.[17]

When discussing an eventual deregulation of the European air transport system, we must remember, as mentioned before, that European governments will never completely give up their control over the air transport system. The governments will have to give up some of their policies to make an eventual deregulation possible. We must also keep in mind that the purpose of an eventual deregulation is to provide the public with better and cheaper air transport services. If that goal can not be achieved, the present system will most likely continue to govern European air transport.

9.3.1 Possibilities for Deregulation of European Air Transport

The deregulation in the U.S. started around 1978. The new system is substantially different from the old one. Hence,

the final effects of the change can not be seen immediately. That is why the European states have been reluctant to follow the U.S. experiment. So far there has been no actual changes in the air transport system in Europe except from the liberal agreements concluded between the U.S. and Belgium, FRG, the Netherlands, and also the Memorandum of Understanding for North Atlantic Air Services 1982. Nevertheless, from different symposiums held, books and articles written, policy statements made, one can draw the deduction that there is a tendency in Europe towards a more liberal air transport system within the framework of the present bilateral system.

We can distinguish two main regulatory trends in Europe: total pricing freedom subject only to antitrust laws, and regulated pricing flexibility exemplified by the liberal bilateral agreements and the Memorandum of Understanding 1982.[18] We shall examine the different proposals a little more closely and see if there exists a common European air transport policy.

In 1981 there was an air transport symposium held by the Royal Aeronautical Society in London. The subject of the symposium was «The European Aviation Scene: A Review of the 80's». Scholars, politicians, and airline people gave their opinions about how the future air transport system in Europe would look like. Lord Trefgarne expressed a common view that decisions in aviation is often made by politicians with the result that the decisions tend to have political considerations instead of commercial.[19]

Aviation has changed a great deal in the technical and commercial fields since World War II, but the regulatory system has remained the same. Lord Trefgarne suggested that airlines should have freedom to offer prices based on market forces instead of being cost related as they are now. The trade shall be free but fair. There can not be a fair trade if not all airlines have the same opportunity to compete.[20] The purpose of these proposals is to make European airlines more competitive. Not through a complete deregulation like in the U.S. though, but an orderly deregulation through international bodies like EEC and ECAC. Intervention by governmental authorities shall be limited to control that fares are not dumped, but generally in line with costs and they shall also prevent abuse of monopoly.

Also Antoin Daltman from Aer Lingus argued that aviation policy must be broadly consistent with Europe as a whole rather than geared to narrow sectioned interests.

A rapid liberalization of the present system is essential according to A.V.P.Vernieuwe, Secretary General of Independent Air Carriers of EEC. The flag carriers will, otherwise, gain an even more dominant position and it will be extremely difficult to establish new services. Others argue that the deregulation must be taken step-by-step. An orderly deregulation and reorganization of services is more appropriate.[21]

The suggestions by Vernieuwe will improve flexibility of charter fares so operators can meet demand better and traffic

rights will also be more easy to obtain. Vernieuwe's view is that the major obstacles to implement his proposals are the pool revenue sharing and capacity determination even on the high density routes. The best solution according to Vernieuwe is to let the EEC administer the air transport system in Europe.

Erdmenger[22] also emphasized the flexibility concept. It must be easy for the airlines in Europe to enter new markets. There is no possibility for a total deregulation, so it must be balanced between freedom and intervention to the interest of the airlines and travellers. Erdmenger wanted a reduction in the national interest by establishing a network of services between European states, based on airline initiatives and not based on bilateral agreements.

Other authors argued that there should be different systems on different markets. Erik Wessberge argued in his article «Fair and Equal Opportunity», ITA bulletin no. 12, 1981, that liberalization is suitable in different grades in different regions and on different routes. Antoin Daltman gives the same view and argues that there should be low prices on high density routes and high prices on low density routes.[23] There are also voices that want to take a more careful approach to an eventual deregulation of the European air transport system.

The fact is that the present system has worked well since World War II. The airlines were subsidized in the beginning but are not any longer. More and more people use aviation as a mode of transport. And the most important of all, compared to

other prices, fares have not risen as much. Opponents to deregulation, thus, argue that one should be careful changing a well functioning system. I will here give a brief summary over the most common arguments against deregulation.

Liberal policies are not within everyone's reach. Liberal agreements have only been introduced between countries that have strong markets, i.e. the industrial and «new industrial» countries in south-east Asia. The carriers from those countries can - contrary to airlines from developing countries - chose whether they want to participate or not in low fare policies. The other countries are able to participate in these policies only if they benefit simultaneously from a major traffic flow or have a seizable cost advantage. These developing states can not adopt liberal policies because they operate services in their markets and their airlines are often high cost operators. A more suitable approach is co-operation between these states to try to reduce costs.

However, protectionism is not a solution to their problems because it would remove them even further from the main traffic flows.[24]

Rigas Doganis adds more arguments in his article:[25]

1) Unregulated markets would result in cut-throat price warfare with chaos and adverse consequences for all participants;

2) aviation is a quasi-public utility which the governments prefer to stand on its own feet. Hence, they give the airlines a protective position to survive economically; and

3) scheduled services must be protected from non-scheduled services, since scheduled services have certain obligations to provide service for the public.

Furthermore, a state will never limit its sovereignty over the airspace by permitting access to it for all the other states through a multilateral agreement. Similar arguments are given by Director General of IATA Knut Hammarskjold.[26] Heavy investments are made in national airlines. The states would thus never let their national carrier go under.[27] There are also fears that all routes will not be served properly.

A common argument is that there will not be a fair and equal opportunity to compete, since new airlines will only operate on profitable routes while the established airlines have to serve the non-profitable routes as well. Hence, why should there be no competition even on high density and profitable routes.[28]

At the above-mentioned symposium held by the Royal Aeronautical Society, the social aspects of air transport were emphasized by Clive Iddon, Secretary General, Committee of Transport Workers, EEC. Deregulation, even if it is very little and organized, means that airlines have to be more productive which means less employment. He also believes that competition is likely to lead, under certain conditions, to misuse and waste and that the workers will suffer in the end. Layoffs with only a couple of per cent will have large consequences since, e.g. British Airways alone has about 45,000 employees.

A summary of all the opinions indicate a trend toward an orderly deregulation. The concept implies more flexibility in pricing and market entry so the airlines are able to change fares and route structure according to demand. The states can not deregulate alone, all European states have to deregulate together. Hence, a coherent European policy is necessary, preferably within the framework of EEC and ECAC. How much it is possible to deregulate can only be told by the future. The reason for orderly deregulation is that the European air transport system is so well established with the same type of bilateral agreements and the same kind of policy among the European states. To change this overnight is impossible and above all, the European states will never agree on U.S. type of deregulation.

Another reason for a careful approach is that the fundamental problem in European air transport is the high costs (see Chapter 7). Without lowering costs first, it is difficult to lower the fares. Furthermore, many states have other concerns than liberalization of aviation at the moment. There are more crucial matters that the airlines have to deal with first such as the economic recession over capacity, inflation, rising costs, crowded airways, and illegal discounting of tariffs. States, therefore, want order in air before they can think of liberalizing the system.[29]

The purpose of an eventual deregulation is to make air transport more available to the public by offering them more choices of routes and lower prices.[30]

A good summary of the purposes and results of deregulation is made by Hans Raben[31] and his opinion is also reflecting the opinions I have presented above:

1) for a start, states will refrain from further reducing the level of services on existing routes;

2) they will allow experiments with capacity if it would result in better services;

3) they will relax restrictions on application for services to or from other airports than the large hubs;

4) they will authorize fare innovations within a fixed set of rules, e.g. fare zones;

5) a close surveillance of the market by the states must be established to produce evaluation of experiences and to spot dangerous situations; and

6) the possibility of remedial actions in agreed circumstances should be provided for.

There is already signs of that the policy of orderly deregulation will be implemented in the future. The liberal agreements concluded between the U.S. and Belgium, the Netherlands, and FRG are example of a more liberal policy as well as the Memorandum of Understanding 1982 with its fare zones over the North Atlantic.

A study group established by ECAC - COMPAS which studied the conditions for deregulation in Europe, advocated orderly deregulation and flexibility.[32]

CHAPTER 9: FOOTNOTES

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10. E. Driscoll, Deregulation - the U.S. experience from International Business Lawyer 1981, Vol. 9, p. 157.

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18. Gary Heillbronn, ibid, footnote 5, Chapter 8, p. 163.

19. See also J.Erdmenger, ibid, footnote 3, p. 41.

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23. See also Ali Ghandour, ibid, footnote 7, p. 56f.

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CHAPTER 10: ECAC AND EEC AVIATION POLICY

10.1 EEC Aviation Policy

By its nature international air transport tends to override purely national interests, although this is not to suggest that, when necessary, national sovereignty can not be exercised. The question is whether an international body like EEC is suited to regulate European air transport, bearing in mind the concept of national sovereignty of the member states and their common interest in a well functioning air transport system. Regardless of what the final conclusion might be, European air transport can not be looked at simply from a Community standpoint, since intra-European services affect and are affected by, extra-European air services.[1]

The EEC can not alone work out a series of co-operative agreements among member states because the nature of the Community is a general concept that flows into all fields of economic activities.[2]

The EEC can not operate alone to improve aviation in Europe. It needs help from member states and the rest of the world.[3] The Council of Ministers and the European Parliament can not force proposals in the air transport field, on the member states. And most members are not yet ready to yield national sovereignty to give the European Parliament legislative powers in a federal Europe.[4]

So far, European states have been very reluctant to enter into co-operation in air transport. The states are more concerned about their own airlines than a common European air transport policy. Nevertheless, the Community has taken measures to try to improve the European air transport system.

It has studied the system and has proposed solutions that would benefit the Community as a whole. Furthermore, it has urged member states to implement the proposed policy. A liberalization of the European air transport system will stand a better chance to be implemented if all states do it at the same time. This does not only concern the states but also the airlines, that must be given the opportunity to take initiatives.[5]

In 1961 the European Parliament set out a policy that was aiming at an integration between air transport and other modes of transportation. The policy wanted to establish: low tariffs, progressive abolition of state aids, formation of prices on the basis of costs, orderly competition between airlines, freedom of action for airlines, neutrality as between airlines and as between modes of transport, predominance of a world solution over a Community solution.[6] As we will see, most of these proposals are still advocated by the European Parliament and EEC. The first four proposals have also been implemented. That was easily done at the beginning of the sixties when international air transport grew steadily.

With the crisis in aviation starting in the middle of the seventies, EEC became more active with attempts to solve

the problems of European aviation. Study groups and commissions were established. I will give a summary over proposals and actions taken by the EEC and any of its bodies. The European Commission, which act as a civil service staff to the EEC, has studied the issues of fares and airline competition. In 1979 it issued a memorandum entitled «Air Transport: A Community Approach». Included are four goals as follows:

1) a total network unhampered by national carriers with efficient services beneficial to the different user groups, at prices as low as possible without discrimination;

2) financial soundness for the airlines, a diminution of their costs of operation and an increase of their productivity;

3) safeguarding the interests of airline workers in the general context of social progress including elimination of obstacles to free access to employment; and

4) improvements in conditions of life for the general public and respect for the wider interests of our economies and societies.

The goals are to some extent in conflict with each other. The interests of the employees is part of what caused European airline productivity figures to be far lower than in the U.S.A. But cutting costs through work force reductions would be political suicide. The Commission also emphasized an overall European policy and co-operation between the states.[7]

The Transport Commission of the EEC has made extensive studies over the past years in the field of European air transport policy. In the progress of its work it publishes reports

and proposals that do not necessarily reflect the opinions of the Community. One of these reports from 1981 advocates, apart from technical co-operation:

1) the Community should co-operate more with international aviation bodies like ECAC and ICAO;

2) facilitate regional aviation. This proposal has always been criticized by transport trade unions and railways. A more thorough examination of regional aviation will be made in Chapter 13; and

3) tariff matters should be dealt with by those who are most fitted to do so, like IATA, and they should also be regulated through bilateral agreements.

As mentioned, the Commission does not always reflect the views of the Community. As a matter of fact, there are various opinions in the Community and among member states on how to regulate the European aviation system. That is why there is no practical results so far in the liberalization of the system. The EEC has taken a careful approach and only adopted some resolutions urging the member states to comply with free-trade principles in establishing air fares to increase the competition between airlines.[9]

The most comprehensive proposal was made by the Commissioners of the EEC in February 1984. The proposal would relax fare and capacity restrictions, limit pooling and forbid governmental aid to the national carriers. The proposed «Common Air Transport Policy» has to be approved by the transport ministers of the member states.[10] The reason for this proposal was that

the European Parliament filed charges with the European Court of Justice alleging that EEC violated the EECT by not deregulating air transport, since the treaty requires free competition also in air transportation as well as in other commercial activities.[11]

The Common Air Transport Policy meets the demands of the treaty without having full deregulation like in the U.S.

The main elements of the Commissioner's proposal include:

- Governmental aid to airlines will be forbidden, apart from when it is a matter of special circumstances, such as subsidizing a newly emerged airline;
- Governments will not be able to require airlines to participate in pooling as a condition of granting routes. They may, however, allow the airlines to establish pools. Capacity limitations are only permitted if both states agree, and can not be imposed as a condition of granting traffic rights. The proposal encouraged fare zones, in which proposed fares would automatically be approved.

Again it must be stated that - as the Association of European Airlines does - the basic problem is to lower the costs. And as mentioned in Chapter 7, the governments are responsible for most of the airlines costs. Thus, deregulation is good, but the airlines must have a chance to make full use of an eventual deregulation.

As we can see now, the position of the individual states in Europe is restrictive. The most important aviation state in Europe-United Kingdom - is supposed to be the most liberal even

though it is more restrictive than the U.S.[12] As all other European states, the U.K. has a strict control over its airlines,[13] but, nevertheless, it wants a certain liberalization and orderly deregulation.[14]

This policy is, however, not confirmed by its practice. In 1979 the U.K. concluded bilateral agreement with Sweden,[15] which is very restrictive. It only provides for third and fourth freedom traffic, Art. 2 and section 1, and the tariffs are to be established according to the International Agreement on the Procedures for the Establishment of Tariffs for Scheduled Air Services from 1967, Art. 8, which is regarded as hampering liberal tariff innovations. The capacity provisions resemble the Bermuda I capacity provisions, Art. 7.

One might think that the agreement was forced upon the U.K. by a protectionist Sweden. However, Sweden regards itself as being liberal minded and uses Bermuda I type agreements. In recent years, however, it has been forced to make concessions due to a widespread protectionism. The basic concept for Sweden in bilateral negotiations is now mirror reciprocity including predetermination of capacity. Tariffs are to be regulated according to the 1967 International Tariff Agreement. Sweden is, moreover, reluctant to force its airline to enter into pooling agreements. In matter of the liberal trends implemented by the U.S., FRG, Belgium and the Netherlands, Sweden has for the moment taken a careful approach.[16]

10.1.1 Impact of the EEC Treaty on European Air Transport

As mentioned in Chapter 10.1, the European Parliament has filed charges with the European Court of Justice alleging that EEC violated the EECT by regulating air transport which is supposed to be left to market forces.[17]

There are different opinions whether the EECT governs air transport activities and if that is the case, is the present air transport system violating the EECT.

Weber argues[18] that air transport enterprises are not regarded as pure public utilities in the EECT, meaning that they have not a protected position in matter of competition and, therefore, can not invoke Art. 90.2 of the Treaty which reads:

> «Any enterprise charged with the management of services of general economic interest or having the character of a fiscal monopoly shall be subject to the rules contained in this Treaty, in particular to those governing competition to the extent that the application of such rules does not obstruct the de jure or de facto fulfilment of the specific tasks entrusted to such enterprises. The development of trade may not be affected to such a degree as would be contrary to the interests of the Community.»

Since air transport is here regarded as an activity with the usual rules of competition applicable, the price fixing through IATA can be considered as being against the rule of competition in EECT Art. 85.3. That article reads as follows:

> «Nevertheless, the provisions of paragraph 1 (competition rules) may be declared inapplicable in the case of:
>
> - any agreements or clauses of agreements between enterprises;

- any decision or classes of decisions by associations of enterprises; and

- any concerned practices or classes of concerned practices which contribute to the improvement of the production or distribution of goods or to the promotion of technical or economic progress while reserving to users an equitable share in the profit resulting therefrom and which:

  a) neither impose on the enterprises concerned any restrictions not indispensable to the attainment of the above objectives; and

  b) nor enable such enterprises to eliminate competition in respect of a substantial proportion of the goods concerned.»

But, Weber continues, the price fixing is linked to the task given, by law, to the airlines to perform services. It is a condition under which the route concessions for the scheduled airlines are granted, especially with reference to the International Tariff Agreement 1967.

Aviation can not be understood as being a task in the sense of Art. 90.2 of the EECT. But, one can argue that to fulfill their task of rendering air transport services, the airlines must be able to fix prices through IATA, otherwise the fulfilment of the task would be obstructed. Furthermore, full application of EECT rules would lead to non-IATA price-fixing, no governmental subsidies and free competition. But the system would also be limited to the Community which would not be favoured by third states.

Salzman argues, on the other hand, that the price fixing system[19] of IATA is not consistent with Art. 85.3 EECT because the essential element of competition - price - is missing. However, Art. 90.2 could be an escape clause, if the airlines were regarded as having a special task to fulfill according to said article.

The non-application of the EECT to European air transport is argued by Pallott.[20] He means that the general rules of the Treaty do apply to air transport, but they are only significant in relation to establishment and of marginal significance in relation to rules of competition, the negotiation of agreements and representation in international organizations.

Whatever the application of the Treaty is on air transport, the EEC apparently feels that there is a need for liberalization and deregulation and, thus, has started to take measures. The progress is slow, due to resistance from member states.

10.2 ECAC and ICAO Activities

ECAC has also studied the problems of European air transport and in 1982 it published a report on competition on intra-European air services.[21] The report, known as the COMPAS report, does not necessarily represent ECAC policy, but is is extremely useful.

It was used as a basis for recommendation at the 11th triennial session of ECAC in June 1982, which requested the European states to examine the possibilities for progressively

introducing some additional degree of flexibility and competition and to consider the use of the more flexible concepts described in the report.

The report suggested some possible changes of the regulatory framework. It must be more flexibility in tariff and capacity regulation and in route entrance, in order to raise the level of competition on intra-European routes. «Safety nets» must be provided for since there is different competitive capacity of the European airlines, and that the degree of liberalization that would be acceptable to governments, is not the same on all routes.

The «zones of freedom» that would be created for tariffs would look very much like the zones established in the Memorandum of Understanding 1982. A zone would be established round a reference price and all prices proposed by an airline would automatically be approved by the governments concerned. About the zones of capacity and routes, see Chapter 8.2.

These zones of freedom would be supervised by the governments under one of the following systems:

- no government intervention;
- dual disapproval;
- home state approval; and
- country-of-origin approval.

A step in the opposite direction, towards more regulation and government intervention, was taken at an ICAO conference in 1977. It was the developing countries that wanted this conference

to try to achieve what they could not achieve in IATA or through bilateral agreements. Resolutions were adopted stating that capacity should be regulated through predetermination by governments and/or airlines. The conference also agreed on more government control over both scheduled and non-scheduled air services.

However, it is doubtful whether this conference has contributed a solution to the problems of the present international air transport system. First, ICAO must be regarded as wrong forum in this matter. Second, resolutions by ICAO are not binding on the member states. Third, many important aviation states did not agree to the resolutions.[22]

CHAPTER 10: FOOTNOTES

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2. P.J. Allot, The Common Market and the Regulation of Air Transport from Aeronautical Journal July 1975, p. 308.

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4. Airline Newsletter, Aug. 15, 1979, p. 165.

5. ITA Bulletin Nr. 16, 1974, p. 373.

6. P.J. Allot, ibid, footnote 2, p. 310.

7. ATW Oct. 1980, p. 38.

8. Raymond de Goy, EEC Air Policy Takes Shape from Transport May/June 1981 nr. 3.

9. See, for example, Aviation Daily, July 20, 1981, p. 4; AWST Nov. 14, 1983, p.

10. AWST Jan. 30, 1984, p. 28.

11. AWST Jan. 31, 1983, p. 30. I will deal with the impact of the EECT on European Aviation in Chapter 10.1.1.

12. The Economist, Aug. 18, 1979, p. 5.

13. Jacques Lauriac, Air Transport Policies Regarding Public and Private Airlines from ITA Studies Nr. 2, 1979.

14. See also ITA Magazine nr. 8, Sept. 1983, France Aviation Policy. France also emphazises the public service role which is difficult to implement since Air France would rather reduce the amount of employees. About U.K.'s policy, see Chapter 8.1.3.

15. Agreement between U.K. and Sweden relating to air services 1979.

16. Kortfattad oversikt over riktmarken av principiell karaktar som for skandinaviskt vidkommande varit kursangivande vid forhandlingar om ulformningen av luftfartsvtal, 1975-08-06.

17. See also AWST Nov. 8, 1982, p. 50 and AWST July 18, 1983, p. 31.

18. Ludwig Weber, Air Transport in the Common Market and the Public Air Transport enterprises, Annals of Air and Space Law, Vol. V 1980, p. 294ff.

19. Alan Salzman, IATA, Airline Rate Fixing and the EEC Competition Rules from 2 European Law Review 1977 pp. 409-427.

20. P. Allott, The Common Market and the Regulation of Air Transport from Aeronautical Journal July 1975, p. 316.

21. Flight International, May 7, 1977, p. 1237.

CHAPTER 11: AIR TRAFFIC OVER THE NORTH ATLANTIC

The busiest air transport market in the world is the North Atlantic. Hence, many airlines want to establish air services there. The result is a market with extremely fierce competition. Every airline wants to continue their services over the North Atlantic, even if it means that they will lose money, which, as a matter of fact nearly all of the airlines are doing. The competition is especially fierce in the low-fare market.[1]

To meet the competition from charter and low-fare carriers like Peoples Express, the established airlines introduced APEX, Advanced Purchase Excursion Fare, and other discount fares.[2] There are now hundreds of different discount fares over the North Atlantic with different kinds of restrictions.

It was Lakers «Skytrain» that introduced the low fares in 1977. This event caused confusion on the market, contrary to IATA's policy of order and stability.[3]

To some extent the airlines compensate the low yields from the discount fares by increasing business and first class fares. The reason for these measures is to fight the charter competition and stimulate travel during a period of the recession.[4] IATA, thereby, changed its view that air transport over the North Atlantic should be coordinated and regulated. IATA has now accepted the rules of competition over the North Atlantic.[5]

The effect of the liberal agreements between the U.S. and Belgium, the Netherlands, and FRG is shown in Annex 1. Fares between these states are somewhat lower, especially the discount fares.

An overview of the market on the North Atlantic shows that the «open rate» situation, started by Laker, with differential pricing, has turned out to be possible and that demand for air transport was very price elastic. Contrary to fears of established carriers, low fares resulted in more traffic all around. IATA turned out to be irrelevant on the North Atlantic. Airline management has though managed to adjust to the new situation and been able to handle all the different fares.

The situation also shows that European carriers are able to cope with unpooled, uncontrolled, unregulated and unpredictable air transport, so long as they offer the services that the public wants.[6]

The Memorandum of Understanding 1982 (see Chapter 5) is another factor that has affected the situation over the North Atlantic. The U.S. wanted free competition over the North Atlantic but the European states did not agree. They wanted something in between cartel-type fares and free competition so they established the Memorandum of Understanding as a compromise.

The Memorandum also helps relations between the U.S. and states critizising the U.S. for unilaterally forcing deregulation on unwilling states.[7]

Moreover, the Show Cause order, preventing American carriers from taking part in North Atlantic ratemaking conferences, was

not implemented due to the Memorandum. The Memorandum has given the governments more to say about fare setting since they decide the limits of the fare zones. The role of IATA in fare setting on the North Atlantic has thus declined.[8]

The governments will be involved even more in the fare setting, because the airlines are, due to competition, forced to set the fares below the zone limit, which means they have to go through the usual procedures to achieve governmental approval of their fare proposals. The Memorandum has set a trend in international fare setting policy with more flexibility, but still governmental control. It is exemplified with the proposals from ECAC and EEC, about intra-European fare policy, which are similar to the Memorandum. It must be pointed out though that the Memorandum did not have any affect on Belgium, the Netherlands and FRG and their traffic over the North Atlantic, since they had already concluded their liberal bilateral agreements with the U.S.

CHAPTER 11: FOOTNOTES

1. Aviation Daily April 1983, p. 13.
2. AWST June 27, p. 30 and AWST May 2, 1983, p. 26.
3. Flight International Aug. 13, 1977, p. 465 and AWST Aug. 22, 1977, p. 32.
4. Aviation Daily Feb. 1983, p. 38.
5. Airline Newsletter, April 15, 1977, p. 231 and AWST Nov. 14, 1977, p. 29.
6. A Lowenfeld, Deregulation - Is it Contagious? from International Air Transport in the Eighties, p. 29f.
7. Aviation Daily June 5, 1981, p. 2.
8. ATW Dec. 1983, p. 18.

CHAPTER 12: CHARTER

The relationship between scheduled services and charter services is one of the most urgent problems in the field of regulatory policy. There is a sharp conflict between individual and collective demand on the air transport system. Hence, a need for regulation.

Scheduled services are essentially a collective demand and charter services an individual demand. Without some kind of regulation the growth of charter operations in many markets would lead to a decline in scheduled services.[1]

This statement has proven to be true on the intra-European market where charter services take care of 50% of all passenger km.[2] Charter services also increased over the North Atlantic during the seventies, due to the liberalization of charter rules, which has blurred the distinction between charter and scheduled services. A lot of different charter concepts were introduced on the North Atlantic, beginning in the middle of the sixties. I have described the most important of them in Chapter 1.

Thus, over the years, new types of services developed which are neither scheduled nor charter services. These low cost and low fare services are performed more or less regularly in accordance with a timetable, they are open to the public and are not subject to «common carrier obligations».

There is one important distinction though. Charter services can not be offered directly by the airlines but have to

be sold through travel agencies.[3] There is not much regulation of charter. Charter is exclusively governed by unilateral actions from the governments. Only two multilateral conventions on charter have been concluded, the multilateral Agreement on Commercial Rights of Non-Scheduled Air Services among the Association of South-East Asian Nations 1971 and the Multilateral Agreement on Commercial Rights of Non-Scheduled Air Services in Europe in 1956, which I have referred to in Chapter 5. None of these two agreements have contributed much to the development of international charter traffic.

In the beginning of the seventies, the U.S. started to conclude bilateral agreements that included regulation of charter services. It was on the basis of the 1970 Nixon statement.[4] Bermuda II was the first bilateral with this arrangement that took the form of a temporary memorandum of understanding on non-scheduled air services or a bilateral non-scheduled air services agreement.[5] The bilateral agreements between the U.S. and Belgium, FRG and the Netherlands all contain provisions about charter. These actions are all in line with the suggestions given by different authors during the seventies implying that the concepts of charter and scheduled services should be regulated together.

Bernard Wood argues[6] that the same rules should be applicable to both kind of services with the implication that limitations should be imposed to protect charter from the market powers of scheduled services and to protect scheduled services

from the price advantage of charters. Airlines operating scheduled services should also be able to make room for charter passengers on the same flight to fill up the aircraft. E. Driscoll[7] has four recommendations about the relationship between scheduled and charter services:

1) country-of-origin approach for charter;
2) bringing scheduled capacity in line with demand;
3) the restructuring of IATA rather than its elimination; and
4) that both scheduled and charter airlines listen to what the travellers are saying.

It is obvious that the trend is heading towards a closer relationship between scheduled and charter services. In the future these two concepts may be regulated and defined in the same manner. We must though remember that there are different charter services. There still exists pure charter flights where, for instance, a group of persons or a company hire an aircraft for one specific trip. Special rules will, of course, be applicable to that kind of service.

The European charter market is totally different from charter over the North Atlantic. Originally, European charters were themselves the product of a very high fare European scheduled system. As mentioned, the result is that charter in Europe now accounts for 50% of all intra-European traffic. This caused severe problems for the scheduled traffic and in fact, it is the wide availability of charter services in Europe that

has contributed to the current situation of high fares on scheduled services.[8] One solution could be a common (de) regulation of charter and scheduled services.

When an international system is left to unilateral actions, there is no coherence and control over the activities which in the worst cases can lead to organized protectionism.

A step in the right direction is already taken by the U.K., the U.S., Belgium, the Netherlands, and FRG when they included charter services in their bilateral agreements.

CHAPTER 12: FOOTNOTES

1. S. Wheatcroft, ibid, from Aeronautical Journal Aug. 1970, p. 624 f.

2. AWST May 30, 1983, p. 233.

3. A. Merckx, ibid, Chapter 9, footnote 12, p. 139f.

4. U.S. Statement on International Air Transportation Policy June 21, 1963, U.S. Dept. of State Bulletin at 86.

5. A. Merckx, ibid, p. 142.

6. Bernard Wood, Bilateral Agreements - A Current View Unpublished article.

7. E. Driscoll, ibid, International Business Lawyer, Vol. 9, 1981, p. 154.

8. ATW Oct. 1980, p. 46, and Jan. 1979, p. 48a.

CHAPTER 13: REGIONAL AVIATION IN EUROPE

The development of regional air transport in Europe has taken place mainly in the last ten years. Growth was slow in the beginning due to financial problems. Other major obstacles in the development was the privileged position given to the national carriers by the governments.

There have never been clear and precise regulations governing regional transport in Europe. There is no exact definition of what type of aircraft the regional carrier can use and there is no regulation about the services that can be provided. Administrative procedures are also more complicated and time consuming. There is, thus, a very unstable working base for the 30[1] commuters in Europe, taking care of about 5% of the air traffic.[2]

Before further discussion, we should give an approximative definition of a regional airline, or commuter. It can best be defined as a licensed scheduled operator, which serves the air transport needs of a particular area of a given country. Its route network can extend beyond national borders.

Despite the difficulties in the beginning, European commuters have now stabilized their operations. Rationalization, accounting discipline, a helping hand from national carriers are factors that have helped to put the commuters on a more stable footing. Especially the help from national carriers has been a major influence in the development of the commuters.

The national carriers have subcontracted services to them or provided indirect financial assistance. That is a recognition of the fact that commuters can perform certain services at much lower costs.[3]

13.1 European Regional Aviation Organization

With the goal to develop European regional aviation, the European Regional Aviation Organization - ERA - was formed in 1981. The founder of ERA, Moritz Suter believes that the determining factor for the development is that the corresponding cost structure is maintained. It is not so important what type of services they offer.

The airlines have been hesitating to join ERA though. ERA is mainly supposed to deal with long-term goals such as improving bilateral and multilateral co-operation, standardization of equipment and the drawing of an overall plan designed to encourage the harmonious development of regional air transport in Europe in order to create the basis of stability without which this sector can not continue to exist or prosper. The European commuters are, however, first interested in short-term factors such as the competition from fast trains and the national carriers. The fact that ERA is also accepting aircraft and engine manufacturers - officially to encourage co-operation between manufacturers and operators - is not seen in a very good light by all the regional airlines.[4]

13.2 Opportunities For, and Restrictions On, European Regional Aviation

Regional airlines have to compete not only with the large, established carriers, but also to a high degree with a well built road transport and railway system.

The commuters' advantage over ground transport is speed. However, since commuters operate only on short-haul routes, the advantage is not so great. Hence, the time the passengers spend on the ground must be as short as possible. Moreover, airports used by commuters must be sited close to the city, which is possible in matter of noice aspects, since most aircraft use propeller engines which are not so noisy as jet engines. It is when the flight is over mountains or water when the time gained is considerable.[5]

Commuters have become a compliment to the large carriers, since it is too expensive for large carriers to operate on short-haul routes due to the type of aircraft they use. The commuters use much smaller and fuel efficient aircraft.

Feeder services are the most attractive types of services for commuters. The airline is then operating between smaller cities - not served by the big airlines - and the large hubs where the traffic is taken care of by the big airlines. To only operate between smaller cities is not profitable enough since there is not enough traffic.

The problem is that most European routes only connect capitals and larger cities and they are only served by the

national carriers. The European governments are very reluctant to permit commuters operating from big hubs.[6] The commuters are, thus, left to serve smaller cities where they are not competing with the national carriers. Hence, there are disputes about what type of airports and cities commuters can serve. Three different categories of airports have been defined, as follows:

Category 1 - is principal airports;

Category 2 - is major provincial airports;

Category 3 - is other airports.[7]

Governments are not willing to let commuters serve routes between category 1-1, 1-2 and 1-3 since those services would compete with flag carriers. To the detriment of the commuters, the governments work to protect the revenues of the flag-carriers and to do this they keep ticket prices up and restrict capacity and cross-border operations for commuters.

Another chief obstacle is the international law that gives the states the control over its airspace and commuters can not thrive in it unless the states support legislation favourable to their existence.[8]

As we can see there is resistance against commuters because some believe that there is no room for them. Moreover, the present financial situation of the flag-carriers is so bad that more competition would harm them to the disadvantage of the public. The commuters will also have severe financial difficulties due to the unprofitable routes they serve. The

airlines will, therefore, abandon the services to the detriment of the travelling public.[10] But this is not true. If the public wants the regional services, it will continue to use them and thus keep the commuters profitable.

As mentioned in the previous chapters, there seems to be a tendency towards liberalization of the European air transport system. This trend has also affected regional aviation and there is proposals from scholars, governments, EEC and ECAC how to facilitate regional aviation in Europe. The role of future regional air transport will be dependent on the attitude of a large number of parties - or of conflicting parties,[11] as follows:

- national civil aviation authorities which may be, to a greater or lesser extent, liberal or restrictive towards commuters;
- agencies other than civil aviation departments such as Department of Transport, regional development, trade development and finance agencies;
- international organizations which to a greater or lesser extent support liberalization of inter-regional air transport;
- the national carriers which see their operations threatened;
- competing transport media; road and railway;
- regional authorities capable of financing the creation and/or operation of air networks involving their region; and
- aircraft manufacturers whose projects will be influenced by the attitudes taken by the different parties.

Despite resistance, especially from the national carriers, there is a degree of optimism among some of the commuters. It stems from the potential of regulatory reforms among European states as well as from increasing patterns of co-operative efforts between commuters and larger airlines such as the co-operation between Crossair-Swissair and Swedair-SAS.

There is a movement to bring about regulatory reforms in Europe and advances made in this area are expected to have a positive impact on regional airlines. Studies are made by ECAC and EEC in this field. Such reforms would create opportunities for commuters to develop their international flights and provide them with better access to important markets.

The best way for commuter airlines to develop in Europe is to allow them to fly time conscious and relatively price insensitive business passengers from an airport near their home, over geographical obstacles of waters and mountains or distances where train can not compete, to the city where they want to do business that day.[12] It will though take quite a while before the European states agree to such a liberal system for commuters. However, there is a tendency that smaller steps will be taken to liberalize regional aviation. An initiative was taken by the Commission of the European Communities in November 1980 to regulate the operation of certain regional air services. The aim would be to set up an inter-regional network based on secondary markets with inadequate services. The

objectives of the proposal would open up markets, create flexibility in regulations and lower fares. The result should be growth in local and regional air transport to the benefit of existing or new carriers, major airports, which will be less congested, and to the users through extended public services.

The services regulated in this manner would operate on categories 1-3, 2-2, 2-3 and 3-3. The minimum stage length would be 200km except where considerable time could be gained due to geographical situation. The aircraft would have a maximum capacity of 130 seats or a maximum take-off weight of under 55 tons and services would be scheduled.

The proposal met, of course, resistance from national carriers, but also from governments, afraid of embarking on a multilateral system with inadequate or ambiguous provisions.[13] If the proposal is adopted, the services mentioned would be regulated multilaterally and fall outside the scope of bilateral agreements.

Another proposal worth mentioning is one that advocates the introduction of «shuttle service», like NLM's city hopper with on board ticketing[14] and also the proposal that would facilitate services with documents and small parcels.[15]

The proposal from the Commission of the European Community has to be approved by the Council of Transport Ministers. However, in the final directive there are amendments to the Commissions proposal that limit the liberal approach taken by the Commission.

The original proposal allowed services between airports of category 1-3 to exist outside the scope of bilateral agreements. The final directive only provides for services among category 2 and 3. Contrary to the original proposal, the directive does not provide for all-cargo or mail services. The types of aircraft to be used are smaller than originally proposed. The maximum seat capacity will only be 70 seats and the maximum take-off weight will only be 30 tons. According to the directive, airlines still have to apply for permission to exercise fifth freedom rights. The directive also restricts the extra-bilateral licensing of Community regional air services. The directive also doubles the minimum distance for extra-bilateral services to 400km.

ERA sees these limitations as unnecessary and restrictive. Nevertheless, it must be seen as an important step forward politically - it is the first time air legislation produced by the Community. The largest impact of the directive is that fares are now allowed to be cost-related for commuters. They do not have to charge the same high prices as the national carriers do. The fares will be «air carrier determined» instead of government determined.[16]

To summarize the situation of European regional aviation, it is still restricted by the governments due to their protection of the national carriers. This protection is the largest obstacle for the development of European regional aviation.

The directives adopted by the Commission of the European Communities are not liked by the ERA because it feels the directive is too restrictive. It will not improve European regional aviation to any greater extent. However, it is a step in the right direction and it will most likely be further liberalization in the future.

CHAPTER 13: FOOTNOTES

1. For a detailed list over all European regional air lines, see Interavia March 1979, p. 249.
2. AWST Nov. 8, 1982, p. 56.
3. Interavia, March 1979, p. 247.
4. Interavia, July 1982, p. 710.
5. R. Le Goy, ibid., footnote 3, Chapter 10.
6. AWST Aug. 15, 1983, p. 40.
7. Shelag Roberts, Royal Aeronautical Society's Air Transport Symposium London 1981.
8. See e.g. ATW Aug. 1982, p. 87 and ATW Jan. 1984, p. 74ff.
9. AWST Oct. 10, 1983, p. 44.
10. ITA Bulletin nr. 42, 1981, p. 936.
11. ITA Monthly Bulletin June 1982 «Regional Air Service»
12. AWST Oct. 10, 1983, p. 44.
13. ITA Bullentin nr. 10, 1981, p. 242 and ATW Aug. 1982, p. 87.
14. Aerospace June/July 1975, p. 17.
15. Aerospace Jan. 1980, p. 17.
16. For further Comments see Flight International July 2, 1983, p. 4.

CONCLUSION

In previous chapters, I have given a view over the present stage of European air transport and its different aspects. There seems to be a tendency towards regulatory changes in Europe. Most authors agree that some deregulation and liberalization of the present bilateral - and in case of charter, unilateral - system in Europe has to be made. The dispute concerns mainly how and to what extent the liberalization should be exercised.

As we know, the present system has worked without major changes since the introduction of Bermuda I. The system obviously has advantages since it has been working for such a long time. The traffic has grown steadily, fares are relatively lower now than before. Every European state has managed to develop an international airline having to subsidize them other than during the first years of operation. So the question is, is there a better system for both the airlines and the travelling public.

There has been two attempts, 1944 and 1947, to establish an international convention on commercial air transport. Both failed. According to Hammarskjold a much more flexible system was produced instead-a system of bilateral agreements between governments with inter-linking remote control through their respective flag carriers.[1] Hammarskjold continues, that governments had a need to obtain the optimum advantages from every route concession which would only be possible through bilateral ATA.

So far there is no multilateral agreement established that mitigate the disadvantages with bilateral agreements, without requiring individual states to sacrifice the advantages. Only recently is there a plurilateral proposal in these matters which I will deal with later.

IATA has played a crucial role in achieving many of the objectives contained in a multilateral system. IATA has acted as a multilateral link between the bilateral agreements. It is clear, according to Hammarskjold, that had there not been this loose form of multilateralism, the system today would have been very different from the one hoped for.

The system is, of course, not perfect. Wessberge argues[2] that the system is ill-adapted to air transport's universal role since it does not perfectly meet the objective of optimum reciprocity sought by pairs of partners and it is detrimental in various ways to the users. However, Wessberge concludes that there is no better existing system.

Another point is that the international air transport market is not only located between the two parties concluding a bilateral agreement. In the international context a market is not a service point in the narrow, technical sense of the word. It is a complex whole, subject to various factors: traffic flows, government agreements, the state and impact of competition. The result is that balanced participation in air services between bilateral partners is an uncertain business, with no possibility to regulate capacity and use pools in a

perfect way. Another argument in favour of the bilateral system is the introduction of the liberal bilateral agreements concluded by the U.S. They exemplify the flexibility of the bilateral system by the fact that they are different from earlier bilateral agreements and that they provide various possibilities in setting of fares and providing of capacity. Bermuda I has served as a model for a large number of agreements in the world. Hence, it provides a coherence among all the bilateral agreements. If there should be a deregulation of international air transport system, all bilateral agreements have to be changed in the same manner and at the same time or a multilateral air transport convention must be established.

The U.S. has tried to promote their competition philosophy through unilateral actions without multilateral consultations.[3] The passenger rich U.S. is using this bargaining tactic towards smaller states since the U.S. can prevent substitution of alternative routes. Airlines of smaller states are dependent on the big American market. KLM, for instance, would suffer enormously if traffic between the Netherlands and the U.S. was cancelled. For the American carriers it would not matter so much, because they can carry traffic from the U.S. to London, Frankfurt or Brussels, from where the travellers would go on to the Netherlands. The U.S. has been exploiting this weakness of its negotiating partners by seeking liberal agreements with selected, strategically situated states, to put maximum pressure on neighbouring states to conclude similar agreements. The

Benelux states in Europe and Singapore in Asia have served as such wedges to promote U.S. aviation policy.[4]

Whether this U.S. policy will be successful is difficult to say. If the European states believe the liberal trend is going to far, they probably will organize and apply a common more restrictive policy towards the U.S.

I think that we can conclude that an eventual deregulation in Europe can not be achieved through a multilateral convention but has to be achieved within the framework of bilateralism.

Even in Europe, there are different environments and markets. Different social, political and economic factors determine the air transport policy of a state, which implies different opportunities for the airlines to operate, e.g. the public service role can be more emphasized in certain states with the obligatorium for the flag-carrier to serve low density routes.[5]

What we are talking about here is the core of the bilateral agreements; tariffs, routes and capacity. Technical and administrative procedures are naturally easy to agree upon in a multilateral convention. We have come to a point where we can propose a solution to how an eventual liberalization and deregulation of the European air transport system would look like. It must be an organized multilateral deregulation in the framework of the present bilateral system.

The approach has been advocated by the International Chambers of Commerce, ICC.[6] In its statement, ICC considered

a new contractual system in the framework of a multilateral agreement within which bilateral agreements could be negotiated. The main principles would be compliance with market mechanisms, a minimum of government intervention and no excessive financial costs to be imposed on airlines for national political reasons. The approach would be gradualism without procrastination meaning that a solution is urgent but that it is necessary to proceed slowly and in stages.

A very extensive proposal similar to ICC's ismade by representative from the Dutch authorities and from KLM. It is called the «Plurilateral Air Transport Agreement» PATA.[7]

Their definition of plurilateralism is: «co-operation between more than two states irrespective of their geographic location, but not encompassing a majority of world states. The term plurilateral was preferred to multilateralism to indicate that the aim was to include some variants of bilateralism within a multilateral regulatory framework. In other words, to combine the two systems in response to the differences in situations and to permit the progressive and orderly development of this plurilateralism.[8] Plurilateralism is supposed to link states together with the same private approach towards their airline's interest and operations.

Member states of the PATA shall, when concluding a bilateral agreement with another member state, include the provisions given in the PATA. They can naturally provide for even more liberal arrangements than the PATA is providing for. The PATA is essentially a combination of different bilateral agreements.[9]

When fifth freedom traffic rights are granted in a bilateral agreement, it is not sure that the airline that has received this right, can exercise it due to restrictions from third country. The PATA solves this problem by giving complete freedom for third, fourth, and fifth freedom traffic rights, but only between members of the PATA.

The PATA can be a step towards gradual liberalization of international air transportation through a step-by-step approach. Special arrangements can be agreed upon between parties bilaterally so long as they are not more restrictive than the provisions in the PATA.

The essential objectives of the PATA is to promote responsible, efficient and economic airline operations under non-discriminatory conditions with an optimum benefit for the users of air transportation. Thus, a sort of cabotage rights for all designated airlines between the territories of the member states. This freedom is expressed in Art. 11 of the draft proposal - «Fair competition». Pricing is supposed to be left entirely to the airlines. However, if a party is dissatisfied with a fare, it can require consultation with the other party, Art. 12.1.b.ii.

Essential elements in the PATA are fifth freedom traffic, tariff freedom, route freedom and capacity freedom, charter freedom and fair competition. The built in mechanism to arrive at these freedoms gradually, by concluding bilateral agreements within the framework of the PATA, makes the PATA a flexible

instrument for progressive liberalization of international air transportation. This flexible and pragmatic approach is highlighted by the provisions in the PATA which authorizes member states to deviate between them from the PATA, if they agree that their specific bilateral relations so require, as long as the interests of other parties to the PATA are not affected thereby. With the PATA, the shortcomings of bilateral agreements are overcome at the same time as the states sovereignty and control over their territories are maintained.

The Netherlands has proposed the draft PATA to the U.S. since the U.S. is the most important aviation state and for the reason that the draft is similar to the U.S.-the Netherlands, ATA.[10] It has not yet been reached an agreement.

The plurilateral proposal was criticized by the former U.S. State Department Expert, James Atwood at the Amman Conference on «Regionalism in International Air Transport» on 19-21 April 1983.

Instead of creating a snowball effect, the formula would rather resemble a spider's web. For example, state A, after concluding a PATA with B, might try to obtain substantial advantages from third states by holding out the possibility of extending the PATA to them. They have to accept the whole agreement if they want to implement it. Hence, only A, promoting the PATA has a veto right. The PATA would, thus, be used by A as a bait without its partner B being able to intervene - which would be a warped form of bilateralism. Additionally,

if A is a minor market and B is a major market, B loses out in the exchange system set up by the bilateral model. Moreover, third states would probably prefer to keep the advantages acquired with B in their respective bilateral agreement: there would, thus, be a return to bilateralism, with plurilateralism and multilateralism being checked.

The criticizm is mainly focused on details which can be changed. Thus, if the European governments really want a liberalization and deregulation of the European air transport system, a system containing the PATA is worth discussing.

CONCLUSION: FOOTNOTES

1. Knut Hammarskjold, ibid, footnote 1, Chapter 9, p. 145.

2. ITA Bulletin nr. 32, 1981, p. 823.

3. E. Driscoll, Deregulation - the U.S. Experience from International Business Lawyer Vol. 9, 1981, p. 158.

4. Christer Jonsson, ibid, footnote 4, Chapter 9, p. 299.

5. ITA Bulletin nr. 12, p. 288, 13 p. 319 and 32, p. 823.

6. ICC, Air Transport Committee, Session of Feb. 17, 1981 Doc. nr. 310/NT 139.

7. It is presented by H. Wassenbergh and K. Veenstra in International Air Transportation in the Eighties, p. 205-221.

8. H. Wassenbergh, The Future of Multilateral Air Transport Regulation in the Regional and Global Context from Annals of Air and Space Law, Vol. 8 1983, McGill Univ. Montreal, p. 272.

9. For the full text of the PATA, see Annex 2.

10. AWST Nov. 3, 1980, p. 49.

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ICAO Doc. A24-WP/62 EC/13 23/9/83

ICAO Doc. 7107-12, C1823-12 and 55

ECAC Press Release Nr. 54E 5/5/82

DOC ECAC/Int. 5/8 Annex Doc. ECAC/9 Report p. 87, Memorandum of Understanding on North Atlantic Charter

ECAC Doc. 25 1982

U.S. DOS Bulletin Vol. LXVIII No. 1749 1/1 1973, p. 20 et seq., «The Ottawa Declaration» on Non-Affinity Charter Between Europe and U.S.A.

U.S. DOT 14-82 May 3, , 1982

ICC, Session of Feb. 17, 1981, DOC Nr. 310 INT 139

BILATERAL AIR TRANSPORT AGREEMENTS

Agreement between USA and Belgium TIAS 9903, 1980

Agreement between USA and New Zealand TIAS 9956, 1981.

Agreement between USA and Israel TIAS 9002, 1978

Agreement between USA and FRG TIAS 9591, 1978

Agreement between USA and U.K., U.S. DOT Washington, D.C. 205 90 July 23, 1977 (Bermuda II)

Agreement between The Netherlands and USA, Tractatenblad van het Koninkrijk der Nederlanden Jaargang 1978 nr. 55

Agreement between UK and Italy for air services between and beyond their respective territories, 1976

Agreement between UK and Sweden relating to air services 1979.

ANNEX 1

DOMESTIC US - INTRA-EUROPEAN - AND NORTH ATLANTIC FARES AS OF JANUARY 1984

Fares Over the North Atlantic

	Economy Fare	Lowest Fare
New York-London	550	150
New York-Frankfurt	697	395
New York-Brussels	542	170
New York-Amsterdam	566	330
New York-Stockholm	680	565
New York-Paris	PA-619, TWA-705, AF-747	593
New York-Rome	711	659

Domestic US Fares

	Flight Time	Economy Fare	Lowest Fare
New York-Dallas/Fort Worth	2,5h	300	210

Intra-European Fares

	Flight Time	Economy Fare	Lowest Fare
London-Stockholm	2,5h	460[1]	281
Paris-Helsinki	2 h	421	337
Amsterdam-Rome	2 h	318	337
Brussels-Madrid	2 h	284	256
Copenhagen-Zurich	2 h	279[2]	251
Athens-Madrid	2,5h	474	251
London-Vienna	3 h	324	304
Stockholm-Paris	2,5h	432	272
London-Copenhagen	2,5h	350	215

[1] London-Copenhagen 350

[2] Stockholm-Zurich 393

II. Text and comments*

DRAFT PLURILATERAL AIR TRANSPORT AGREEMENT

ARTICLE 1

Definitions

For the purposes of this Agreement, unless otherwise stated, the term:

a) 'Aeronautical authorities' means, in the case of any party, any person or agency notified by that party as having jurisdiction over air transportation;

b) 'Airline' means any enterprise performing air transportation;

c) 'Air transportation' means any operation performed by aircraft for the public carriage of traffic in passengers, baggage, cargo and mail, separately or in combination, for remuneration or hire;

d) 'Convention' means the Convention on International Civil Aviation opened for signature at Chicago on December 7, 1944, and includes:
(i) any amendment thereto which has entered into force under Article 94(a) thereof and has been ratified by the parties concerned, and
(ii) any Annex or any amendment thereto adopted under Article 90 of that Convention, insofar as such Annex or amendment is in force for the parties concerned;

e) 'Designated airline' means an airline designated and authorized in accordance with Article 3 (Designation and Authorization) of this Agreement;

f) 'Party' means any state for which this Agreement is in force;

g) 'Price' means any amount charged or to be charged by airlines, directly or through their agents, to any person or entity for the carriage of passengers (and their baggage) and cargo (excluding mail) in air transportation, including:
(i) the conditions governing the availability and applicability of a price; and
(ii) the charges and conditions for any services ancillary to such carriage which are offered by airlines;

h) 'Territory' means the land areas, and the territorial waters adjacent thereto, over which a state exercises jurisdiction in matters of air transportation;

i) 'This Agreement' means this Agreement, its Annex(es), and any amendments thereto, insofar as any such amendment is in force for the parties concerned;

j) 'User charge' means a charge made to airlines for the provision at any given time of any specific airport, air navigation, or aviation security, property or facilities.

In the Chicago Convention (art. 96) the term 'airline' exclusively refers to the operator of scheduled air services. Since the PATA intends to cover any type of commercial public carriage by air, including so-called charter flights (see also the definition of the term 'air transportation' in conjunction with Section 2 of Annex 1), a broader definition of the term 'airline' has been inserted in this Article. However, the inclusion of charter air transportation in the PATA does not extend to the relation

* *The comments are provided, where appropriate, under each article in italics.*

between the charterer and the public, because the PATA addresses itself to the activities of the direct air carrier only. Hence, the definition of the term 'price' includes the wholesale but not the retail price for charter air transportation.

The terms 'scheduled' and 'non-scheduled' have not been defined, if only because there is no general worldwide agreement on their precise meaning. Moreover, such definitions would have been relevant only in respect of the air transport relations between PATA members and non-PATA states. In respect of air transportation between PATA members the distinction between 'scheduled' and 'non-scheduled' by one of them has no implications for the airlines of the other members (see also the comments under Annex 1).
The definition of the term 'user charge' envisages that such charges may vary depending on the airport used and on the time at which the services in question are provided.

ARTICLE 2

Grant of Rights

1. Each party shall have the rights specified in this Agreement in respect of international air transportation by its airline(s).
2. Nothing in this Agreement shall be deemed to grant the right for the airline(s) of any party to participate in cabotage air transportation within the territory of any other party, except that, as from the date on which Annex 2 to this Agreement ceases to apply, such airline(s) shall be entitled to participate in such transportation within the territory of any other party if:
   a) the national law of that other party permits it to allow (an) airline(s) other than its own airline(s) to participate in such transportation within its territory, and
   b) the party of which such airline(s) is (are) a national allows participation in cabotage air transportation within its territory by the airline(s) of that other party.

It is common practice for states to reserve cabotage air transportation for their own airlines. In article 7 of the Chicago Convention this is even explicitly permitted. However, since the PATA seeks to promote efficiency and fair competition in air transportation, its members should in principle be prepared to grant each other's airlines cabotage rights on their international air services operated pursuant to the PATA. In fact, if an airline of a state serves two or more points in the territory of another state on the same international flight, it is normally in a position to utilize part of its capacity for the carriage of local 'fill-up' traffic between such points. Without the right to carry such traffic, the airline concerned operates less efficiently, while it has a competitive disadvantage if an airline of that other state operating an international service on the same route is permitted to exercise such local 'fill-up' rights.

However, in various states the grant of cabotage rights to foreign airlines requires a change in the national law. It would be impractical to make such change a prerequisite of PATA membership. Moreover, states need sufficient time to realize such change and cannot be expected to grant any cabotage rights to foreign airlines without adequate reciprocity.

In view thereof paragraph 2 of this Article envisages a reciprocal grant of cabotage facilities only if, at the end of the transitional period defined in Annex 2, the national law of the PATA member concerned permits it to allow such facilities. As long as its national law does not so permit, a PATA member may at least be expected to avoid an unduly restrictive interpretation of the term 'cabotage'. To this end PATA members should consider the origin/destination of the traffic (as evidenced by the document of carriage) and not the points of uplift/discharge as the decisive cabotage criterion. In other words, only the carriage of purely domestic traffic should be classified as 'cabotage air transportation'.

ARTICLE 3

Designation and Authorization

1. Each party shall have the right to designate as many airlines as it wishes for the conduct of international air transportation pursuant to this Agreement and to withdraw or alter such designations. Such designations shall be transmitted in writing through diplomatic channels to any other party to or from whose territory such transportation is to be performed.
2. On receipt by a party of a designation and of applications from the airline(s) so designated for operating authorizations and technical permissions, in the form and manner prescribed for such applications, that party shall grant appropriate authorizations and permissions with a minimum of procedural delay, provided:
   a) substantial ownership and effective control of that airline are vested in the party which has designated that airline or in nationals of that party or in both, and
   b) that airline is qualified to meet the conditions prescribed under the laws and regulations which the party considering the applications normally applies to the conduct of international air transportation, provided such laws and regulations are not inconsistent with this Agreement or any of its provisions; and
   c) the party which has designated the airline is maintaining and administering the standards set forth in paragraph 2 of Article 6 (Safety) of this Agreement.

Multiple designation, in which some states have an immediate and understandable interest, is not an 'absolute' right under the PATA. Like the other air transportation opportunities specified in the PATA, multiple designation should be used by PATA members in a manner which is consistent with the purposes of the Agreement, notably those set out in paragraph 1 of the Article on 'Fair Competition'. If a member in a specific case wishes to object to multiple designation on the ground that it is inconsistent with those purposes, nothing prevents that member to resort to consultations and arbitration. Moreover, a PATA member preferring single designation on a route can at any time propose to the other member concerned to conclude between them a special agreement to that effect which will override the multiple designation provision contained in paragraph 1 of this Article (see paragraph 3 of the Article on 'Entry into Force'). During the transitional period a PATA member can even without such special arrangement maintain the single designation provisions of the bilateral agreement concluded with another PATA member and in force between them on and before the date that both of them become PATA members (see Section 5 of Annex 2).

ARTICLE 4

Revocation or Suspension of Operating Authorization

1. Each party may revoke, suspend, or limit the operating authorizations or technical permissions of an airline designated by any other party in the event:
   a) substantial ownership and effective control of that airline are not vested in that other party or in that other party's nationals or in both; or
   b) that airline has failed to comply with the laws and regulations referred to in paragraphs 2 and 3 of Article 5 (National Laws and Regulations) of this Agreement; or
   c) that other party is not maintaining and administering the standards as set forth in paragraph 2 of Article 6 (Safety) of this Agreement.
2. Unless immediate action is essential to prevent further non-compliance with subparagraphs 1 b) or 1 c) of this Article, the rights established by this Article shall be exercised only after consultation with the other party concerned.

ARTICLE 5

National Laws and Regulations

1. Any party's national laws and regulations pertaining to any part or aspect of, or to any matter related to, air transportation performed under this Agreement shall be, and shall be applied in a manner which is, reasonable and not inconsistent with the purposes of this Agreement.
2. While entering, within or leaving the territory of any party, the laws and regulations of that party relating to the operation and navigation of aircraft shall be complied with by the airline(s) of any other party.
3. While entering, within or leaving the territory of any party, the laws and regulations of that party relating to the admission to or departure from its territory of passengers, crew or cargo on aircraft, including regulations relating to entry, clearance, aviation security, immigration, passports, customs and quarantine or, in the case of mail, postal regulations, shall, in so far as such laws and regulations require compliance by airlines, be complied with by the airline(s) of any other party.

It is obvious that international air transportation performed pursuant to an international agreement like the PATA will in many respects continue to be governed by national laws and regulations of the parties. However, as stated in paragraph 1 of this Article, a party may be expected not to use its authority in this area in a manner which would be either unreasonable or inconsistent with the purposes of the PATA. By incorporating this provision in the PATA each party remains accountable vis-à vis the others for its own legislative, administrative and judiciary activities in respect of international air transportation under the PATA.

ARTICLE 6

Safety

1. Each party shall recognize as valid certificates of airworthiness, certificates of competency, and licences issued or validated by any other party and still in force for the purpose of performing air transportation pursuant to this Agreement, provided that the requirements for such certificates or licences at least equal the minimum standards which may be established pursuant to the Convention. Each party may, however, refuse to recognize as valid for the purpose of flight above its own territory, certificates of competency and licences granted to, or rendered valid for, its own nationals by any other party.
2. Each party may request consultations with any other party concerning the safety and security standards maintained by that other party relating to aeronautical facilities, aircrew, aircraft, and operations, of the airlines of these parties. If, following such consultations, the party which has requested such consultations finds that the other party does not effectively maintain and administer safety and security standards and requirements in these areas that are equal to or above the minimum standards which may be established pursuant to the Convention, that other party shall be notified of such findings and of the steps considered necessary to bring the safety and security standards and requirements of that other party to standards at least equal to the minimum standards which may be established pursuant to the Convention; and that other party shall take appropriate corrective action. The party which has so notified that other party reserves the right to withhold, revoke, or limit the operating authorizations or technical permissions of that other party's airline(s) in the event that other party does not take such appropriate action within a reasonable time.

ARTICLE 7

Aviation Security

Each party:

1. reaffirms its commitment to act consistently with the provisions of the Convention on Offences and Certain Other Acts Committed on Board Aircraft, signed at Tokyo on September 14, 1963, the Convention for the Suppression of Unlawful Seizure of Aircraft, signed at The Hague on December 16, 1970, and the Convention for the Suppression of Unlawful Acts Against the Safety of Civil Aviation, signed at Montreal on September 23, 1971; and
2. shall require that operators of aircraft of its registry act consistently with applicable aviation security provisions established by the International Civil Aviation Organization; and
3. shall provide maximum aid to any other party with a view to preventing unlawful seizure of aircraft, sabotage to aircraft, airports, and air navigation facilities, and threats to aviation security; give sympathetic consideration to any request from any other party

for special security measures for its aircraft or passengers to meet a particular threat; and, when incidents or threats of hijacking or sabotage against aircraft, airports or air navigation facilities occur, assist any other party by facilitating communications intended to terminate such incidents rapidly and safely.

ARTICLE 8

Commercial Operations

1. Each airline of any party shall be allowed:
   a) to establish in the territory of any other party offices for the promotion and sale of air transportation as well as other facilities required for the provision of air transportation, and
   b) to bring in and maintain in the territory of any other party – in accordance with the laws and regulations of that other party relating to entry, residence and employment – managerial, sales, technical, operational and other specialist staff required for the provision of air transportation.
2. Each airline of any party shall be allowed:
   a) in the territory of any other party to engage directly and, at that airline's discretion, through its agents in the sale of air transportation in the currency of that other party and at prices which that airline may charge for the transportation concerned under Article 12 (Pricing) of this Agreement, irrespective of the right of that airline to perform such transportation, and
   b) to convert and remit promptly to its home country any revenues obtained in the territory of any other party in excess of sums locally disbursed, such conversion and remittance to be permitted without restrictions or taxation in respect thereof and at the rate of exchange applicable to current transactions and remittance.
3. Each airline of any party shall be allowed to perform its own ground handling at the airport(s) in the territory of any party ("self-handling") or, at the option of that airline, to use the ground handling services of any person or entity authorized to perform such services at such airport(s), it being understood that the authorization to perform such services shall not be unreasonably withheld from any person or entity selected by that airline, and furthermore that such airline shall not unreasonably be prevented from performing ground handling services for any other airline(s) at the airport(s) in the territory of any party.
   These rights shall be subject only to physical constraints resulting from reasonable considerations of airport safety or airport capacity, it being understood that the party in whose territory such constraints occur shall provide appropriate evidence thereof In the event such constraints limit or preclude self-handling at any airport in the territory of any party, that party shall
   a) endeavour to remedy such situation as soon as possible and, pending such remedy, to minimize the adverse effects which such situation may have on the airlines of the parties, and
   b) prevail upon the airport authorities concerned that, whenever reasonably possible and

economically justified, existing self-handling facilities are made available to the airlines of the parties proportionate to the ground handling facilities which each of these airlines may reasonably require for the conduct of its operations to and from that airport.

4. Each airline of any party shall be allowed to enter into co-operative arrangements with any other airline(s) and any other interested person(s) or entity (entities)

a) for the purpose of resolving problems caused by insufficient capacity to provide, at any time, customs, technical or operational services and facilities, including handling and other ground services and facilities, and

b) for the purpose of achieving a more efficient use of aircraft, staff or facilities, assisting – at least temporarily – less developed airlines, or simplifying technical and operational conditions,

provided such arrangements are not inconsistent with the provisions of this Agreement.

This Article groups together some of the important commercial facilities which airlines require when performing international air transportation. Since these facilities are sometimes not (adequately) made available to airlines, there is ample reason for specifically including them in the PATA. In paragraph 2 a) a distinction is made between the right to sell and the right to perform air transportation, because some governments seem to hold the (incorrect) view that an airline's right to apply approved air fares is limited to the few route segments for which it has received traffic rights (see for an analysis of this restrictive view H.A. Wassenbergh's article on the sixth freedom question included in this volume).

On a number of airports not more than one airline or agency is licensed to perform ground handling services. Generally, such a monopoly situation has a negative effect on both the quality and the cost of the handling services. For that reason paragraph 3 of this Article specifically includes the option of „self-handling". Furthermore, this paragraph allows the airline of a PATA member to perform ground handling services for any other airline. This additional right enables the handling airline to achieve the required level of efficiency in the use of its handling facilities, e.g. through a more regular utilization of its handling staff and equipment. Sometimes, however, the exercise of these ground handling rights may have to be limited. While recognizing the need thereof, paragraph 3 seeks to prevent any undue restriction of such rights by governments or by airport authorities. To that end this paragraph narrowly defines the circumstances in which ground handling rights may be restricted and specifies which additional obligations the PATA member concerned has to meet in such circumstances. Paragraph 4 of this Article allows airlines to enter into various types of arrangements, such as arrangements for the allocation of available airport slots among airlines and for the conduct of international air services on a lease, blocked space or similar basis. However, PATA members cannot be expected to permit airlines to conclude arrangements which are inconsistent with the PATA itself. Such arrangements are therefore excluded under this paragraph

ARTICLE 9

Customs Duties and Taxes

1. On arriving in the territory of any party, aircraft engaged in international air transportation by the airline(s) of any other party, their regular equipment, ground equipment,

fuel, lubricants, consumable technical supplies, spare parts including engines, and aircraft stores (including but not limited to such items as food, beverages and liquor, tobacco and other products destined for sale to or use by passengers in limited quantities during the flight) and other items intended for or used solely in connection with the operation or servicing of aircraft engaged in international air transportation shall be exempt, on the basis of reciprocity, from all import restrictions, property taxes and capital levies, customs duties, excise taxes, and similar fees and charges imposed by the national authorities, not based on the cost of services provided, provided such equipment and supplies remain on board the aircraft.

2. There shall also be exempt, on the basis of reciprocity, from the taxes, duties, fees and charges referred to in paragraph 1 of this Article, with the exception of charges based on the cost of the service provided:

   a) aircraft stores, introduced into or supplied in the territory of any party, and taken on board, within reasonable limits, for use on outbound aircraft engaged in international air transportation by the airline(s) of any other party, even when these stores are to be used on a part of the journey performed over the territory of the party in which they are taken on board; and

   b) ground equipment and spare parts including engines introduced into the territory of any party for the servicing, maintenance or repair of aircraft engaged in international air transportation by the airline(s) of any other party; and

   c) fuel, lubricants and consumable technical supplies introduced into or supplied in the territory of any party for use in aircraft engaged in international air transportation by the airline(s) of any other party, even when these supplies are to be used on a part of the journey performed over the territory of the party in which they are taken on board; and

   d) any other equipment introduced into the territory of any party for use by the airline(s) of any other party in its (their) commercial operations under this Agreement.

3. Equipment and supplies referred to in paragraphs 1 and 2 of this Article may be required to be kept under the supervision or control of the appropriate authorities.

4. The exemptions provided for by this Article shall also be available where the airline(s) of any party have contracted with any other airline(s) for the loan or transfer in the territory of any other party of the items specified in paragraphs 1 and 2 of this Article, provided such other airline(s) similarly enjoy such exemptions from that other party.

5. Each party shall use its best efforts to secure for the airline(s) of any other party on a reciprocal basis an exemption from taxes, duties, charges and fees imposed by state, regional and local authorities on the items specified in paragraphs 1 and 2 of this Article, as well as from fuel through-put charges, in the circumstances described in this Article, except to the extent that the charges are based on the actual cost of providing the service.

ARTICLE 10

User charges

User charges imposed by the competent charging authorities of any party on an airline of any other party shall be just, reasonable, and non-discriminatory. Such charges may reflect,

but shall not exceed, an equitable portion of the full economic cost to the competent charging authorities of providing the airport, air navigation, and aviation security facilities and services concerned. Facilities and services for which charges are made shall be provided on an efficient and economic basis. Reasonable notice shall be given prior to changes in user charges. Each party shall encourage consultations between the competent charging authorities in its territory and the airlines using the services and facilities and shall use its best efforts to ensure that such authorities and airlines exchange such information as may be necessary to permit an accurate review of the reasonableness of the user charges.

ARTICLE 11

Fair Competition

1. The parties shall ensure that conditions of fair competition prevail among all airlines of the parties in respect of any part or aspect of, or any matter related to, air transportation performed under this Agreement. To this end each party shall in particular.

   a) provide each airline of any party the opportunity to perform, and to compete in, air transportation under this Agreement on an economic and efficient basis, and

   b) within its legal powers ensure, or otherwise use its best efforts to ensure, that its own airline(s) and any other person or entity under its jurisdiction do not affect unduly the opportunity for the airline(s) of any other party to perform, and to compete in, air transportation under this Agreement, and

   c) in any other respect use its best efforts to avoid at any time situations to arise or to continue which unduly affect the opportunity for the airline(s) of any party to perform air transportation under this Agreement and to compete in such transportation under conditions of fair competition.

2. No party shall, in respect of air transportation performed under this Agreement by an airline of any other party, without the agreement of that other party limit or restrict, or permit any person or entity under its jurisdiction to limit or restrict, that airline's traffic, capacity, frequency of service, regularity of service, aircraft type(s), aircraft configuration(s), or rights specified in this Agreement, except as may reasonably be required for customs, technical, operational or environmental reasons under the uniform conditions envisaged in Article 15 of the Convention, provided that:

   a) such conditions do not affect fair competition as described in paragraph 1 of this Article, and

   b) such conditions are applied without discrimination to all airlines of the parties to this Agreement and are not more restrictive than those applied to the airline(s) of any state not party to this Agreement, and

   c) the party wishing to apply such conditions provides as soon as possible appropriate evidence to the other parties of the need for such conditions, so as to allow for any consultations pursuant to Article 13 (Consultations) of this Agreement prior to the date of effectiveness of such conditions.

3. No party shall impose, or permit any person or entity under its jurisdiction to impose, on any airline of any other party any requirement or condition, including a first refusal

requirement, uplift ratio and no-objection fee, which is inconsistent with the purposes of this Agreement.

4. Each party shall as much as possible facilitate the conduct by airlines of air transportation under this Agreement, in particular by minimizing administrative requirements and procedures.

Paragraph 1 of this Article highlights the principle of fair competition which is to be considered as one of the key-stones of the PATA. Briefly, this paragraph recognizes the fundamental right of the airline(s) of each individual PATA member to be and remain competitive when performing air transportation under the PATA. In the PATA fair competition has been described in general terms because this guiding principle should apply to many different elements of international air transportation under the PATA, such as tariff levels and conditions, access to airports and airline reservation systems, designation of airlines, capacity and frequency planning etc. Also, in the light of sometimes substantial economic and other differences between states as well as between airlines, fair competition needs to be defined in flexible terms so as to permit its application in different situations. As long as governments and airlines have an open mind for each other's specific air transport problems and requirements, the application in practice of such generally worded principle should not cause any serious problem. Only in the exceptional case of basic disagreement between PATA members, will it be necessary to resort to arbitration for an impartial assessment of what constitutes 'fair competition' in that particular situation.

A basic objective of the PATA system is to give individual airlines the freedom to establish the scope of their own operations under the PATA with a minimum of interference by governments. In line with that objective paragraph 2 of this Article specifically excludes capacity/frequency limitations or related types of restrictions, while paragraph 3 contains a ban on the imposition of royalties or similar requirements in respect of air transportation pursuant to the PATA. This means that under the PATA capacity and other restrictions cannot be imposed on airlines unless they have specifically been agreed upon between the PATA members concerned (such agreements being envisaged in paragraph 3 of the Article on 'Entry into Force'). The only alternative for a PATA member wishing to limit the capacity offered by the airline of another member is to seek bilateral consultations and eventually arbitration on the basis of the argument that such capacity offer is not in conformity with the principles of 'fair competition' listed in paragraph 1 of this Article. Unilateral restrictive actions by PATA members are incompatible with the objectives of the PATA.

ARTICLE 12

Pricing

1. In international air transportation by any airline of any party between any point in the territory of any party and any point in the territory of any other party, including transportation on an interline or intra-line basis.
   a) each Party shall permit that airline to establish any or all of its prices.
      (i) individually or, at the option of that airline,
      (ii) through co-ordination with any other airline(s); and
   b) no party shall prevent the inauguration or continuation of any price proposed or

charged by that airline pursuant to subparagraph a) of this paragraph, except that any of the parties between whose territories such transportation is performed, as well as the party of which that airline is a national, may prevent the inauguration or continuation of such price if:

(i) with regard to such price that party has reached an agreement referred to in paragraph 2 of this Article, or

(ii) following the consultations referred to in paragraph 2 of this Article, that party reasonably determines that such price established pursuant to subparagraph a) (ii) of this paragraph for air transportation to or from its territory or for air transportion by its own airline(s), unduly restricts or eliminates competition under this Agreement; and

c) each party shall accord to that airline the right to:

(i) meet any price proposed or charged by any other airline or by any charterer, and

(ii) establish at any time, using such expedited filing or notification procedures as may be necessary, a price substantially similar to any price proposed or charged by any other airline or by any charterer for air transportation between the same points.

In the case of interline transportation under this paragraph by any airline of any party in conjunction with any other airline, notification or filing by the first airline of prices for such transportation, if notification or filing of such prices is required, shall be deemed sufficient for the applicability of this paragraph

2. If a party is dissatisfied with a price proposed or charged:

a) by an airline of any party for air transportation between the territory of the dissatisfied party and the territory of any other party, or

b) by an airline of the dissatisfied party for air transportation between the territories of any other parties,

it shall as soon as possible notify such other party or parties.

In such notification the dissatisfied party shall state the reasons for its dissatisfaction and may request consultations with the party or parties so notified. These consultations shall be held not later than thirty days after receipt of the request.

The parties entering into such consultations shall co-operate in securing information necessary for reasoned resolution thereof. If such parties reach agreement with respect to a price for which a notice of dissatisfaction has been given, each of them shall exercise its best efforts to put that agreement into effect.

3. In international air transportation by any airline of any party

a) between any point in the territory of that party and any point in the territory of any state not party to this Agreement, and

b) between any point in the territory of any state not party to this Agreement and any point in the territory of any other such state,

including transportation on an interline or intra-line basis, no party except the party of which that airline is a national shall exercise any authority over prices proposed or charged by that airline.

4. In international scheduled air transportation by any airline of any party between any point in the territory of any other party and any point in the territory of any state not party to this Agreement, including transportation on an interline or intra-line basis:

a) each party shall accord to that airline the right to meet any price proposed or charged by any other airline for such transportation; and

b) the party of which that airline is a national and the party to or from whose territory that airline performs such transportation shall, in case a state not party to this Agreement limits or excludes the access by that airline to (a) price(s) referred to in this paragraph, consult as soon as possible on the request of either party and use their best efforts to put an end to such limitation or exclusion.

5. In international non-scheduled air transportation by any airline of any party between any point in the territory of any other party and any point in the territory of any state not party to this Agreement, prices shall be governed by the provisions of Section 5 of Annex 1.
6. In international air transportation from and to its territory any party shall allow the airline(s) of any state not party to this Agreement to meet any price proposed or charged by any other airline for scheduled air transportation, provided in international air transportation from and to its territory that state extends the same treatment to the airline(s) of that party.
7. Each party may require notification or filing with its aeronautical authorities of prices proposed to be charged to and from its territory by airlines of the parties. Such notification or filing may be required no more than sixty (60) days before the proposed date of effectiveness of any such price.
8. For the purposes of this Article, the term "meet" means the right for an airline to establish at any time, using such expedited filing or notification procedures as may be necessary, for air transportation between the same points, an identical price, except for differences in conditions relating to routing, interlining and intra-lining, or aircraft type; or such price through a combination of prices.
9. Notwithstanding paragraphs c) and g) of Article 1 (Definitions) of this Agreement, the airline(s) of each party shall for the purpose of this Article be permitted to substitute for part of the international air transportation any surface transportation that is incidental to air transportation, provided that passengers or shippers are not misled as to the facts concerning such substitution.
10. The rights available to an airline pursuant to this Article to establish prices, including the right to meet prices:

a) can be exercised by that airline irrespective of its right to perform the air transportation between the points concerned, and

b) cannot be exercised by that airline where, in interline transportation, that airline participates in such transportation only within the territory of one state, if any other airline participating in such transportation would, as a result of the exercise of such rights, obtain pricing opportunities otherwise not available to that other airline pursuant to this Article.

One of the most restrictive features of the traditional bilateral air transport agreement is the so-called 'double approval' tariff control system. Under that system individual airlines do not obtain any pricing freedom whatsoever. In that case, tariff coordination is not a matter of free choice but constitutes the only practical procedure for the establishment of a tariff. If both parties to a bilateral

agreement have to approve the tariffs for air transportation between their territories, a tariff agreement between the airlines involved is by far the best method to obtain such approval. Without such tariff agreement the individual airline entirely depends on the willingness of each of the two governments concerned to approve its tariff proposals. In such circumstances the airlines of the states with the biggest air transport markets have the best chances to get their specific tariff proposals approved. Furthermore, a system in which tariffs are subject to the approval of governments makes sense only if in actual practice the tariffs are also properly enforced. Where this is no longer the case, the approval system as such has lost its „raison d'être".

For these reasons the PATA is based on the so-called 'double disapproval' system in respect of tariffs for air transportation by an airline of a PATA member between the territories of any two PATA members (see paragraph 1 b) (i) of this Article). As a corollary to this system of greater pricing freedom, the airline concerned is free to determine how to establish its tariffs: independently or through co-ordination with other airlines (see paragraph 1 a) of this Article). Only in case the airline chooses to co-ordinate tariffs, each of the PATA members concerned has the right unilaterally to disapprove the result of such co-ordination, if such result is unduly anti-competitive. In that case, the PATA member expressing such disapproval must first consult with the other member(s) concerned. Moreover, any such unilateral disapproval always remains subject to arbitration under the PATA. This specific exception to the double disapproval system has been included in the PATA as a counterbalance against tariff co-ordination: if one agrees with the large majority of states that the right for airlines to co-ordinate their tariffs is a „conditio sine qua non" for a stable international air transport system in our world, one must also under the PATA allow a member to disapprove an inter-airline tariff agreement which unduly restricts or eliminates competition.

Unlike the term 'double disapproval' suggests, three PATA members may actually be involved in the disapproval process referred to in paragraph 2 of this Article. This is so because the PATA member of which the airline (whose tariffs are being disputed) is a national, should always be a party to the agreement whereby such tariffs are disapproved. Otherwise, that airline's pricing freedom could be frustrated by other PATA members in respect of tariffs for air transportation between their territories.

The points of embarkation and disembarkation of a passenger, i.e. the points on an air service between which traffic rights are exercised, do not necessarily coincide with the first point and the furthest point on that passenger's ticket, i.e. the points between which tariff rights are exercised. Transportation between such points may involve interline transportation (i.e. transportation involving two or more different air services of two or more different airlines) or intra-line transportation (i.e. transportation involving two or more different services of the same airline). The explicit inclusion of these two types of transportation in various paragraphs of this Article therefore means that an airline enjoys tariff rights also between points where it does not enjoy or exercise traffic rights (see paragraph 10 a) of this Article in conjunction with paragraph 2 a) of the Article on 'Commercial Operations').

Under the PATA different types of tariff rights are available to airlines. For air transportation (on a direct, interline or intra-line basis) between the territories of two PATA members the airline(s) of any PATA member enjoy(s) full tariff rights (see paragraph 1 of this Article), while for air transportation (on a direct, interline or intra-line basis) by an airline of a PATA member between

the territory of another PATA member and the territory of a non-PATA state only the right to match is exchanged under the PATA (see paragraph 4 a) of this Article for tariffs in scheduled air transportation and paragraph 5 of this Article in conjunction with Section 5 of Annex 1 for tariffs in non-scheduled air transportation). The right of an airline to match the tariffs of any other airline for transportation between the same points constitutes one of the most basic principles in international air transportation. This right to match is therefore also extended, on the basis of reciprocity, to airlines of non-PATA states in respect of international air transportation to/from the territory of any PATA member (see paragraph 6 of this Article).

If, on the other hand, a non-PATA state restricts the matching right of an airline of a PATA member by limiting or excluding the participation of that airline in tariffs between the territory of another PATA member and that non-PATA state, that other PATA member (wich exercises direct control over these tariffs) may be expected to render all possible assistance to fight such discriminatory treatment (see paragraph 4 b) of this Article). Normally, such tariffs would have to be disapproved by that other PATA member.
Under the PATA the airline(s) of each PATA member obtain(s) pricing rights in respect of air transportation (on a direct, interline and intra-line basis) to or from the territory of every other PATA member. Tariffs used by such airline(s) for air transportation do not directly concern any such other member. Under the PATA A control over these tariffs is therefore left to the PATA member of which the airline concerned is a national (see paragraph 3 of this Article).
In the light of the tariff filing procedures referred to in paragraph 7 of this Article, the right to match tariffs has been included also in paragraph 1 of this Article, i.e. for airlines of PATA members operating under the 'double disapproval' system. It would be unreasonable to deny these airlines the right to match tariffs at shorter notice than required under the normal filing procedures, while that right is granted under the PATA to airlines not operating under the double disapproval system (see e.g. paragraph 4 a) of this Article).

Substitution of surface transportation for part of the air transportation is common practice, particularly as regards international cargo traffic. In order to permit airlines to use the applicable air cargo rates for the carriage of such traffic surface transportation had to be brought under the pricing provisions of the PATA (see paragraph 9 of this Article). However, this reference in the PATA to surface transportation is entirely a matter of pricing because, if no air tariffs would be used for such surface transportation, that transportation would remain outside the scope of an air agreement.

In the case of interline transportation the various pricing rights specified in this Article are not available for an airline participating in such transportation on a domestic sector only, if another airline would thereby obtain pricing opportunities to which it is not entitled under the PATA (see paragraph 10 b) of this Article). Otherwise, it would be possible for an airline of a non-PATA state to enjoy in practice e.g. a 'double disapproval' tariff regime between the territories of any two PATA members, by making an interline arrangement with a domestic airline of either of these members.

ARTICLE 13

Consultations

Any party may, at any time, request consultations with any one or more other parties with respect to the performance of this Agreement, including any part or aspect of, or any matter related to, air transportation performed under this Agreement. Such consultations shall begin at the earliest possible date, but not later than 60 days from the date that other party or parties receive(s) the request, unless otherwise agreed. Each party to such consultations shall prepare and present during such consultations relevant evidence in support of its position in order to facilitate informed, rational and economic decisions. Prior to the commencement of such consultations the parties thereto shall inform any party not participating therein of the nature and date of such consultations and any such party shall have the right to attend such consultations as an observer.

ARTICLE 14

Applicable Law and Jurisdiction

1. The parties shall take the appropriate steps, in accordance with their respective constitutional procedures, to ensure that this Agreement and all of its provisions are incorporated in their respective national legislations.
2. This Agreement shall be governed by international law and the parties undertake to perform this Agreement in good faith.
3. In case a dispute between any two or more parties arises under this Agreement concerning any matter regulated by this Agreement or concerning the applicability of this Agreement, its interpretation or application, the dispute shall be considered to arise under international law, the determination and interpretation of which shall be resolved exclusively in accordance with the provisions of Article 15 (Settlement of Disputes) of this Agreement.

A basic legal problem arising in respect of international agreements between states concerns the relationship between national law and international law.
It is important that the PATA acquires force of law also within the legal order of each of the PATA members. This will e.g. permit an airline of a PATA member to invoke the provisions of the PATA in a legal action brought before a local court of another member. To secure such force of law, paragraph 1 of this Article stipulates that each PATA member should take such action as will be necessary to that end under its own constitution. In some states the formal approval or acceptance of the agreement as such, through a parliament, a president, or otherwise, will entail such force of law. In other states the constitution will require that national legislation is passed transforming the agreement into national law.

However, the effect of the incorporation of the PATA in the national legal order of a PATA

member should not be that within that legal order the PATA would lose its international legal status and would thus be applied and interpreted as any national law of that member. Otherwise, the PATA could, as national law of that PATA member, be set aside by other national law of that member, while a local court of that member, in applying the PATA, would not be bound to take account of the rules and principles of international law. For that reason paragraph 2 of this Article explicitly states that the PATA shall be governed by international law. This paragraph, however, is necessarily open-ended. Questions concerning the legal status of an intergovernmental agreement within the national legal order of a state party to that agreement, can only be solved by that state. Unless the constitution of a state recognizes the principle that within its jurisdiction international law takes precedence over national law, different national legal principles may be applied by that state.

Paragraph 3 of this Article stipulates that disputes between PATA members concerning the PATA should be kept entirely outside the national jurisdiction of any particular PATA member. In such disputes no rules and principles other than those pertaining to the international legal order should apply. Consequently, the determination, interpretation and application of these rules and principles in each specific case should be left to the decision of the arbitral tribunal, i.e. the international judiciary under the PATA system.

ARTICLE 15

Settlement of Disputes

1. Any dispute between any two or more parties arising under this Agreement which is not resolved by a first round of consultations held between these parties pursuant to Article 13 (Consultations) of this Agreement, may be referred by agreement of these parties for decision to some person or body. If these parties do not so agree, the dispute shall at the request of any of them be submitted to arbitration in accordance with the procedure set forth below.
2. Arbitration shall be by a tribunal consisting of as many arbitrators as there are parties to the dispute plus one additional arbitrator. This tribunal shall be constituted as follows:
   a) within 30 days after the receipt of a request for arbitration, each party to the dispute shall name one arbitrator. Within 60 days after these arbitrators have been named, they shall by agreement appoint an additional arbitrator, who shall act as President of the arbitral tribunal;
   b) if any party to the dispute fails to name an arbitrator , or if the additional arbitrator is not appointed in accordance with subparagraph a) of this paragraph, any party to the dispute may request the President of the International Court of Justice to appoint the necessary arbitrator or arbitrators within 30 days. If the President of the International Court of Justice is of the same nationality as one of the parties to the dispute, the most senior Vice-President of the International Court of Justice who is not disqualified on that ground shall make the appointment(s).
3. Each arbitrator shall have one vote, except that, in case the total number of arbitrators is even, the President of the arbitral tribunal shall have two votes.
4. Except as otherwise agreed between the parties to the dispute, the arbitral tribunal shall

by majority vote determine the limits of its jurisdiction in accordance with this Agreement and establish its own procedure. At the direction of the tribunal or at the request of any party to the dispute, a conference to determine the precise issues to be arbitrated and the specific procedures to be followed shall be held no later than 15 days after the tribunal is fully constituted.

5. Except as otherwise agreed between the parties to the dispute, each party shall submit a memorandum within 45 days of the time the tribunal is fully constituted. Replies shall be due 60 days later. The tribunal shall hold a hearing at the request of any party, or at its own discretion and by majority vote, within 15 days after replies are due.
6. The tribunal shall attempt to render a written decision within 30 days after completion of the hearing or, if no hearing is held, after the date the replies are submitted, whichever is sooner. The decision of the majority of the tribunal shall prevail.
7. The tribunal shall be competent, at any time and in any event, either upon its own motion or at the request of any party, to prescribe provisional measures necessary to safeguard the rights of the parties. Any party may make such requests in its written pleadings, at the hearing, or subsequently.
8. The parties to the dispute may submit requests for clarification of the decision within 15 days after it is rendered and any clarification given by majority vote shall be issued within 15 days of such request.
9. Each party to the dispute shall, consistent with its national law, give full effect to any decision or award of the arbitral tribunal.
10. The expenses of the arbitral tribunal, including the fees and expenses of the arbitrators, shall be shared equally by the parties to the dispute. Any expenses incurred by the International Court of Justice in connection with the procedures of paragraph 2 b) of this Article shall be considered to be part of the expenses of the arbitral tribunal.

In case it is felt that under the PATA a substantial need for conflict resolution should be envisaged, a different Article on 'Settlement of Disputes' should be drafted. Notably, the establishment of a permanent judicial body could then be contemplated. The present Article largely represents the orthodox (bilateral) approach to the settlement of disputes. However, paragraph 7 constitutes an important innovative provision which introduces the concept of 'provisional measures' to be taken at the tribunal's instruction pending the final decision.

ARTICLE 16

Amendments

This Agreement may be amended at the request of any party. Any proposed amendment to this Agreement must be approved by at least two-thirds of the number of parties and shall then become effective between the parties having approved the amendment.

ARTICLE 17

Registration with ICAO

Upon the entry into force of this Agreement the Government of ..... shall register this Agreement and all amendments thereto with the International Civil Aviation Organization and shall keep that Organization informed of the states parties to this Agreement.

ARTICLE 18

Acceptance and Withdrawal

1. This Agreement shall be open for acceptance by any state member of the International Civil Aviation Organization.
2. Any state referred to in paragraph 1 of this Article wishing to accept this Agreement shall deposit a notification of acceptance with the Government of ....., and such state depositing such notification shall have accepted this Agreement on the date of the receipt thereof by the Government of .....
3. Any state may at any time withdraw from this Agreement by depositing a notification of withdrawal with the Government of ..... . A party depositing such notification shall cease to be a party to this Agreement one year after the date of the receipt thereof by the Government of ....
4. The Government of ..... shall at once inform all states which have accepted this Agreement of the date of receipt of any notification deposited with that Government pursuant to paragraphs 2 and 3 of this Article.

The objective of the PATA is to establish a better regulatory framework for international air transportation through multilateral cooperation. Such framework should not be restricted to a few 'chosen' states. Therefore, membership of the PATA should in principle be open to all states.

According to paragraph 1 of this Article, ICAO membership is the only prerequisite for becoming a PATA member. This criterion has been inserted in the PATA for organizational purposes. It ties in with the various references in the PATA to both the Chicago Convention and ICAO and it avoids any problems under the PATA concerning e.g. state recognition. In view of the undisputed role of ICAO as the only worldwide intergovernmental organization in which virtually all states cooperate for the purpose of developing and promoting international air transport, membership of that organization seems a fair and reasonable prerequisite for a state to become member of the PATA.

For reasons of simplification and convenience paragraphs 2 to 4 of this Article provide that one particular government shall act as depositary in respect of the instruments of acceptance and withdrawal and as administrator as regards the information to be circulated among the members about such acceptance and withdrawal. The same government would be in charge of the information to be provided to ICAO persuant to the preceding Article.

ARTICLE 19

Entry into force

1. This Agreement shall enter into force:

   a) for any state accepting this Agreement before the date that Annex 2 to this Agreement ceases to apply, in the manner which that Annex specifies for such entry into force; and

   b) for any state accepting this Agreement on or after the date that Annex 2 to this Agreement ceases to apply, on the date of such acceptance.

2. Any agreement, arrangement or understanding related to air transportation, in force between any two or more parties before and on the date of the entry into force of this Agreement between such parties shall, as between them:

   a) be replaced by this Agreement, if and to the extent such agreement, arrangement or understanding prevents the full implementation of this Agreement or of any part thereof, and

   b) otherwise remain in force.

3. Any agreement, arrangement or understanding related to air transportation, other than this Agreement, which enters into force between any two or more parties on or after the date of the entry into force of this Agreement between such parties and which contains terms and conditions different from those contained in this Agreement, may at any time be applied between these parties, provided that:

   a) such agreement, arrangement or understanding does not affect the rights of any other party pursuant to this Agreement, and

   b) the provision(s) of such agreement, arrangement or understanding which prevent the full implementation of this Agreement or of any part thereof shall cease to apply three (3) years after the date of their entry into force or at such earlier date as agreed between the parties concerned, unless these parties agree to extend the effectiveness of such provision(s) for one or more subsequent period(s), each of which shall not exceed three (3) years, it being understood that no such extension shall be effectuated more than six (6) months before the date on which such provision(s) would otherwise cease to apply, and

   c) such agreement, arrangement or understanding shall be notified promptly to all other parties to this Agreement.

4. Any party to this Agreement which unilaterally terminates the effectiveness of the provisions of any agreement, arrangement or understanding which remain in force pursuant to subparagraph b) of paragraph 2 of this Article, shall cease to be a party to this Agreement as from the date on which such termination takes effect.

The general rule contained in subparagraph 1 b) of this Article is that the PATA enters into force for a state on the date that it accepts the PATA. Only during the transitional period, when Annex 2 applies, the entry into force will be at a later date (see Section 4 of Annex 2). This exception has been made in order to give each of the states accepting the PATA during the transitional period the opportunity to determine whether or not the PATA can already at that stage be fully implemented between them.

The remaining part of this Article regulates the legal relationship between the PATA and other air transport arrangements between PATA members. Except in the special circumstances mentioned in Section 5 of Annex 2, pre-PATA air transport arrangements (i.e. arrangements in force between states before they join the PATA) should obviously remain in force only in so far as airlines derive opportunities therefrom in addition to those set out in the PATA itself (e.g. fifth freedom traffic rights in addition to the 'minimum regime' pursuant to paragraphs 1 to 7 of Section 2 of Annex 1). If a PATA member cancels such additional pre-PATA opportunities (in accordance with the termination clause contained in the relevant pre-PATA arrangement), it will simultaneously lose its PATA membership (see paragraph 4 of this Article). This provision is included in the PATA because PATA members may be expected to refrain from unilateral restrictive actions vis-à-vis each other.

On the other hand PATA members should be free to conclude between them arrangements which differ from the PATA, provided they do not affect the rights which others hold under the PATA (see paragraph 3 of this Article). Without such provision, the PATA would become an unnecessarily rigid and dogmatic instrument. However, the facility should not affect the obligation of each PATA member to refrain as much as possible from concluding arrangements with any other PATA member which are inconsistent with the PATA. This paragraph therefore provides that such type of arrangement can be concluded c.q. revalidated for (a) limited period(s) of time only, thus forcing the PATA members concerned periodically to review the necessity of maintaining any bilateral arrangement which deviates from the PATA.

ANNEX 1

Section 1

The airline(s) designated by a party shall, subject to the terms of its (their) designation, be entitled to operate any route for the conduct of international air transportation and on such route:

1. to fly over the territory of any other party, either without landing in that territory or in connection with (a) landing(s) (to be) made at any point in that territory; and
2. to include, as a stop for any purpose, any point in the territory of any other party, provided that, if any such point is included on such route for the purpose of performing international air transportation between that point and any other point, a point in the territory of the party which has designated that (those) airline(s) shall be included on that route for the same purpose.

Section 2

Any airline of any party operating any route pursuant to Section 1 of this Annex shall, subject to the terms of its designation, be entitled to perform any international air transportation between any points on such route, except that between any such point in the territory of any other party and any such point in the territory of any state not party to this Agreement, such airline may perform only:

1. international air transportation in respect of traffic which, as evidenced by the document authorizing the carriage thereof between such points, has been carried in such trans-

portation from or will be carried in such transportation to any point(s) outside the territories of that other party and of that state, and

2. any international scheduled air transportation if no airline of that other party performs international scheduled air transportation between the same points, and
3. any international non-scheduled air transportation if, during the period of 30 days preceeding the day on which such transportation is to be performed, no airline of that other party has performed international air transportation between the same points, and
4. any international scheduled air transportation if, and up to the same number of flights with which, any airline of any party, with the exception of the airline(s) of that other party, performs such transportation between the same points, and
5. any international non-scheduled air transportation if, and up to the same number of flights with which, during the period of one year preceeding the day on which such transportation is to be performed, any airline of any party, with the exception of the airline(s) of that other party, has performed such transportation between the same points, and
6. any international scheduled air transportation if, and up to the same number of aircraft-kilometers over which, such transportation is performed between (a) point(s) in the territory of the party which has designated that airline and (a) point(s) in (a) state(s) not party to this Agreement by (an) airline(s) of that other party, and
7. any international non-scheduled air transportation if, and up to the same number of aircraft-kilometers over which, during the period of one year preceeding the day on which such transportation is to be performed, such transportation has been performed between (a) point(s) in the territory of the party which has designated that airline and (a) point(s) in (a) state(s) not party to this Agreement by (an) airline(s) of that other party, and
8. any international air transportation in addition to the transportation referred to in paragraphs 1 to 7 above, as permitted by that other party pursuant to any agreement or understanding or otherwise, it being understood that any request to permit that airline to perform such additional international air transportation not included in such agreement or understanding shall not be denied by that other party without reasonable grounds.

Section 3

Each party shall allow any airline designated by any other party, when operating any route and performing air transportation pursuant to Section 2 of this Annex, on any or all flights and at the option of that airline, without loss of any right otherwise available to that airline:

1. to operate flights in either or both directions and without directional or geographic limitation, and
2. to omit stops at any point(s) outside the territory of the party which has designated that airline and at any except all points in the territory of that party, and
3. to change, at any point, the type or number of aircraft operated or the flightnumber, provided that, in case such change takes place at a point outside the territory of the party which has designated that airline, the operation from such point is a continuation of the operation to such point.

Section 4

To the extent any rights available to a party for the conduct of international air transportation between any points are not used by its own airline(s), that party shall, at the request of any other party, allow any flight(s) operated between the points concerned by the airline(s) of that other party to be used for such air transportation.

Section 5

To the extent that an airline of one party is permitted to perform international non-scheduled air transportation between (a) point(s) in the territory of another party and (a) point(s) in the territory of a state not party to this Agreement:

1. that airline shall comply with the laws, regulations and rules which that other party at any time specifies to be applicable to such transportation, and
2. that other party shall, if it applies different conditions to different airlines in respect of such transportation, apply the least restrictive of such conditions to that airline.

Section 6

For the purpose of this Annex:

1. to perform transportation between points shall mean to perform transportation from one point to another point without interlining or intra-lining in between and, except as regards paragraph 1 of Section 2 of this Annex, irrespective of the origin and destination of the traffic carried in such transportation,
2. the words „the same points" shall be interpreted so as to include in respect of each of these points any airport in the same country within a great circle distance of 100 kilometers from that point.

As in bilateral air transport agreements, the primary purpose of this Annex is to define the routes which may be operated by the designated airline(s) of any PATA member to, from and via the territory of any other PATA member and the traffic rights which such airline(s) may exercise on such routes.

Consistent with the basic objective of the PATA, this Annex extends a maximum of opportunities to the airlines of PATA members with a minimum of conditions and restrictions. This is particularly so in respect of the route rights, since the right for an airline to select the points to be included on its services has a much smaller competitive effect on other airlines than the right to carry traffic between such points. Under the PATA, therefore, no restrictions apply to route structures (see Section 1 of this Annex). As explained in the Introduction, the only exception is the condition that a route on which an airline of a PATA member makes a traffic stop in the territory of another PATA member, must also include a traffic stop in that airline's home-country.

In respect of traffic rights Section 2 of this Annex makes a distinction between fifth freedom traffic rights (i.e. under the PATA the right for an airline of a PATA member to carry traffic from the territory of another PATA member to a non-PATA state and vice versa), and all other traffic rights. While such fifth freedom rights are restricted under the 'minimum regime' described in paragraphs 1 to 8, the other traffic rights can be exercised freely by airlines of PATA members.

It should be pointed out that, unlike pricing rights, traffic rights are basically determined by the points of uplift and discharge of the traffic. In view thereof interline and intra-line transportation, which are of substantial importance in relation to pricing, are practically irrelevant for the purpose of this Annex (see also paragraph 1 of Section 6 of this Annex). Consequently, unlike pricing, the carriage of traffic in so-called sixth freedom is under the PATA nothing but a combination of third and fourth freedom carriage.

The need to distinguish under the PATA between scheduled and non-scheduled air transportation exists only where the minimum traffic rights regime applies, i.e. in fifth freedom transportation to/from non-PATA states (see Sections 2 and 5 of this Annex). For any type of air-transportation between PATA members a regime of freedom applies in respect of routing, traffic rights, capacity and pricing. The only reason for a PATA member to maintain the scheduled/non-scheduled distinction in respect of such transportation would be to determine which market segments its own designated airlines are to serve. This, however, is purely a matter of domestic policy which should remain outside the PATA.

The scope of the 'minium regime' is necessarily somewhat arbitrary, although there is ample justification for this particular selection of minimum traffic rights. Paragraph 1 of Section 2 has been inserted because there is no good reason why any protection which an airline wishes to enjoy in respect of traffic between any two countries, should be extended so as to include traffic of which the origin or destination is in a third country. Paragraphs 2 and 3 of Section 2 have been included because there is equally no good reason to protect an airline on a route where it does not operate services requiring such protection. Paragraphs 4 and 5 of this Section seek to extend 'most favoured airline treatment' to the airlines of PATA members vis-à-vis each other, while paragraphs 6 and 7 reflect the principle of reciprocity among PATA members. Finally, paragraph 8 of this Section should be read in conjunction with paragraphs 2 and 4 of the Article on 'Entry into Force'.

ANNEX 2

Transitional Arrangements

In order to facilitate the transition from existing air transport agreements, arrangements and understandings to this Agreement, the following provisions shall apply during the introductory phase of the application of this Agreement.

Section 1

Not later than thirty (30) days after the date of acceptance of this Agreement by any state, that state may request consultations with any other state having accepted this Agreement, and any such other state may request consultations with that state, for the purpose of concluding between them a transitional arrangement under which the implementation of any of the provisions of this Agreement between such states is made subject to certain conditions as laid down in such arrangement.

Such consultations shall take place within sixty (60) days from the date of such request and the states participating therein shall endeavour to conclude between them such transitional

arrangement which ensures that this Agreement is implemented between them to the extent reasonably possible.

Section 2

Any arrangement concluded between any states as a result of the consultations referred to in Section 1 of this Annex shall:

1. be identified as a transitional arrangement envisaged in this Annex, and
2. be transmitted promptly to all other states which have accepted this Agreement, and
3. not affect the rights under this Agreement of any other state party to this Agreement, and
4. cease to apply at the time this Annex ceases to apply, or at such earlier date as agreed between the states concerned.

Section 3

If between any two states having accepted this Agreement consultations pursuant to Section 1 of this Annex have not been requested before the end of the period of thirty (30) days referred to in that Section, these states shall be deemed to have reached a tacit understanding to implement this Agreement between them without any conditions.

Section 4

1. Upon the expiration of a period of thirty (30) days following the acceptance of this Agreement by any state, this Agreement shall enter into force for that state as soon as that state has concluded an arrangement pursuant to Section 1 of this Annex, or has reached an understanding pursuant to Section 3 of this Annex, with at least one state then party to this Agreement, or, during the time that no state is party to this Agreement, with at least one other state having accepted this Agreement. However, such entry into force shall in no case be later than the date on which this Annex ceases to apply.
2. The Government of... shall at once inform all states which have accepted this Agreement of the date on which this Agreement enters into force for any state pursuant to paragraph 1 of this Section.

Section 5

If between any two states, each of which has accepted this Agreement and has become a party thereto, neither an arrangement pursuant to Section 1 of this Annex has been concluded nor an understanding pursuant to Section 3 of this Annex has been reached, this Agreement shall, notwithstanding the provisions of paragraph 2 of Article 19 (Entry into force) thereof, not be implemented between them in so far as, during the period of effectiveness of this Annex, such implementation prevents the continued application between such states of any agreement, arrangement or understanding referred to in that paragraph. If any of the parties between which this Section applies unilaterally terminates such continued application, that party shall cease to be a party to this Agreement as from the date on which such termination takes effect.

Section 6

This Annex shall cease to apply as soon as this Agreement has entered into force pursuant to Section 4 of this Annex for... (number to be specified) states. Thereafter this Annex shall remain ineffective regardless of any subsequent change in that number

The difference between a small and a large group of PATA members is more than merely numerical. As long as only a handful of states is member of the PATA, this new regulatory regime has a relatively limited effect. Moreover, with only a few PATA members it will be practically impossible to ensure that the advantages of the PATA are spread more or less equally among these members. In other words, to achieve its objectives a multilateral agreement of this type requires a fairly large number of participants. Before such time its application may have to be made subject to certain conditions so as to avoid large imbalances of opportunities.

In view thereof the PATA provides in this Annex 2 for a transitional period until such time that an agreed number of states has become member of the PATA (see Section 6 of this Annex). During that transitional period PATA members may, depending on their specific bilateral air transport relations, agree either to apply the PATA between them without any amendment (see Section 3 of this Annex) or to deviate from the PATA in a restrictive sense. In the latter case they conclude a transitional arrangement which can be applied between them only during the period of validity of Annex 2 (see Sections 1 and 2 of this Annex). PATA members which agree on the need to deviate from the PATA after that period should conclude between them the type of special arrangement envisaged in paragraph 3 of the Article on 'Entry into Force'.

A state which accepts the PATA and subsequently enters into consultations with a PATA member about a transitional arrangement, may fail to conclude such arrangement with that member. In that case these two states have no alternative but to continue to apply the bilateral air transport agreement previously concluded between them (see Section 5 of this Annex). However, the failure of a state accepting the PATA to reach an agreement with a PATA member about the manner in which the PATA should be implemented between them during the transitional period, should not prevent that state from becoming a PATA member, provided that state has reached such agreement with at least one PATA member (see Section 4 of this Annex). A state which does not meet this minimum requirement cannot realistically be said to qualify for PATA membership. This means that the PATA will become effective as soon as two states have accepted to apply the PATA between them, either without any amendment or on the basis of certain conditions laid down in a transitional arrangement.