TRENDS IN THE ECONOMIC REGULATION OF INTERNATIONAL AIR TRANSPORT IN THE AFTERMATH OF BERMUDA II

by

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Master of Laws, LL.M. (McGill University) 1983

A thesis submitted to the Faculty of Graduate Studies and Research, McGill University, in partial fulfillment of the requirements for the degree of DOCTOR OF CIVIL LAW.

Institute of Air and Space Law
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Montreal, Canada

January 1986

To my wife

MONA

whose patience and inspiration have helped
me to surmount all difficulties

M. K. Moursy

ABSTRACT

The legal framework of international air transport consists of bilateral and multilateral treaties. Until the mid-1970s, this framework enjoyed nations' support. In 1977 one of the exemplars of the order, the Bermuda I Agreement of 1946 (between the United States and the United Kingdom), was superseded by a new agreement, the Bermuda II Agreement. It seemed that Bermuda II might set a standard for other bilateral agreements as its predecessor had. The United States, however, considered it protectionist and in reaction revised its international air transport policy to reflect the philosophy underlying its municipal policy of deregulating aviation. The response of other nations was that of hostility illustrated in the 1980 Air Transport Conference of ICAO. By 1982-1984, a change in emphasis occurred in American aviation policy with commercial advantage enjoying equal status to the primary principle of the policy. This, however, raised doubts about the order and called for new solutions.

This thesis examines the regulatory regime prior to 1977, its evolution, and changes occurring since then. It stresses, inter alia, the regulation of charter flights,

capacity and tariffs in the light of the two Bermuda Agreements, the American procompetitive bilaterals and the two ICAO's Conferences of 1977 and 1980. It also reviews the effect of deregulation in the United States, its success and its significance to the world order of international aviation.

Throughout the research events, policies and the legal framework are critically reviewed and possible solutions to the existing uncertainties are made. This leads one to conclude that international air transport may now be facing a period of transition towards a new multilateral regulatory regime. The future role in this process of regional air transport agreements should not be underestimated.

RESUME

Les traités bilatéraux et multilatéraux ont composé le cadre juridique au sein duquel le transport aérien international a évolué jusqu'au milieu des années 70. Ce cadre juridique bénéficiait alors de l'approbation de toutes les nations. L'accord Bermuda I, conclu en 1946 entre les Etats-Unis et le Royaume-Uni constituait alors un modèle de ce cadre juridique, mais fut remplacé par un accord semblable, le Bermuda II. Bermuda II, à l'instar de Bermuda I, semblait pouvoir encore servir de cadre de référence pour les accords bilatéraux à venir. Les Etats-Unis déploraient cependant le caractère protectionniste de Bermuda II, et leur réaction a entrainé la révision de leurs politiques en matière de transport aérien international afin de mieux refléter leurs objectifs nationaux visant la déréglementation du transport aérien. En réponse à cette initiative, d'autres nations se sont révélées hostiles à cette manoeuvre, surtout lors de la conférence sur le transport aérien, tenue sous l'égide de l'OACI en 1980. De 1982 à 1984, il s'est produit un changement des politiques américaines en matière de transport aérien: tout en respectant les principes de l'accord, elles ont également accordé une

importance toute particulière aux avantages commerciaux découlant du phénomène de dérèglementation, ce qui provoqua cependant de graves doutes sur la survie de l'ordre juridique déjà établi et entraîna une recherche de nouvelles solutions.

Cette thèse analysera donc le système réglementaire d'avant 1977, son évolution et les changements effectués depuis lors. Elle se penchera, entre autres, sur la réglementation des vols nollisés, les dispositions relatives à la capacité et à la tarification dans le contexte des accords Bermuda I et II, des accords bilatéraux pro-compétitifs américains et des deux conférences de l'OACI de 1977 et 1980. Elle examinera également les retombées de la dérèglementation aux Etats-Unis, sa réussite et son importance vis-à-vis l'ordre mondial en matière de transport aérien international.

Tout au long de cette analyse critique des politiques avancées et du cadre juridique ci-haut mentionné, des solutions seront suggérées afin de répondre aux incertitudes sous-jacentes. Cette étude nous amènera à conclure que le transport aérien international, maintenant en transition, se dirige vers un nouveau système de réglementation multilatérale. Dans ce contexte, l'influence des accords régionaux en matière de transport aérien ne saura être sous-estimée.

ACKNOWLEDGEMENTS

The encouragement, support, patience and assistance of many people and institutions have contributed to the completion of this thesis.

A balanced presentation of the subject-matter of this dissertation would have been impossible without the help of my thesis supervisor Professor Martin A. Bradley. His enormous knowledge and experience in the subject, advice, suggestions and criticisms have been most valuable to this work. No matter how onerous his duties and activities have been, he has always found time to provide me with information and discuss points of complexity. His enthusiastic encouragement, guidance, cheerful character and personal kindness have been a source of comfort and inspiration during what has often been a lonely and difficult journey. Here I must also mention that during the completion of this thesis, I had the misfortune to go through unfavourable and hindering health problems and again at this juncture, both his and Mrs. Bradley's concern and support was indispensable to pushing me towards better achievement.

I am very grateful to Dr. Nicolas M. Matte, Director of the Institute of Air and Space Law, for his support and kind treatment, and for encouraging me to

continue my studies at this esteemed Institute. Also, my sincere thanks to Professor Ivan A. Vlasic, Dr. Jean-Louis Magdelénat and Professor Peter P.C. Haanappel for their kindness, friendship and concern. Additional thanks are due to Mrs. Ileana Silion for her kind offer of the technical and administrative facilities.

In particular, I wish to acknowledge my deepest appreciation for the UNDP financial assistance, through the efforts of the government of the Arab Republic of Egypt, without whose help this course could not have been completed. To all these and to Mr. Legesse Mammo, Chief of ICAO's Fellowships Section, and his staff sincere thanks are due. Also, my deep gratitude to Mr. Fawzi El Soweify of the UNDP for his concern, kindness and assistance.

The writer owes a special debt of gratitude to the Egyptian Civil Aviation Organization which considers education as an investment rather than an expenditure. Sincere appreciation is therefore expressed to AVM Aly O. Ziko, Chairman of the Egyptian Civil Aviation Authority, for his support, kindness and understanding. Also, I am indebted to Dr. Khairy Y. Moustafa, Director General of Air Transport, for his encouragement, consideration and friendship. While the writer is honored to work in that Department as Chief of Bilateral Air Transport Agreements, any views expressed in

this thesis are so rendered in an exclusively personal capacity, and, in no way, reflect any official position.

Very special thanks are certainly due to Dr. Fouad K. Moursy whose faithfulness and devotion to working in civil aviation for more than forty years have inspired me to follow his career. Also, sincere thanks are extended to Mr. Fauzy M. Hassanein, Representative of Egypt to ICAO Council, for his kind assistance in furnishing me with important ICAO documents and materials.

I must also acknowledge my sincere gratitude to Mr. Moustafa A. El Gallad, Director General of Aswan Airport, for his assistance, kindness, patience and friendship.

Similarly, special thanks are due to Mr. Said R. Sharaf, Director General of Financial Affairs in the Egyptian Civil Aviation Organization for his encouragement, support and concern and for all my colleagues in this Organization.

The writer also desires to express his appreciation to the staff of the McGill Law Library and in particular to Mr. Kuo-Lee Li, Mr. Nazmy Mobarak and Mrs. Jeanne Sahni for according all the facilities in the preparation of this research. Similar thanks are due to the staff of the ICAO Library for their friendly co-operation.

A special note of gratitude is extended to Mrs. Maria D'Amico whose sacrifice in giving up many week-ends to type and re-type the various parts of this manuscript in a very accurate way, will long be remembered with appreciation.

The contribution of all these excellent people and others not mentioned, are reflected in this study, save that the writer is solely responsible for any errors in fact or judgment therein.

Montreal — Moatasim K. Moursy

December, 1985

PREFACE

For more than thirty years, the international civil aviation industry has been growing in a relatively stable regulatory environment, established by the Chicago Convention of 1944 and the Bermuda Agreement of 1946. During these years, the international aviation community accepted the desirability of economic regulation to satisfy the needs of governments, airlines and consumers. In recent years, however, the United States government began to question the need of regulation to guarantee the objective of a viable, worldwide air transport regime; in fact, inspired by the philosophy of free-market economics, it has become convinced that regulation has not been in the best interests of the public. Based on the alleged demonstrated success of its domestic industry deregulation, the United States has attempted to incorporate its free-market economic ideology into the international arena. This American action, however, amounted to a bombshell and caused tremors across the world. The old order of international aviation, the ancient regime, has been threatened and the world community mustered all the strength at its disposal and violently reacted against this.

It is customary to also indicate in the preface to a thesis a statement of the writer's opinion regarding his original contribution to knowledge. It is, of course, difficult to precisely set out what one considers to be a new contribution to knowledge in a field, particularly when that field is air law.

This thesis, besides providing a comprehensive study and analysis of the present legal regime of international air transport - a subject which is of significant contemporary importance to the international community, contributes two particular elements. First, it points out a serious deficiency in the current regulatory regime of commercial aviation which will most probably continue to deteriorate even further in the future. This situation has resulted from a lack of cohesion among nations caused by their endorsing divergent and conflicting aviation policies, but more recently worsened by transferring domestic procompetitive policies to international operations, particularly by the United States. Second, this study prescribes, inter alia, a remedy to the above-mentioned situation. It proposes that the system of bilateral air transport agreements, which in fact constitutes the prime source of norms for the economic regulation of international civil aviation,

is now ripe for replacement by a multilateral regime in the form of regional air transport agreements. This can be simply materialized by forming an "integrated union" among neighbouring countries for their internal aviation objectives, and/or by treating themselves as a "single unit" for purposes of conducting air transport negotiations with third nations. It is, however, paramount that such regional co-operation should then not be a defensive and parochial in outlook, but a method to better integrate into the worldwide air services network of the future to arrive at a truly multilateral economic regulatory system for international aviation.

It should be noted that this work was completed in September 1985, and the writer has attempted to use all relevant information available at that time. The air transport industry is so volatile and dynamic that, even by the date of submission, some of the detailed data and observations may have become out-of-date. However, it is believed that this manuscript presents a fair and reasonably full overview of major developments in the years following the conclusion of Bermuda II Agreement and the increased competition in the international arena.

Finally, although the multidisciplinary implications of the subject made the task difficult, it is wise to recall the famous author, Will Durant, when he stated:

> "We are all imperfect teachers, but we may be forgiven if we have advanced the matter a little and have done our best. We announce the prologue and retire; after us, better players will come."

TABLE OF ABBREVIATIONS

I

AACO	Arab Air Carrier Organization
AAFRA	Association of African Airlines
ABC	Advance Booking Charter
ACAC	Arab Civil Aviation Council
ACCA	Air Charter Carriers Association
AEA	Association of European Airlines
AFCAC	African Civil Aviation Commission
AFRATC	African Air Traffic Conference
AITAL	Asociacion Internacional de Transporte Aéreo de América Latina
Am. J. Int'l L.	American Journal of International Law
APEX	Advance Purchase Excursion (Fare)
ASEAN	Association of South East Asian Nations
ATA	Air Transport Association of America
ATRP	Panel of Experts on the Regulation of Air Transport Services
Avi.	Aviation Cases
BIT	Bulk Inclusive Tour
Bus. Wk.	Business Week
CAA	Civil Aviation Authority (U.K.)
CAB	Civil Aeronautics Board (U.S.A.)
Can. B. Rev.	Canadian Bar Review

Can. Y.B. Int'l L.	Canadian Yearbook of International Law
Den. J. Int'l L. & Pol'y	Denver Journal of International Law and Policy
Dep't St. Bull.	Department of State Bulletin
DOT	Department of Transportation (U.S.A.)
ECA	Economic Commission for Africa
ECAC	European Civil Aviation Conference
EEC	European Economic Community
FAA	Federal Aviation Administration (USA)
FIATA	International Federation of Freight Forwarders' Associations
FRP	Panel of Experts on the Machinery for the Establishment of International Fares and Rates
Ga. J. Int'l & Comp. L.	Georgia Journal of International and Comparative Law
Geo. Wash. L. Rev.	George Washington Law Review
GIT	Group Inclusive Tour
Harv. Int'l L. J.	Harvard International Law Journal
Harv. L. Rev.	Harvard Law Review
IACA	International Air Carrier Association
IATA	International Air Transport Association
ICAN	International Commission for Air Navigation
ICAO	International Civil Aviation Organization

ICASL	Institute and Centre of Air and Space Law
ICC	International Chamber of Commerce
ILA	International Law Association
Int'l Bus. Law.	International Business Lawyer
Int'l & Comp. L.O.	International and Comparative Law Quarterly
Int'l L. Rep.	Interntional Law Report
Int'l Org.	International Organization
Int'l Trade L.J.	International Trade Law Journal
ITA	Institut de Transport Aërien
ITC	Inclusive Tour Charter
ITX	Individual Inclusive Tour
J. Air L. & Com.	Journal of Air Law and Commerce
J. Am Judicature Soc'y	Journal of the American judicature Society
KLM	KLM-Royal Dutch Airlines
LACAC	Latin American Civil Aviation Commission
L.J.	Law Journal
LNTS	League of Nations Treaty Series
L. Rev.	Law Review
MIT	Massachusetts Institute of Technology
NACA	National Air Carrier Association
OAA	Orient Airlines Association
OAU	Organization of African Unity

OPEC	Organization of Petroleum Exporting Countries
OTC	One Stop Inclusive Tour Charter
Pan Am	Pan American World Airways
PICAO	Provisional International Civil Aviation Organization
SAS	Scandinavian Airlines System
SATC	Special Air Transport Conference
SEC	Sepcial Event Charter
SFFL	Standard Foreign Fare Level
SIFL	Standard Industry Fare Level
TC	Traffic (or Tariff) Conference
TGC	Travel Group Charter
TIAS	Treaties and Other Interntion[redacted] Acts Series
Transp. L.J.	Transportation Law Journal
TWA	Trans World Airlines
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNTS	United Nations Treaty Series
UTA	Union de Transports Aériens
Va. J. Int'l L.	Virginia Journal of International Law
Va. L. Rev.	Virginia Law Review
WTO	World Tourism Organization
Yale L.J.	Yale Law Journal

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INTRODUCTION

The post-war pattern for the development of international civil aviation was set by the Chicago Convention of 1944. This recognized the principle of national sovereignty - that each State has exclusive and complete sovereignty in the airspace over its territory and has full right to determine the conditions on which the airlines of other States may use that airspace.

The establishment of this principle led over the years to the conclusion of a network of bilateral air transport agreements between governments providing for exchange of commercial traffic rights on the basis of "fair and equal opportunity". The great majority of international scheduled air services are covered by such agreements, the first of which was the so-called Bermuda I Agreement of 1946 (between the United Kingdom and the United States).

The regulatory regime (established by the Chicago Convention coupled with Bermuda I) worked reasonably well for over thirty years, until new forces arose calling for its revision. The last fifteen years have probably been the most difficult years for international air transport. Early in the 1970's, wide-bodied aircraft were introduced. In

August 1971, the Nixon Administration announced that the United States would no longer exchange gold for dollars which caused monetary instabilities to which air carriers are particularly sensitive. A few years later the first energy crisis made it plain that aviation would also have to cope with this major problem in the future.

In this climate, the share of United States airlines in the international market was steadily declining and this led to unilateral economic measures to safeguard and protect the American national carriers from economic competition. In the middle of the 1970's, the need was felt in the United States for an overhaul of its traditional aviation policy. The denunciation on June 22, 1976, of Bermuda I by Great Britain was one episode in the sequence of events.

The subsequent agreement, Bermuda II, signed on 23 July 1977, represented a compromise providing some protection and some liberalism. It was, however, soon considered as "the most anticompetitive understanding ever entered into by the United States." In reaction the Americans began negotiating a new type of bilateral agreement, with a number of countries, based on free-market competition with the object of achieving a wide variety of service and price options for the consumer. In short, this new policy aimed

at a competitive regulatory system, whereby the forces of the marketplace would play a dominant role and the role of governments would be minimized. Low innovative tariffs would be promoted; restrictions on capacity, frequency, routes and operating rights would be removed. Also, charter rules would be liberalized to a great extent and incorporated into bilateral agreements. Although most of the world aviation community questioned the logic and the fundamental premises of this policy, a few nations eagerly seized the opportunity to obtain long-term, valuable economic benefits by embracing the American policy. It is no secret now that, in some cases, the United States used market leverage to convince recalcitrant countries to accept its policy; in other cases, new route opportunities were exchanged for low fares and multiple designation.

During the last few years, ICAO has also become more involved in the economic regulation of international air transport. This involvement gained momentum in the 1977 and 1980 Air Transport Conferences. In general, these Conferences strongly rejected the new American policy and advocated a more restrictive regulatory framework, taking into consideration the interests of all participants.

The post-Bermuda II trends in international civil aviation law are indeed ambiguous: while unilateralism and

bilateralism are more prevalent, particularly under international deregulation, the majority of nations advocate a multilateral approach, particularly within ICAO. One might wonder where it is possible to find a suitable economic regime for international air transport, given the confusion which now exists.

Perhaps the slowed growth in the economies, high operating cost and a change in the composition of United States travellers have produced a challenging economic environment for implementation of the new liberalized regulatory policies - free-for-all competition and lower promotional fares. Since the majority of nations view their airlines as instruments of foreign policy and integral parts of their national economies, it is paramount that the world community establish regulatory policies on a multilateral basis; policies that not only harmonize divergent national objectives but also are consistent with the changing economic environment. The future role in this process of regional air transport agreements should hence not be underestimated. One might, however, be disappointed when realizing the limited role of lawyers and international law in general in drawing up a new regulatory framework of international air transport:

> "The international lawyer is entitled, and probably not least qualified, to point out the inherent advantages and shortcomings of any particular blue-print and the conditions on which its attainment depends. The choice, however, is for governments and public opinion. It involves political decisions which are outside the lawyer's province."[a]

The purpose of this thesis is to examine certain economic aspects of international air transport, particularly capacity regulation, tariffs and the distinction between scheduled and non-scheduled air operations. The First Chapter explores the controversies surrounding the origin of the airspace sovereignty principle. The Second Chapter reviews the developments from Bermuda I to post-Bermuda II liberal bilaterals. The feasibility of transferring a domestic philosophy to international aviation is analyzed in the Third Chapter. The Fourth Chapter predicts a revival of multilateralism on the regulation of commercial aviation, in the form of regional agreements. The Fifth Chapter examines the development of charters and their impact on scheduled operations. The determination of capacity in international air transport is discussed in the Sixth Chapter. The Seventh Chapter is devoted to evolution and need of the

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a. Schwarzenberger & Brown, A Manual of International Law, Rothman & Co., South Hackensack, New York at 20 (1976).

IATA multilateral forum to resolve divergent and often conflicting objectives of governments and airlines in order to achieve negotiated solutions. The last Chapter contains the final remarks and conclusion. Each of these chapters also ends with a preliminary conclusion which often reflects the writer's recommendations and final results. Finally, it should be noted that this thesis collects data, inasmuch as possible, up to date until September 1985.

CHAPTER I

THE SEARCH FOR UNIFORM INTERNATIONAL ECONOMIC REGULATION OF AIR TRANSPORT

SECTION I - GENERALITIES AND HISTORICAL BACKGROUND

The State's sovereignty over the airspace above its territory is the basis on which the present international legal regime of air transport rests. A brief study of the evolution of airspace sovereignty doctrine is, therefore, necessary to an understanding of the development of national and international air transport law, which guides and regulates the conduct of aviation policies of individual nations.

Prior to the emergence of aviation as a commercially feasible activity, substantial intellectual efforts were undertaken, mainly in Europe, to deal with the attendant problems.[1] In the legal field, the major concern was what principles should regulate this new mode of trans-

1. Hazeltine, The Law of the Air, The University of London Press at 1-4 (1911).

portation. It was realized that the aircraft's potential for trans-border movement posed novel issues.[2] This is not surprising as Europe was the centre of aviation activity prior to World War I, and it was plain that, even with the available primitive aircraft, aviation's potential could not be realized without trans-border movement.

When compared with other commercial activities, aviation is unique because it directly engages the national security interests as well as the sovereignty and the prestige of almost all countries of the world. In short, as expressed by Lowenfeld:

> "International aviation is thus not just another problem in a changing international economic system, though it is that; international civil aviation is a serious problem in international relations, affecting the way governments view one another, the way individual citizens view their own and foreign countries, and in a variety of direct and indirect connections the secur-

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2. It may appear of interest to note that the first legal discussions concerning the treatment of flight occured during the Franco-Prussian War in 1870-71 in which ballons were used on both sides, although the real birth of air law is generally regarded as a product of the 20th century. See, e.g., Vlasic, The Grant of Passage and Exercise of Commercial Rights in International Air Transport, unpublished thesis, McGill University, Montreal at 13, 48 (1955); Faller, Germany and International Civil Aviation, unpublished thesis, McGill University, Montreal at 46 (1966).

ity arrangements by which we live."[3]

The principle of State sovereignty, including sovereignty over territorial airspace, is the starting point for consideration of any facet of the economic regulation of international air transport. It is apparent that in no other field of international communication is the concept of sovereignty as major a pillar as in aviation. Indeed, air transport has never benefited from a liberal regime in sharp contrast to that found in international maritime shipping where many States have adopted an "open-port" policy.[4]

It is not the writer's intention to disregard the well founded international law rule of sovereignty in airspace as a barrier to the healthy development of international aviation. However, the unwillingness amongst nations to limit the exercise of their sovereignty makes civil aviation perhaps one of the last sectors of international econ-

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3. Lowenfeld, "A New Take-Off for International Air Transport", 54 Foreign Affairs at 36 (October 1975).

4. Lissitzyn, International Air Transport and National Policy, New York at 26, 403-404 (1942). It is worth noting here that the "open-port" policy for maritime shipping remained the rule until, in 1974, Article 2 of the U.N. Convention on a Code of Conduct for Liner Conference (U.N. Doc. TD/Code/13/Add.1) began to recommend that some 20% of intra-State maritime traffic be reserved for third-country shipping lines with the remaining 80% shared between national shipping lines (the 40-40-20 rule).

omics to be dealt with on a bilateral discretionary basis.[5]

There is controversy surrounding the origin of the principle of airspace sovereignty. It is generally believed that the concept of a State's sovereignty over the airspace above its territory evolved as a principle of customary international law during World War I and was officially recognized in Article I of the 1919 Paris Convention for the Regulation of Aerial Navigation.[6] However, according to Cooper, the legal regime of airspace predates by many centuries the discovery of the art of flight. In his dissertation on the origin of the maxim "Cujus est solum ejus est usque ad coelum",[7] he concluded that States since Roman

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5. Wassenbergh, "Aviation Policy and a New International Legal Order", 6 Air Law at 169-170, 174 (1981); Cooper, The Right to Fly, (New Henry Holt & Co.) at 122-123 (1947).

6. See, e.g., Wagner, International Air Transportation as Affected by State Sovereignty, Bruylant-Bruxelles at 36 (1970); Sand, Pratt & Lyon, An Historical Survey of the Law of Flight at 12 (1961); Johnson, Rights in Air Space, Manchester University Press at 33 (1965); McNair, The Law of the Air, 3rd ed., London at 5 (1964).

7. When translated it states "who owns the land, owns even to the skies". See Thomas, Economic Regulation of Scheduled Air Transport, Southwestern Legal Foundation Series at 20 (1951); Sand, Pratt & Lyon, op.

times "claimed, held and in fact exercised sovereignty in the airspace above their national territories".[8]

Whether or not one agrees with Cooper's conclusion, it is the writer's opinion that at the end of the 19th century the maxim "Cujus est solum" was not generally regarded as stating a principle of international law respecting the legal status of airspace. An analysis of the doctrine of airspace sovereignty would indeed reveal that, by the beginning of the 20th century, most scholars accepted to a greater or lesser extent the concept of a State's sovereignty in the airspace as it is understood and applied today.[9]

The early discussions which took place on the legal

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cit., note 6, at 4.

8. Cooper, "Roman Law and the Maxim 'Cujus est solum' in International Air Law", in Explorations in Aerospace Law, Ed. by Vlasic, McGill University Press, Montreal at 102 (1968). However, contrary views have been expressed by other writers like Bouvé and Lee. See Cooper, "State Sovereignty vs. Federal Sovereignty of Navigable Airspace", 15 J. Air L. & Com. at 27-31 (1948).

9. Wagner, op. cit., note 6, at 2-6, 53; Thomas, op. cit., note 7, at 176, 179. However, the only exception was probably Professor Nijs, who stated that the air was a res communis at the disposition of everybody. See Hazeltine, op. cit., note 1, at 11-12.

regime of airspace were inaugurated by the French jurist Fauchille's celebrated treatise on "Le domaine aérien et le régime juridique des aérostats" published in 1901.[10] In the following year, Fauchille submitted to the Institute of International Law a detailed study on the subject supplemented by a draft code of law governing the use of the air.[11] Other European jurists contributed to the discussion through publications and meetings that took place, sponsored in particular by the Institute of International Law and the International Law Association. Until the beginning of World War I, the debates were extremely contentious and the legal world was faced with a new "Battle of Books",

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10. Fauchille, "Le Domaine Aérien et le Régime Juridique des Aérostats", 8 Revue Générale de Droit International Public at 414 (1901). According to Professor Hazeltine, this essay marked the beginning of a new period in the history of aerial law. See Hazeltine, op. cit., note 1, at 4. However, on the contrary, Professor Cooper noticed that a forgotten French Law Professor Elgar Ortolon, asserted that the air was as free as the sea, maybe more than 30 years before Fauchille suggested the same doctrine. See Cooper, "Background of International Public Air Law", Yearbook of Air and Space Law, Montreal, McGill University Press at 10 (1965).

11. Cooper, "Air Law - A Field for International Thinking", in Vlasic Ed., op. cit., note 8, at 9-10; Hazeltine, op. cit., note 1, at 4.

as it was wittingly described by Joseph English.[12]

Freedom of the air? or sovereignty of the subjacent States? that was the general question.[13] Although the answer to this question was not (at the time of the deepest controversy) of immediate practical significance, it seemed that all those participating in the dispute were under the impression that the future principles of air navigation would depend upon the solution reached.[14] However, their debates remained of academic interest[15] until Louis

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12. English, "Air Freedom: The Second Battle of the Books", 2 Journal of Air Law at 356 (1931).

13. "Report of the Committee upon Aviation", International Law Association, 28th Report, Madrid at 530 (1913). Between these two extremes, there emerged a number of intermediate theories based on either the principle of a limited sovereignty over the airspace, or on the principle that particular layers of the air require a separate set of rules. For full discussion of the various theories, see, in general, Lycklama a Nijeholt, Air Sovereignty, The Hague at 10-14 (1910); McNair, "The Beginning and the Growth of Aeronautical Law"; 1 Journal of Air Law at 384-385 (1930); Wagner, op. cit., note 6, at 16-31. In this regard, it should always be remembered that while the principle of airspace sovereignty is still firmly recognized, the question of the border between sovereign airspace and free outer space is still unresolved.

14. Kuhn, "The Beginning of an Aerial Law", 4 Am. J. Int'l. L. at 110 (1910).

15. Taneja, U.S. International Aviation Policy, Lexington,

Bleriot, a French pilot, crossed the English Channel and landed in England in 1909.[16] The problem thus left the sphere of legal discussion to become a pressing political question on the highest governmental levels since national security was involved.[17]

SECTION II - THE REGIME PRIOR TO WORLD WAR II

The first attempt of a comprehensive codification of international air law was undertaken by the International Air Navigation Conference which met in Paris on May 10, 1910.[18] Although the immediate cause of the Conference was the concern of the French government over a great number of peaceful but unregulated landings of German ballons on French territory,[19] the scope of this Conference was much

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Massachusetts at 1 (1980).

16. Sand, Pratt & Lyon, op. cit., note 6, at 10; Cooper, op. cit., note 5, at 17.

17. Cooper, op. cit., note 5, at 18.

18. Goedhuis, "Civil Aviation After the War", 36 Am. J. Int'l L. at 597 (1942).

19. In 1908, at least ten ballons crossed the frontier and landed in France carrying over 25 aviators, most of

broader. It was intended to draw up the first international convention regulating air navigation.[20]

Since national air regulations were non-existent at that time,[21] the idea was, as Tombs observed, that all contracting States (and most likely many other countries too) would "establish their own regulations thereafter, in accordance with the international provisions to be laid down by the Conference".[22] However, the Conference adjourned on June 29, 1910 without signing a convention and did not resume its work thereafter as was originally planned.[23]

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whom were German Officers. See Cooper, "The International Air Navigation Conference, Paris 1910", 19 J. Air L. & Com. at 128 (1952).

20. Goedhuis, "The Air Sovereignty Concept and United States Influence on its Future Development", 22 J. Air L. & Com. at 210 (1955).

21. It was not until August 1910 that the first aviation decree was enacted in Prussia. See Sand, Pratt & Lyon, op. cit., note 6, at 6.

22. Tombs, International Organizations in European Air Transport, New York, Columbia University Press at 5 (1936).

23. The date set for the Conference to reconvene was November 29, 1910. See Cooper, "The International Air Navigation Conference, Paris 1910", in Vlasic Ed., op. cit., note 8, at 118.

Although technically the Conference was a diplomatic failure, its influence on the subsequent development of international air law cannot be over-emphasized.[24] Many of the principles discussed and agreed upon at the Conference formed the basis of the deliberations of the Aeronautical Commission of the Paris Peace Conference and were to reappear in the Paris Convention of 1919, as well as, in the Chicago Convention of 1944. Cooper, who has extensively researched on the 1910 Conference, rightly found it regrettable that its historical importance had not received more attention; "Emphasis has been given to the failure of the Conference to agree on the final terms of an international convention. Too little has been said of what the Conference accomplished."[25]

After the breakdown of the Paris Conference of 1910, a number of acts and decrees were issued by the different European States concerning the control of the

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24. The Conference succeeded in preparing the first draft of a comprehensive international convention on air navigation, consisting of 55 articles and 3 annexes. Of particular importance were the provisions on prohibited zones (art. 23 of the draft), cabotage and the establishment of international air services (art. 21 of the draft).

25. Cooper, "A Study on the Legal Status of Aircraft", in Vlasic Ed., op. cit., note 8, at 222.

aerial navigation.[26] With the outbreak of World War I, neutral States such as Switzerland and The Netherlands declared their aerial frontiers closed and forbade the belligerents to cross them. Both belligerents and neutrals generally complied with those measures.[27]

After the war, an Aeronautical Commission was established by the Peace Conference at Versailles in 1919 to prepare, among other things, a convention for international air navigation in peace-time.[28] The "Convention Relating to the Regulation of Aerial Navigation" was eventually signed in Paris on October 13, 1919.[29] According to the first clause of Article 1 of this Convention, the contracting Parties recognize that "every Power has complete and exclusive sovereignty over the airspace above its terri-

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26. Jönsson, "Sphere of Flying: The Politics of International Aviation", 35 International Organization at 277 (1981); MacBrayne, Right of Innocent Passage, unpublished thesis, McGill University at 103 (1956).

27. Hotchkiss, A Treatise on Aviation Law, New York at 6 (1938); Johnson, op. cit., note 6, at 32.

28. Slotemaker, Freedom of Passage for International Air Services, Leiden at 15 (1932).

29. Hereinafter cited as the Paris Convention. For the text of the Convention, see id. at 101 et seq.

tory". As evident from the words "every Power", the principle of airspace sovereignty was recognized by the contracting States as an already established rule of customary international law binding on all States whether Parties to the Convention or not. The adoption of the State sovereignty principle by the Paris Convention, was seen by Gibson as "a result of its recognition during the First World War by both belligerents and neutrals".[30] Cooper attempted, from his historical perspective, to read this 1919 mentality into the considerations of the States' delegates in 1910.[31] However, the official records of the 1910 Paris Conference clearly evidenced that States neither desired nor intended to discuss the topic of the legal status of flight space.[32]

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30. Gibson, "Multi-Partite Aerial Agreements", 5 Temple Law Quarterly at 406 (1931).

31. Professor Cooper tried to prove that it was not the 1919 Paris Conference, as commonly supposed, but the 1910 Paris Conference which first evidenced general international agreement that States had exclusive sovereignty over the national airspace. See, e.g., Cooper, op. cit., note 23, at 105, 123, 126; supra note 25, at 223.

32. See, e.g., Foreign Office Papers for the Civil Aerial Transport Committee, His Britannic Majesty's Government at 1 et seq. (June 25, 1917); Goedhuis, "Some Trends in the Limitation of Air Sovereignty", Studi in

The acceptance in the Paris Convention of 1919 of the principle of airspace sovereignty was the basis of almost all the subsequent international law of the air, even in the countries which were not bound by the Convention. However, in the interest of international aerial intercourse it was necessary to lay down rules relating to the admission of foreign aircraft above the territory of a State. In this respect, the Convention introduced in paragraph 1 of Article 2, the freedom of innocent passage which each contracting State undertook to accord above its territory to the aircraft of the other contracting States.[33] This conventional freedom did not represent a natural right but existed only as a privilege for the aircraft of the contracting States,[34] and as such, could be denied to non-contracting

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Onore di Antonio Ambrosini at 360 (1957); Vlasic, op. cit., note 2, at 64-65.

33. Article 2, Paragraph 1 of the Paris Convention stipulates: "Each contracting State undertakes in time of peace to accord freedom of innocent passage above its territory to the aircraft of the other contracting States, provided that the conditions laid down in the Convention are observed".

34. According to Bouvé, this freedom exists "as a privilege only, for no reason other than that sovereignty in the supervening airspace is vested in the State flown over. It would seem that the privilege should be susceptible of enjoyment only under the conditions

States.

In fact, the right of innocent passage mentioned in Article 2 of the Paris Convention was not clearly defined since Article 15, paragraph 3 provided that "the establishment of international airways shall be subject to the consent of the States flown over". The ambiguity of the term "airways" which could mean both "routes" or "services"[35] was clarified in 1929 when the Convention was amended to provide that

> "Every contracting State may make conditional on its prior authorization the establishment of international airways and the creation and operation of regular international air navigation lines, with or without landing on its territory."[36]

Thus, having come to realize the economic potential of

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imposed by the party granting it". See Bouvé, "The Development of International Rules of Conduct in the Air Navigation", 1 Air Law Review at 25-26 (1930).

35. O'Connor, Economic Regulation of the World's Airlines, New York at 17-18 (1971); Goedhuis, op. cit., note 18, at 601.

36. League of Nations, Treaty Series, Vol. 138 at 421 (1933). This amendment was seen by Latchford as a clear expression of the desire of many of the States not "to do any more than to bring Article 15 into the line with the interpretation which had been placed upon it". See Latchford, "The Right of Innocent Passage in International Civil Air-Navigation Agreements", 11 Department of State Bulletin at 21 (1944).

commercial aviation and seeking to protect their own national airlines, the nations excluded economic regulation of commercial aviation from the provisions of the Paris Convention and, thereby, made it subject to other arrangements, notably bilateral agreements.

Inspired by the Paris Convention of 1919, two other international multilateral conventions were concluded in the years after. The Madrid Convention of 1926,[37] followed closely the provisions of the Paris Convention, but where the Paris regime tended largely to apply to Europe, the Madrid Convention sought to link Spain with Latin America.[38] However, so few States ratified the Convention that it never became effective. Commenting on its failure, Warner stated that:

> "After having been signed by two European and nineteen Latin-American States it has been ratified by only five, is not being pressed for ratification anywhere else,

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37. The Ibero-American Convention relating to Air Navigation was signed in Madrid on November 1, 1926, by Spain, Portugal, and 19 Latin American States (commonly known as the Madrid Convention). See Hudson, "Aviation and International Law", 1 Air Law Review at 190 (1930). For the text of this Convention, which never entered into force, see 8 Journal of Air Law at 263 (1937).

38. Colegrove, International Control of Aviation, Boston at 89 (1930); Lupton, Civil Aviation Law at 25 (1935).

and now appears as of purely academic and historical interest."[39]

The second agreement was the Pan American Convention on Commercial Aviation of 1928, commonly known as the Havana Convention.[40] This Convention was initiated by the United States which sought "to do for the Western Hemisphere what the Paris Convention was doing for Europe - chiefly to provide uniform regulations for air navigation and safety".[41] Article 1 of the Havana Convention recognized, just as did the Paris Convention, "complete and exclusive" sovereignty of each State over its superjacent

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39. Warner, "The International Convention for Air Navigation and the Pan-American Convention for Air Navigation: A Comparative and Critical Analysis", 3 Air Law Review at 226 (1932). However, according to Shawcross & Beaumont, the Madrid Convention was ratified by 7 States. See Shawcross & Beaumont, Air Law at 14 (1945).

40. The initial steps to prepare the draft of the Convention had been taken through a Pan-American Commission met in Washington in May 1927. This draft was later submitted to the Sixth Pan-American Conference which met in January 1928 at Havana. With modifications this project was adopted by the Conference on February 20 and signed by every one of the 21 States of the Pan-American Union. See Latchford, "Havana Convention on Commercial Aviation", 2 Journal of Air Law at 207 (1931); Colegrove, op. cit., note 38, at 88; Fixel, The Law of Aviation, Virginia at 21-22 (1945).

41. O'Connor, op. cit., note 35, at 18. For more details, see Warner, op. cit., note 39, at 224; Taneja, op. cit., note 15, at 1.

airspace. Warner described this similarity as "Essentially the same statement, except for phraseology. The Pan-American form has the virtue of brevity, but the Paris Convention is the more specific."[42]

The Havana Convention had a provision[43] that could have been construed as a mutual grant of the rights to establish scheduled international air services. However, it was not so construed because of the protectionist policy of the member States which continued to require prior authorization.[44] Therefore, the effort of the Havana Convention was no more significant than that of the Paris Convention, as Lissitzyn concluded:

> "The establishment and operation of regular air transport lines require the consent of every State flown over. The power to withhold such consent is used by most national States as a bargaining weapon to their own advantage."[45]

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42. Warner, op. cit., note 39, at 226.

43. Article 21 of the Havana Convention.

44. Rhyne, "Legal Rules for International Aviation", 31 Va. L. Rev. at 275 (1945); Latchford, op. cit., note 36, at 23; Cooper, op. cit., note 5, at 140.

45. Lissitzyn, op. cit., note 4, at 421. It has to be remembered here that all the three Conventions previously discussed in this section are not in force at the present day, as a result of the conclusion of the Chicago Convention of 1944.

To conclude this section, it is worth mentioning here that the only pre-World War II agreement which succeeded in opening up the skies of the member States for commercial aviation was the Zemun Agreement of September 19, 1937, concluded between Italy, Roumania and Yugoslavia.[46]

SECTION III - THE CHICAGO CONFERENCE OF 1944 AND ITS AFTERMATH

On September 11, 1944, in response to a British initiative,[47] the United States invited all the allied powers as well as some neutral governments to participate in an international conference on civil aviation. The Conference convened in Chicago in November 1, 1944, where

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46. Matte, Treatise on Air Aeronautical Law, ICASL, Montreal at 123 (1981). Although this Agreement was approved by the three countries, it was of a little practical importance. See Cheng, "The Right to Fly", 42 The Grotius Society at 107-108 (1956). For the text of the Agreement, which was in the form of a protocol, see Hudson, International Legislation, Vol. VII, Washington at 841-842 (1941).

47. In fact, the British government, in August 1944, requested that a civil aviation conference should be called by the U.S. The U.K. and subsequently Canada were willing to host such a conference if the U.S. found it inconvenient to do so. See Taneja, op. cit., note 15, at 8; Verschoor, An Introduction to Air Law, Kluwer at 9 (1983).

fifty-two nations were represented[48] - hoping in the words of President Roosevelt's opening message "to write a new chapter in the fundamental law of the air".[49]

The Chicago Conference sought to conclude worldwide agreement for the economic regulation of international civil aviation and to set forth rules governing international technical and navigational matters.[50]

On the technical problems, the Conference was eminently successful. It produced a basic treaty - the

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48. Several documents state that 54 nations participated in the Conference; however, Denmark and Thailand were represented by their respective Ministers in Washington who were invited in their personal capacity and did not have the right to vote. See Proceedings, infra (footnote 49) at 13, 49. It is also interesting to note that the USSR had initially accepted the invitation, but surprisingly it withdrew at the last minute, ostensibly as a protest against the participation of certain pro-Facist countries such as Portugal and Spain. See Gidwitz, The Politics of International Air Transport, Lexington Books, Toronto at 46-48 (1980); Osterhout, "A Review of the Recent Chicago International Air Conference", 31 Va. L. Rev. at 378 (1945). However, the writer sees that the Soviet Union feared to enter a competitive situation in which American superiority was so obvious.

49. Proceedings of the International Civil Aviation Conference, U.S. Department of State, Chicago, Vol. I at 43 (1948) (hereinafter cited as Proceedings).

50. Id. at 14-15; Lowenfeld, Aviation Law, Cases and Materials, 2nd ed., Matthew Bender, New York at 2-5 (1972).

Chicago Convention[51] - providing, inter alia, for the establishment of the International Civil Aviation Organization (ICAO) which subsequently has played a significant role in the standardization of the technical aspects of international aviation. However, it has to be remembered that, in order to avoid the possible allegation that nations were illegitimately delegating their sovereign power to an international authority, it was agreed that ICAO would not itself make safety rules and standards; rather, this Organization would simply recommend such rules and standards and leave their actual implementation to the nations themselves.[52] On the major economic issues, however, the Conference could not reach agreement, and therefore, ICAO was given no significant role.[53]

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51. Convention on International Civil Aviation, opened for signature on Dec. 7, 1944 and entered into force on Apr. 4, 1947. See 15 U.N.T.S. at 295-375 (1948), ICAO Doc. 7300/6. The Convention was signed in 1944 by 35 States and adhered to as of 1985, by 156 States.

52. FitzGerald, "ICAO Now and in the Coming Decades", in Matte Ed., International Air Transport: Law, Organization and Policies for the Future, Toronto at 50 (1976).

53. In recent years, ICAO began to change this character and has become more involved in studying economic aspects of air transport. See infra Chapter IV, Section III.

It can be stated that the major effort of the Chicago Conference was directed towards the multilateral regulation of economic rights in international air transport. Four main theses were proposed with regard to this subject. Australia and New Zealand presented a joint plan advocating outright international ownership and operation of the world's trunk air routes by a single international air transport authority, in which each nation should participate.[54] This proposal was strongly rejected by the Conference, which clearly indicated the tendancy of the majority of States away from extensive international control of air transport. It was correctly realized by Goedhuis that "it is an idle dream to believe that the States will be prepared to entrust to an international organization such an important and political attribute of power as aviation."[55] At the other extreme, the United States, the leading air power at the Conference, advocated a position essentially of "free enterprise" in international aviation and hoped to have a multilateral grant of the five freedoms

54. Proceedings, op. cit., note 49, at 77-84.

55. Goedhuis, Idea and Interest in International Aviation, The Hague at 15 (1947).

of the air (detailed hereafter).[56] Failing to reach that, the United States proposed to have routes exchanged bilaterally under a model agreement; economic decisions, including ratemaking, capacity and frequency of service were to be left to airline management and inter-airline arrangements. In its view, any international air organization should concern itself with technical matters and should have no jurisdiction over the economic issues.[57] In sum, instead of regulation, the United States wanted a system of free competition. The United Kingdom, in contrast, envisaged the concept of "order in the air", through an "International Air Authority" having definite powers to fix and allocate international routes, frequencies, capacity and tariffs.[58] This proposal was designed to avoid wasteful competition and assure equitable distribution of the market. The chief British delegate said: "We want to encourage the efficient and to stimulate the less efficient."[59] In a

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56. See infra at 32; Schenkman, International Civil Aviation Organization, Geneva at 82-83 (1955).

57. Proceedings, op. cit., note 49, at 55-62, 525-526.

58. Cheng, The Law of International Air Transport, London at 566-567 (1962).

59. Proceedings, op. cit., note 49, at 65.

somewhat similar vein, the Canadian proposal was almost identical to the British one, but in a rather more elaborate version.[60] Yet, none of the proposals exerted a significant influence in determining the ultimate scope and contents of the Chicago Convention.

It is no secret that the failure of the Conference (to produce a multilateral agreement on the economic regulation of post-war international air transport) was primarily due to the contrasting economic views of the United Kingdom and the United States. The underlying thought for the British restrictionist policy was the fact that it had, as a result of a wartime agreement with the United States, concentrated on the production of combat aircraft and would, therefore, require significant re-adjustment to manufacture civil aircraft. The United States, on the other hand, concentrated on the production of long-range bombers and transport planes. The British felt that the United States could convert more easily than the United Kingdom to the production of civil transport aircraft after the war.[61]

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60. Id. at 570-591; Jennings, "Some Aspects of the International Law of the Air", 75 Recueil des Cours at 524 (1949).

61. See Jennings, id. at 523; Brooks, The World's Airliners, London at 437 (1962); Cribbet, "Some Interna-

A regime of free competition would, therefore, definitely favour the American airlines, and it was exactly this competition which the British feared. In spite of the efforts patiently exerted by the Canadian delegation during the Conference to reconcile the two discordant parties, both countries were unable to reach an agreement.

One of the fundamental principles underlying the Chicago Convention is the fact that all States should be able to participate in air transportation on a basis of equality. The Convention's Preamble provides a pointer in that direction, since it refers to the good faith of States in their dealings with each other and to the regard for equal opportunity and participation. The implementation of this rule, however, is hampered by the limitations of rights States can impose upon each other, limitations which find their origin in the principle of sovereignty of the State over the airspace above its territory expressed in Article 1 of the Convention.[62] In this regard, it has always to be

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tional Aspects of Air Transport", 54 Journal of the Royal Aeronautical Society at 674-675 (1950); Masefield, "Anglo-American Civil Aviation", 1 Air Affairs at 317 (1946).

62. Article 1 provides that "the contracting States recognize that every State has complete and exclusive sovereignty over the air space above its territory".

remembered that the economic consequence of the sovereignty principle is that every State, if it so wishes, can close its airspace to commerce with other nations.

Article 2 of the Convention defines territory, mentioned in Article 1, as including the territorial waters of each nation. However, the Convention states nothing about sovereignty over the airspace above the high seas. The high seas themselves being free for all countries, it follows that the airspace above those high seas is free. This last principle was later incorporated into another Convention (the 1958 Convention on the High Seas) and subsequently reiterated in the 1982 Convention on the Law of the Sea.[63]

During the Chicago Conference, most of the economic discussions amongst the delegations concentrated on the concept of "freedom of the air" in its commercial sense.

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As it is evident from the wording of this Article, this sovereignty principle is an attribute to all States whether Parties to the Convention or not.

63. For more details on the possible implications of the 1982 Convention for the Chicago Convention, see Milde, "U.N. Convention on the Law of the Sea - Possible Implications for International Air Law", 8 Annals of Air and Space Law at 167 et seq. (1983); Hailbronner, "The Legal Regime of the Airspace above the Exclusive Economic Zone", 8 Air Law at 30 (1983).

The words "in its commercial sense" should be stressed, since there was no doubt at Chicago that in the public international law, security, and political sense, the air would not be free - as the principle of airspace sovereignty remained the legal standard in international civil aviation. The concept of commercial air freedom was categorized by the Conference into five air freedoms. For the aircraft of State A, these freedoms are:[64]

> First Freedom: The privilege of flying over the territory of State B without landing.
>
> Second Freedom: The privilege of landing in State B for technical reasons only, i.e. for such purposes as refuelling but not to pick up or put down passengers, cargo or mail.

These two factors have been usually called the "transit", "political" or "technical" freedoms, and they are necessary, of course, to operate a service over or through a foreign country. Although these technical freedoms are perhaps not really commercial rights, they very often form an important pre-requisite for the existence of the other, the purely commercial freedoms. As stated by Morgan, the "transit rights are no good at all if we have no commercial rights anywhere. Their value indeed depends upon their use in

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64. British Air Transport in the Seventies, (The Edwards Report), London at 284 (1969).

reaching countries with which we exchange commercial rights."[65]

> Third Freedom: The privilege to put down in State B traffic, i.e. passengers, cargo, or mail-picked up in State A (outbound traffic).
>
> Fourth Freedom: The privilege of picking up in State B traffic destined for State A (inbound traffic). Third and fourth freedom traffic are closely linked and together form interpartes traffic.[66]
>
> Fifth Freedom: The privilege of picking up or putting down in State B traffic which is destined for or has come from State C (extra-national traffic).[67]

These three freedoms are usually known as the commercial rights, and they are essential to exploit the traffic market of the foreign State itself. In view of the sovereignty principle of Article 1 of the Chicago Convention, it would be linguistically better to speak of "privileges" than of "rights".

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65. The International Civil Aviation Conference at Chicago: what it means to the Americans, U.S. Department of State, blueprint, at 14.

66. Haanappel, Pricing and Capacity Determination in International Air Transport, Kluwer Law and Taxation Publishers at 11 (1984).

67. Occasionally one may come across references to a sixth, a seventh and an eighth freedom. See O'Connor, An Introduction to Airline Economics, Praeger Publishers, New York, 2nd ed. at 49-50 (1982).

In order to make international civil aviation possible, the exchange of commercial aviation rights amongst States, whether on a multilateral or bilateral basis, is necessary. Article 5, paragraph 1, of the Chicago Convention exchanges on a multilateral basis the first two freedoms of the air for non-scheduled international air services under certain restrictions of minor importance. However, the liberal commercial regime for such services included in the second paragraph of the same Article never became a reality, due to the restrictive interpretation given by contracting States to that paragraph.[68] Articles 6, on the other hand, does not grant any privileges for scheduled international air services, leaving their operation depending upon an exchange of commercial rights under bilateral agreements.[69] Thus, Article 1 of the Chicago Convention followed by Articles 5 and 6 laid down the fundamental principles and guidelines which shaped the future development of the commercial international air transport.

Due to the failure of the Chicago Conference to agree that the multilateral exchange of transit and traffic

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68. The interpretation of Articles 5 and 6 will be examined in more details in Chapter V, Section V.

69. Id.

rights for scheduled air services be included in the Convention, two optional agreements were opened for signature at the end of the Conference. The International Air Services Transit Agreement provides for a multilateral exchange of the first two freedoms of the air for scheduled international air services. This Agreement has been widely ratified, and should it become universally accepted in a more permanent form, it would largely solve any difficulties which may impede the establishment of world trade air routes through the territory of any State.[70] In practice (for the States which have ratified or adhered to both the Chicago Convention and the Transit Agreement), Article 5, paragraph 1, of the Convention and Article 1, Section 1, of the Agreement together form a multilateral exchange of the technical freedoms for all international scheduled and non-scheduled air services.

The second agreement is the International Air Transport Agreement which contains a multilateral exchange of all five freedoms of the air for scheduled international air services. It is a reflection of the free enterprise concept of the United States. This Agreement was nipped in

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70. Salacuse, "The Little Prince and the Businessman: Conflicts and Tensions in Public International Air Law", 45 J. Air L & Com. at 825 (1980).

the bud and proved to be a dead letter, due to its lack of ratification from the beginning.[71] The United States itself, the architect of the whole plan, withdrew from it on July 25, 1946, as soon as it became clear that it would not receive general acceptance.[72] However, the curious fact about this Agreement is that it remains unclear today whether the United States, at that time, intended by it to surrender the right to require bilateral route agreements, or whether, on the contrary, it intended that the freedoms granted were to be exercised only along routes negotiated bilaterally.

The failure of the Conference to formulate a comprehensive multilateral framework meant that international civil aviation in the post-war era would have to develop on the basis of bilateral agreements between concerned nations. The participating States themselves were aware of this possibility, for the Final Act[73] of the Conference

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71. El-Hussainy, "Bilateral Air Transport Agreements and their Economic Content with Special Reference to Africa", 8 Annals of Air and Space Law at 120 (1983).

72. To date only 12 States - among whom only the Netherlands and Sweden are major aviation powers - have signed the Agreement.

73. For the outcome of the Conference, see Proceedings,

included a "Form of Standard Agreement for Provisional Air Routes" (commonly known as Chicago Standard Form) to be used in such cases.[74] However, this model contains no provisions on capacity, frequencies, ratemaking and specification of traffic rights to be exchanged.[75] In fact, the Chicago Standard Form influenced future bilaterals only as to their form and language, while the substance was influenced by the terms of the Bermuda I Agreement of 1946.

Berle, the Chairman of the Chicago Conference and head of the United States delegation, expressed his satisfaction on the outcome of the Conference by declaring that:

> "History will approach the work of this Conference with respect. It has achieved a notable victory for civilization. It has begun to put an end to the era of anarchy in the air... ... ... The day of secret diplomacy in the air is past."[76]

There is no doubt that the work of Chicago Conference is

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op. cit., note 49, at 113-372; Bowen, "Chicago International Conference", 13 George Washington Law Review at 311 et seq. (1945).

74. Final Act and Appendices, ICAO Doc. 2187 at 19 et seq. This Standard Form was not intended to be binding on ICAO contracting States.

75. These economic clauses were to be included in annexes to the agreements.

76. Proceedings, op. cit., note 49, at 109, 111.

commendable as it established an international legal framework for the systematic progress of international civil aviation. However, it failed to provide a uniform international economic law of air transport. The basic issues, therefore, such as - routes, ratemaking and capacity for traffic purposes - were left unresolved at Chicago.

After the failure to reach an economic framework for international aviation, the unsettled problems were referred by the Conference to PICAO[77] for further study. In 1946, the Air Transport Committee of PICAO prepared a "Draft Multilateral Agreement on Commercial Rights in International Civil Air Transport". This Draft was presented to the first Interim Assembly of PICAO for consideration in May 1946. The Draft, insofar as economic regulation of international aviation is concerned, contained clauses regarding freedom of the air, capacity, ratemaking and routes.[78] However, the Assembly rejected the Draft, since it was clear that the participating States were far

77. PICAO functioned from June 1945 until April 1947, when ICAO took over.

78. Ryan, "Recent Developments in United States International Air Transport Policy", 1 Air Affairs at 62-65 (1946); For an excellent discussion of this Draft, see O'Connor, op. cit., note 35, at 49-55.

apart in their opinion about a multilateral agreement. It, nevertheless, adopted a Resolution to the effect that a multilateral convention on commercial rights constituted the only solution compatible with the character of international air transport.

During the latter part of 1946, and during the first months of 1947, the Air Transport Committee of PICAO, working through a subcommittee, prepared a new draft which was circulated in March 1947. In short, this proposed agreement (as in the case of the 1946 Draft) rejected bilateral route bargaining and established principles to govern capacity, fifth freedom and tariffs. It differed from the 1946 Draft chiefly in that it would have established no international board for settlement of disputes. Instead, an arbitral tribunal was set up to settle disputes arising from the interpretation of the economic provisions in case bilateral consultations between the disputing Parties failed.[79] The 1947 Draft was submitted to the first Assembly of ICAO in May 1947 for consideration.[80] Again,

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79. Cooper, "The Proposed Multilateral Agreement on Commercial Rights in International Civil Air Transport", 14 J. Air L. & Com. at 125 et seq. (1947); Thomas, op. cit., note 7, at 198-205.

80. Id. The Draft was accompanied by a dissenting Minor-

no general agreement was reached, and the Assembly decided to convene a special commission open to all member States to continue searching for a multilateral agreement.

The Commission met at Geneva from November 4 through November 27, 1947. The discussion on the draft convention dealt with the method for the exchange of traffic rights, settlement of disputes, regulation of capacity and tariffs.[81] This Conference was probably the closest to success that "the major aviation nations have yet come to agreeing a multilateral system of air transport regulation".[82] However, it was unable to reach a multilateral agreement. As at Chicago, the main dispute proved to be whether or not the fifth freedom traffic should be included

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ity Report representing the views of the two major aviation powers, the U.S. and the U.K., as well as China.

81. McClurkin, "The Geneva Commission on a Multilateral Air Transport Agreement", 15 J. Air L. & Com. at 40 (1948).

82. Wheatcroft, Air Transport Policy, London at 72 (1964). Before the Conference started, Warner, the President of ICAO Council at that time, warned that if there was no general agreement on commercial rights, then these would have to be exchanged in 2400 separate bilateral agreements, therefore, one single instrument would be a much better solution. See 2 Interavia at 36 (December 1947).

in a multilateral agreement on the exchange of commercial aviation rights.

The Geneva Conference of 1947 was the last major attempt to reach a multilateral agreement on commercial rights for international civil aviation. In fact, there were further discussions in the Council and Assembly of ICAO, but these were amorphous in character and nothing substantial emerged from them. Conflicts of national interests, particularly with respect to the most crucial problem of fifth freedom traffic, were reflected in a Resolution unanimously adopted by the Seventh Session of the ICAO Assembly in 1953, which recited that: "there is no present prospect of achieving a universal multilateral agreement."[83]

PRELIMINARY CONCLUSION

The conclusion is somewhat disappointing. The economic regulation of international air transport was hardly affected by the Chicago Conference of 1944. Most

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83. This Resolution was adopted unanimously on July 6, 1953. See ICAO, 7th Session of the Assembly, Minutes of the Plenary Meetings, ICAO Doc. 7409, A7-P/2 at 67 (September 1, 1953).

States continued taking advantage of their geographical position and political bargaining power to determine on a bilateral basis which State would be permitted to enter their airspace as well as the commercial operations permissible to foreign airlines in their territory. In other words, there is no uniform international economic regulation for civil aviation. "A lack of political consensus still exists amongst States concerning a multilateral agreement limiting sovereignty for international commercial air transport. However, a tendency towards multilateralism might reappear.[84]

84. See infra Chapter IV.

CHAPTER II

FROM BERMUDA I TO POST-BERMUDA II DEVELOPMENTS

SECTION I - ANALYTICAL INTRODUCTION

Like all other national policies, States' aviation policies are directed, inter alia, by political, geographical, economic and above all prestige and security considerations.[1] Any change in these factors, brought about by a shift in the national objectives or a change in circumstances, necessitates revision of aviation policy. However, a survey of the evolution of international civil aviation reveals that the national interest of each State has been the constant element in the formulation of its individual aviation policy.[2] It is apparent that the national self-interest based upon security and economic considerations was

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1. For an excellent discussion of the relationship between these considerations and the State's aviation policies, see Gidwitz, The Politics of International Air Transport, Toronto at 19-32 (1980).

2. Jones, "The Equation of Aviation Policy", 27 J. Air L. & Com. at 223 (1960).

the underlying factor for the enunciation of the doctrine of airspace sovereignty in both the Paris Convention of 1919 and the Chicago Convention of 1944.

Nations' national interests in aviation vary with the circumstances of each nation. However, common to all is the desire to have effective communications both within the nation and with other nations, with which it has substantial economic, social or political links. International air transport has become over the past four decades a primary means of communication amongst the peoples of the world.[3]

A State's conception of its national interests and needs, the "desires of its travelling public, the esteem a national or private carrier generates for the State, and military and technological considerations combine in complex ways to create a State's air transportation policy".[4] Homer has correctly observed that "it is well to look both forward and backward, that the best may come to pass". Therefore, changes and fluctuations in the aviation policies

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3. Wassenbergh, Aspects of Air Law and Civil Air Policy in the Seventies, The Hague at 9-16 (1970).

4. Dold, "The Competitive Regime in International Air Transportation", 5 Air Law at 142 (1980).

have been made by nations in order to meet the varying needs of their own national interests. The United States and the United Kingdom have been no exception in this regard.

It is interesting to note the change in position advocated by the Americans and the British before and after the Second World War. Historically, the United States had followed protectionist economic policies for international civil aviation and favoured predetermination of capacity and frequency.[5] Reciprocity was often the basis for the exchange of traffic rights between the United States and other countries.[6] An illustration of this American policy may be extracted from its pre-war aviation arrangements with Canada.

The first formal agreement regulating air navigation between the United States and Canada was signed in 1929. The Agreement was wide in scope and covered, on a reciprocal basis, not only the admission of civil aircraft, but also the acceptance of airworthiness certificates and

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5. Tymms, "ICAO - Its Origin and Development: A Personal View", 74 Aeronautical J. at 269 (April 1970); Jack, "Bilateral Agreements", 69 J. of the Royal Aeronautical Soc'y at 471 (July 1965).

6. Cribbett, "Some International Aspects of Air Transport", 54 J. of the Royal Aeronautical Soc'y at 669 (1950).

the issuance of Pilots' Licences.[7] Due to its general application, the 1929 Agreement was replaced by a more restrictive agreement in 1938. Article III of the 1938 Agreement provided that the establishment and operation of regular air services between the territories of both contracting Parties were subject to the consent of each Party.[8] Again, this Agreement was replaced by the 1939 Agreement Relating to Air Transport Services. However, unlike the two previous Agreements, Article III of the 1939 Agreement mentioned clearly that traffic rights for both the American and Canadian carriers were to be exchanged on a basis of reciprocity:

> "...Each Party further agrees, subject to compliance with its laws and regulations and on a basis of reciprocity, to grant operating rights to the air carrier enterprises of the other Party for the operation of international services between a place in the territory of one Party and a place in the territory of the other Party."[9]

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7. Clause 6 of the Agreement laid down the rules for the admission of civil aircraft. However, this Clause constituted a very general and extensive exchange of traffic rights and in fact was rarely used at that time. Canada Treaty Series, 1929, No. 13.

8. See Article III of the 1938 Agreement. Canada Treaty Series, 1938, No. 8.

9. Canada Treaty Series, 1939, No. 10. However, the

During the period between the two world wars, the British had been the proponents of freedom of the air with no restrictions. They realized that the principle of air freedom would allow connecting the most distant parts of the Empire with one another by means of an extensive net of air services, without having to ask the permission of the States overflown.[10] However, it is a paradox of history that the two leading nations had completely reversed their economic aviation policies as the Second World War ended. Some scholars considered this reversal a result of the change in the relative strength of the two nations. The Americans' stupendous wartime experience and growth in long range aircraft production, personnel training, and airline operations widened their aeronautical lead over the British. The United States was now following "the same combination of self-interest and idealism that moved Great Britain to

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Agreement which was of a limited duration was renewed in 1940 and 1943. See Canada Treaty Series, 1940, No. 13 & 1943, No. 4.

10. Wagner, International Air Transport as Affected by State Sovereignty, Bruxelles at 38 (1970); Sand, Pratt & Lyon, An Historical Survey of the Law of Flight at 13 (1961).

assume her historic attitude towards ocean transport".[11]

During the Chicago Conference of 1944, the United States, as was previously pointed out, advocated freedom of the air and interpreted this to mean that competition, unfettered by an international regulatory agency, should be maintained on the world's air routes, without any restrictions on fifth freedom traffic rights. The United States believed that this liberal regime would allow their airlines to compete freely and achieve the aeronautical superiority which air-minded Americans had always wanted. The United Kingdom, on the other hand, had but little experience to offer with resources pitifully reduced in a war effort which had been sustained so much longer. The British, therefore, sought limited, orderly and controlled post-war aviation in which it could participate, even with meagre resources, on a basis of equality with the Americans.[12]

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11. Burden, "Opening the Sky: American Proposals at Chicago", Blueprint for World Civil Aviation, No. 2348, Conference Series 70, U.S. Department of State, Washington at 19 (1945).

12. The United Kingdom desired, among other things, that the fifth freedom traffic (which in fact was the real obstacle to reach agreement at Chicago) should be exchanged through mutual negotiations. See Ryan, "Policy Issues in International Air Transportation", 16 Geo. Wash. L. Rev. at 443, 457 (1948).

The concept of "freedom of the air" as advocated by the United States and the philosophy of "order in the air" as preached by the United Kingdom could not be reconciled at the Chicago Conference. As observed by Harold Jones, such a Conference was a classical demonstration of the postulate that "nations, no matter how enlightened, are not capable of understanding and comprehending anything beyond their own national interest".[13]

In the year following the Chicago Conference, both the United States and the United Kingdom concluded bilateral agreements with third countries in which the principles maintained by both nations at this Conference were followed.

The United States entered into bilateral agreements with Spain, Iceland, the Scandinavian countries, Ireland, Switzerland and Portugal.[14] In each of these agreements, the full five freedom rights were exchanged without control on tariffs, frequency or capacity.[15]

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13. Jones, op. cit., note 2, at 227.

14. United States Aviation Reports, Baltimore at 343-369 (1945).

15. Waldo, "Sequels to the Chicago Aviation Conference", 11 Law & Contemp. Probs. at 624 (1946).

During the same period, the United Kingdom concluded agreements with Canada, Greece, Portugal, Turkey and South Africa. Under these agreements, in general, a provision was made for the predetermination of capacity and its equal division between the carriers of the contracting Parties.[16] As to ratemaking, any tariffs should be determined by the airlines of the contracting Parties subject to governmental approval.

Due to the contradictory philosophies of the United Kingdom and the United States, the development of international air transport services between the two countries was stalled just after the Second World War.[17] Although there was a great pressure from both governments to settle their differences, the United Kingdom was not yet ready to reach an agreement. The British were still in the process of rebuilding their civil air fleet and were unable to compete with the United States' carriers. It is understandable that they were not eager to conclude a bilateral agreement which would incorporate the American principles of free competi-

16. Goedhuis, "Questions of Public International Air Law", 81 Recueil des Cours at 230 (1952).

17. Taneja, U.S. International Aviation Policy, Toronto at 11 (1980).

tion. However, the United States, for its part, was ready to operate to Europe and beyond as well. It needed London and Gander as the basis for transatlantic operations. For the Americans, the British restrictive policy was hindering the start of the international operation for which they were ready.[18]

After the establishment of IATA in 1945, Pan American Airways proposed to lower its New York-London fare from $375 to $275. In addition, the American carriers desired to increase their frequencies to London beyond the limits allowed by the pre-war bilateral arrangements that were still in force in early 1946.[19] These intentions, which were met with fierce British resistance, were probably the impetus for both countries to renegotiate their pre-war aviation agreements.

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18. Smith, Airways Abroad: The Study of American World Air Routes, Madison at 246-247 (1950).

19. Such arrangements limited Pan Am's frequency to two weekly flights and contained no rate provisions. See, in general, 162 L.N.T.S. at 39-57 (1935-1936); Shawcross and Beaumont on Air Law at 69-70 (1945); MacDevitt, "The Triangle Claims Another Victim: A Watery Grave for the Original Bermuda Agreement Principles", 7 Den. J. Int'l L. & Pol'y at 246 (1978).

SECTION II - BERMUDA I AS A FLEXIBLE MODUS VIVENDI

The two countries eventually met at the Bermuda Conference from January 15-February 11, 1946, to work out a bilateral system for the post-war era. Although ostensibly the delegates had come to Bermuda merely to negotiate bilaterally the exchange of commercial rights between their countries, the Bermuda Conference "proved to be one of the most important events in international aviation history".[20] The singular achievement of the delegates in resolving the deadlock reached at Chicago justifies this judgement of the importance of the Bermuda I Agreement. It is for this reason that from Bermuda emerged not merely a bilateral agreement between the two major air transport nations, but "a general philosophy on the way in which the economic regulation of the industry should be achieved".[21]

At the end of the Conference, the following three documents were signed: the Final Act of the Conference, the

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20. Diamond, "The Bermuda Agreement Revisited: A Look at the Past, Present and Future of Bilateral Air Transport Agreements", 41 J. Air L. & Com. at 443 (1975).

21. Wheatcroft, Air Transport Policy, London at 70 (1964).

Bermuda I Agreement and attached Annexes.[22] The most important provisions and innovations of Bermuda I are to be found in the Annexes and in the Final Act rather than in the Agreement itself.[23] Article 1 of the Agreement exchanges traffic rights for scheduled international air services between the two countries. The Annexes to the Agreement reveal what this exchange of traffic rights involves. Annex I defines these rights as: rights of transit, stops for non-traffic purposes, commercial entry and departure for international traffic in passengers, cargo and mail. Such rights are exchanged on the air routes as specified in Annex III or as amended in accordance with Annex IV. Annex V deals with the technical but important matter of "change of gauge",[24] while Annex II contains the ratemaking provi-

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22. Annexes and Final Act of the Civil Aviation Conference held at Bermuda, Jan. 15-Feb. 11, 1946, T.I.A.S. No. 1507; Self, "The Status of Civil Aviation in 1946", 50 J. of the Royal Aeronautical Soc'y at 719, 738 (1946).

23. For such documents, see Bradley and Haanappel Eds., Government Regulation of Air Transport, McGill University at 1 et seq. (1982). Articles 2 to 14 of Bermuda I repeats the ancillary "Chicago Standard" provisions, while Article 1 exchanges the traffic rights.

24. This matter will be discussed in detail in Chapter VI, Section II.

sions.[25] The Final Act of the Agreement contains the principles for the development of international aviation to which both countries subscribed, including a very important resolution on capacity and frequencies issues.[26]

It is worth recalling that both the United States and the United Kingdom (at the time of the conclusion of Bermuda I) expressed their complete accord with each other. On February 26, 1946, President Truman followed the unusual course of issuing out a special statement expressing his satisfaction with the Agreement. At about the same time, official statements in the same tenor were made in both Houses of the British Parliament. In the House of Lords on February 28 of the same year Lord Swinton, the Chairman of the British delegation at the Chicago Conference, called it "probably the most important civil aviation agreement that this country (the UK) has entered into".[27]

Historically, however, the conclusion of Bermuda I was not that amicable. As was previously mentioned, it was

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25. See infra Chapter VII, Section II.

26. For the analysis of Bermuda capacity principles, see infra Chapter VI, Section I.

27. Cooper, "The Bermuda Plan: World Pattern for Air Transport", in Vlasic Ed., Explorations in Aerospace Law at 382 (1968).

essentially a compromise between the "order in the air" advocated by the United Kingdom and the "freedom of the air" preached by the United States. Some scholars defined it as a compromise between the restrictive British and the liberal American concepts. Brancker gave it rather a concise description as a clash between the restrictionism of the "have nots" and the liberalism of the "haves".[28] Whatever the terminology, it was a necessary compromise and a laborious one that would allow each Party to demand a joint review of the operations of the other rather than imposing a system of either rigid control or unregulated freedom.

The success of Bermuda I as a precedent for the aviation industry lies, to a large extent, in the fact that it was nothing more than a compromise. The heart of this compromise was that the United States dropped its objection to governmental tariff control in return for which the United Kingdom relented on the issue of demanding capacity and frequency restrictions for third and fourth freedom

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28. Slotemaker, "Air Policy", in Vlasic and Bradley Eds., The Public International Law of Air Transport at 902 (1974).

traffic.[29] Regarding the much debated issue of fifth freedom traffic, the United States no longer held out for complete fifth freedom rights as proposed at Chicago but settled for the right to fill up seats on through schedules.[30] The British, on the other hand, agreed to let the airlines determine the level of capacity offered as long as it was generally related to the various types of traffic which an airline might carry. The vital element in the whole Agreement was in fact that governments could intervene and seek discussion with each other, but they could not act unilaterally without consultation.

Much has been said on the Bermuda compromise. Some said that the compromise was perfectly acceptable to both countries. Others found that it had only become possible by the promise of an American loan to rebuild the British air transport industry. As Thornton remarked, at Bermuda "the United States was using the desperate need of the United

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29. For the Bermuda compromise see, in general, Chuang, The International Air Transportation Organization, Leiden at 28-29 (1972); McCarroll, "The Bermuda Capacity Clauses in the Jet Age", 29 J. Air L. & Com. at 115 (1963); Adriani, "The Bermuda Capacity Clauses" 22 J. Air L. & Com. at 406 (1955).

30. Baker, "The Bermuda Plan as the Basis for a Multilateral Agreement", in Vlasic and Bradley Eds., op. cit., note 28, at 250.

Kingdom for dollar credits as a way of getting commercial rights which this country (the U.S.) urgently wanted".[31] The influence of non-aviation considerations in bilateral bargainings was indeed not unusual.[32] Wherever the truth may lie, and it probably lies in the middle, Bermuda I in the long run represented a satisfactory way of reconciling the various conflicting considerations between the two Parties and it influenced their international aviation policies.[33]

After the conclusion of Bermuda I, the United States concluded bilateral agreements with France on March 27, 1946, and with Belgium on April 5, 1946, which followed

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31. In fact, the war had left Britain in an extremely weak financial position and was (at that time) concurrently negotiating to obtain a $3.75 billion loan from the U.S. on easy terms. See Thornton, International Airlines and Politics: A Study in Adaptation to Change, Michigan University at 35 (1970).

32. Military objectives, aircraft sales considerations and other economic objectives external to the exchange of commercial rights can play an important or even a decisive role in the process of the negotiations. See, e.g. id. at 80 et seq.; Diamond, op. cit., note 20 at 435.

33. Haanappel, Pricing and Capacity Determination in International Air Transport: A Legal Analysis, Kluwer at 27 (1984); Taneja, op. cit., note 17, at 14.

exactly the Bermuda I pattern.[34] The United Kingdom, however, after the Bermuda Conference, concluded bilaterals with The Netherlands, Turkey, France, Argentina, Ireland and Norway which still reflected the traditional British philosophy of predetermination of capacity and frequency.[35] This British attitude led to a meeting of aviation officials from both countries in London on September 19, 1946, where they issued a joint statement proclaiming Bermuda I as the model for all bilateral air transport agreements to be concluded by the two countries.[36] In the years to follow, however, it can be stated that the United States remained faithful to the liberal Bermuda I principles longer than the United Kingdom.

The significance of Bermuda I in the world of air transport industry is not simply because it involved an agreement between the two leading civil aviation powers of the world, but because it served as the test case with which

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34. 4 U.N.T.S. at 125-154 (1946) (U.S./Belgium Agreement); 139 U.N.T.S. at 114-141 (1952) (U.S./France Agreement).

35. Cheng, The Law of International Air Transport, London at 238-239 (1962).

36. 15 U.S. Dept. St. Bull. at 577-578 (1946).

other bilateral arrangements could be compared.[37] In fact, the Bermuda Agreement constituted a landmark in international aviation history. Since its signature a large number of other States followed the Anglo-American example by concluding Bermuda-type agreements. The Bermuda Agreement was widely welcomed, and it soon became the accepted standard bilateral air transport agreement in the post-World War II era. This was exactly the result predicted by Baker, the Chairman of the American delegation at the Bermuda Conference, when he pointed out in his statement that:

> "What has been worked out here may well form the corner-stone upon which other nations will work out their equally difficult air transport problems."[38]

The results of Bermuda I were not limited to the mutual understanding between States, but made a significant contribution to the post-war expansion of the international air transport. Its principles approached international civil aviation from a basically flexible and liberal point of view. Nevertheless, they also protected the smaller countries against competition and aviation dominance.[39]

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37. Thornton, op. cit., note 31, at 35.

38. Cited in Cribbett, op. cit., note 6, at 670.

39. Stoffel, "American Bilateral Air Transport Agreements

During the decade following the conclusion of Bermuda I, most of the major bilateral agreements were established, and both the United States and the United Kingdom effectively spread the Bermuda principles throughout the world. It has been said that "about one-third of all the bilateral air transport agreements which are in existence today are based on the Bermuda provisions, and another third are very similar in character".[40] What attracted the States to follow these provisions was mainly due to "the so-called Bermuda-type bilateral air agreement still serves as a standard for the exchange of traffic rights for scheduled services".[41] The fact was that the Bermuda principles appeared to be the solution for the economic problems of international air transport in the post-World War II period after the failure of the international aviation community at Chicago to produce a multilateral solution.

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on the Threshold of the Jet Transport Age", 26 J. Air L. & Com. at 122 (1959).

40. Sand, Pratt & Lyon, op. cit., note 10, at 35.

41. Wassenbergh, Public International Air Transportation Law in a New Era, Kluwer at 39 (1976).

SECTION III - POST-BERMUDA I DEVELOPMENTS

Since the signature of Bermuda I in 1946 onward, there have occured dramatic changes in the whole structure of international civil aviation. While the basic principles of Bermuda I and related agreements generally prevailed over the years, the terms and concepts underwent alterations to maintain the Bermuda philosophy as a working document. In general, most deviations from the Bermuda model occurred in the field of capacity and frequency clauses. Many post-Bermuda I agreements turned away from the liberal Bermuda capacity provisions and replaced them, in one form or another, with a system of predetermination of capacity.[42] Some regions, notably Latin America, Africa and Eastern Europe applied more rigid regimes, while numerous countries adopted a selective approach, tending in some bilateral relations to protectionist capacity principles.[43]

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42. See infra Chapter VI, Section III.

43. In fact, South American countries have never adhered to the Bermuda principles and as a region have generally favoured reciprocity or equal sharing of capacity. In Europe, however, Scandinavia and The Netherlands are in favour of liberal capacity provisions, Central Western European countries have a mixed system of liberal and predetermination, while Southern European countries usually adhere to predetermination of capacity. See Hammarskjold, "Trends in Interna-

In the field of tariff clauses, most bilateral agreements have stayed faithful to the Bermuda I principles and delegated the determination of fares and rates to the carriers involved subject to governmental approval.[44] A majority of these bilaterals stipulated that in doing this the carriers might use or could use "wherever possible" the ratemaking machinery of IATA. In fact, most existing bilaterals explicitly delegate the determination of tariffs to the IATA Traffic Conference machinery subject to approval by the concerned governments (i.e. approval by the aeronautical authorities of both contracting Parties to a bilateral agreement). This system of governmental tariff approval has now become known as the "double" or "dual approval" rule.[45]

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tional Aviation and Governmental Policies", Aeronautical J. at 148, 155 (footnote 18) (May 1980).

44. Haanappel, "Bilateral Air Transport Agreements 1913-1980", 5 Int'l Trade L.J. at 255 (1980).

45. This system is exactly the opposite to "double" or "mutual disapproval" pricing rule recently introduced by the U.S. in its liberal bilaterals. See infra Chapter VII, Section III. One should also mention that post-Bermuda I agreements showed a gradual disappearance of intermediate points and of fifth freedom routes, and a gradual appearance of all-cargo routes and also contained the system of single designation.

The United States (at least until the Bermuda II negotiations) remained faithful to the liberal Bermuda I principles and rarely deviated from them.[46] The momentum of the American air transport dominance (after World War II) led to worldwide expansion of their airline services under the Bermuda I principles without any serious difficulties. It can be stated that the United States based its international aviation policy upon these liberal principles, which it suggested possessed some sort of moral or legal sanction.[47] In short, as expressed by one commentator, the Bermuda I Agreement "came to have a meaning for the United States which was not shared by other countries".[48]

The same cannot be said of the United Kingdom which often continued to favour a more restrictive policy, parti-

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46. The most major exceptions are the agreements with India on February 3, 1956 and with USSR on November 4, 1966. The Agreement with India provided for a predetermination of frequencies, see 272 U.N.T.S. at 75-115 (1957). According to the Agreement with USSR, both capacity and tariffs were made subject to a prior arrangement between (Pan Am and Aeroflot) which was then subject to prior governmental approval. For this text, see 55 U.S. Dept. St. Bull. at 791-800 (1966).

47. Jones, op. cit., note 2, at 232; Taneja, Airline Planning: Corporate, Financial, and Marketing, Lexington Books, Toronto at 112 (1982).

48. Diamond, op. cit., note 20, at 476.

cularly in the field of capacity. The British had difficulty with the relative freedom and flexibility allowed to American carriers under the Bermuda I Agreement. They were also disturbed by the 1966 Amendment[49] to Bermuda I in which the United States gave British Airways rights in the Pacific in exchange for the rights of Pan Am and TWA to fly beyond London to almost every European city of any size. Over the years, the Bermuda I Agreement has "become out of date...and no longer corresponds satisfactorily in the view of Her Majesty's government to the conditions of the 1970's".[50]

Since 1946 and for almost three decades, the Bermuda I principles worked reasonably well and provided a standard form for the exchange of commercial rights of air services between nations. By 1959, many States felt that

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49. Signed in May 27, 1966, 17 U.S.T. 683, T.I.A.S. No. 6019. This Amendment dealt with the deletion of several paragraphs of Bermuda I and the inclusion of a new schedule of routes in which the fifth freedom rights were greatly expanded largely to the benefit of the U.S. Thereafter, this Amendment was considered one of the main reasons forcing the Bermuda II negotiations. See Hill, "Bermuda II: The British Revolution of 1976", 44 J. Air L. & Com. at 114 et seq. (1978); Business Week at 104 (August 16, 1976).

50. Edmund Dell, Britain's Secretary of State for Trade, cited in Aviation Week & Space Tech. at 29 (July 5, 1976).

they were too generous to the other States when they granted such rights and made those Bermuda-type agreements. Now, they seek to protect their own national airlines by stretching the liberal Bermuda I principles to suit their purposes or by asking for amendment or renegotiation.[51] International air transport relations are apparently facing some structural problems which bear on the Bermuda Agreement. These, it was said, were "the proliferation in the number of international airlines, the rapid changeovers in equipment brought about by new technology, and the problem of overcapacity".[52]

Beyond these technological and economic changes is the fact that the international aviation community has undergone a profound structural revolution[53] since World War II as a result of decolonization and the emergence of numerous new nations. As these States began to develop their own national airlines, however, two types of problems surfaced. First, emerging foreign airlines were inadequate-

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51. Taneja, op. cit., note 47, at 232; Stoffel, op. cit., note 39, at 119.

52. Diamond, op. cit., note 20, at 470.

53. Sohn, "The Shaping of International Law", 8 Ga. J. Int'l & Comp. L. at 1, 4 (1978).

ly equipped to compete effectively in the international market and, as a result, called on their governments for protection.[54] Second, some strong foreign carriers began to impinge upon markets previously dominated by American carriers, causing the affected United States airlines to prevail upon their government to restrain such operations. Hence, the negotiating history of the 1960s and early 1970s reflects the preoccupation of governments with problems in which carrier interests were paramount.[55]

To this day, many are still comfortable with Bermuda I Language and the concepts it embodies, although by now there are several variatons of the basic concepts. Change was inevitable in a technically-advanced and competitive industry such as aviation. As was previously pointed out, fundamental changes were brought about, inter alia, by the emergence of new airlines, the introduction of jet aircraft and the increase in charter operations. These changes when coupled with other factors like the growth of nationalized industry in the United Kingdom, the economic strength of West Germany and Japan, and the emergence of the Arab

54. Goedhuis, "The Changing Legal Regime of Air and Outer Space", 27 Int'l & Comp. L.Q. at 576, 581 (1978).

55. Wassenbergh, op. cit., note 3, at 22.

countries with their oil resources,[56] all bear on the question of whether the Bermuda principles are still appropriate to meet the needs of international air transport.

In all fairness, it should be recognized that the Bermuda scheme had, after all, endured throughout the remarkable changes of the thirty years following World War II. As observed by Taylor (a TWA Vice-President) following the conclusion of Bermuda II:

> "Mr. H.A.L. Fisher wrote that if a treaty serves its turn for 10 or 20 years, the wisdom of its framers is sufficiently confirmed."[57]

The Bermuda I Agreement had survived for more than three decades and its formula still is a major factor in the bilateral system.

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56. Doty, "British Action Forces Bermuda Review", Aviation Week & Space Tech. at 51 (October 18, 1976).

57. Taylor, "The United States Attitude: A View from TWA", 82 Aeronautical J. at 61 (February 1978).

SECTION IV - BERMUDA II: SOME PROTECTIONISM, SOME LIBERALISM

On June 22, 1976, the United Kingdom announced its denunciation of the Bermuda I Agreement of 1946. According to Article 13 of this Agreement, the Parties had twelve months in which to negotiate a new agreement or suffer the termination of the old one without a replacement. Although nine factors contributed to the decision,[58] the primary reason was Great Britain's newly formed belief that the existing bilateral agreement was unbalanced and that it provided greater economic benefits to the United States carriers. The British memorandum sent to the State Department stated that "we shall be looking for an increase in the earnings of British carriers, and we see no practical means of achieving this except through a reduction in the earnings of United States carriers".[59]

As far as the earnings imbalance was concerned, the United States airlines earned in the year ending March 31,

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58. Hotz, "Bilateral Battles", Aviation Week & Space Tech. at 11 (October 18, 1976); Taneja, op. cit., note 17, at 21; Feldman & Sweetman, "Bermuda 2 Battle Lines", Flight International at 96 (September 25, 1976).

59. Business Week at 37 (September 13, 1976).

1976, nearly £300 million on the routes covered by Bermuda I, whereas the earnings of the British airlines were only some £130 million. Of this latter figure, £127 million was earned on the North Atlantic where United States airlines earned upwards of £180 million.[60] In this regard, it should be kept in mind that the negotiation of any bilateral air transport agreement "has always been based, at least in theory, on the idea of 'fair exchange' - of a satisfactory degree of reciprocity".[61] This appears to have been the principle which led the British to denounce the Bermuda I Agreement in 1976. The Note of Denunciation complained "primarily of an imbalance of benefits" between the two nations,[62] permitting the United States airlines to gain too large a part of the market.

The termination notice served on Secretary of State Kissinger surprised most United States officials, who

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60. Shovelton, "Bermuda 2-A Discussion of Its Implications", Aeronautical J. at 51 (February 1978); Flight International at 4 (July 1976).

61. "On What Principles Should Bilateral Advantages be Assessed?", ITA Bull. at 29 (January 1958).

62. Larsen, "Status Report on the Renegotiation of the U.S.-U.K. Bilateral Air Transport Agreement", 2 Air Law at 82 (1977).

believed that the United Kingdom would first request consultations before issuing such a notice. To many this was unthinkable, since Britain was America's most important overseas market and the "golden nugget" of the whole system. In their view, the British were "very calculating" on the time and manner in which they chose to terminate Bermuda I. It was alleged that the United Kingdom wanted to gain the New York landing rights for the Concorde and as well the embarrassment it might have caused to Queen Elizabeth II during her visit to the United States in the first week of July 1977.[63] However, the British denied that there was any "Machiavellian process" involved in the decision to terminate Bermuda I.

After eight rounds of heated negotiations, the new Bermuda II Agreement was signed and entered into force on July 23, 1977.[64] Although the Agreement was actually negotiated in London, its formal signing took place in Bermuda, apparently for sentiment's sake. In short, while

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63. It was also said that the possibility of a change in President Ford Administration in the fall might play a role in the U.K. decision. See Ellingsworth, "Special Panel to Study Bermuda", Aviation Week & Space Tech. at 31 (July 5, 1976).

64. Bermuda II Agreement, July 23, 1977, T.I.A.S. No. 8641 (hereinafter cited as Bermuda II).

neither the United Kingdom nor the United States got all it wanted, the final Agreement did provide for mutual benefits in the aggregate. Specifically, Bermuda II imposed a restriction on the number of United States - flag carriers in the United Kingdom markets, established a mechanism for the control of capacity,[65] and limited the beyond points to which the American carriers could carry United Kingdom fill-up traffic. On the other hand, Bermuda II did introduce more carriers, open up more markets, and lead to lower fares on the North Atlantic.

In general, one can say that in the key areas of capacity, frequency, and tariffs, the new Agreement reiterates Bermuda I with some elaborations and restrictions. As to capacity principles, Article 11 of Bermuda II sets forth the vague Bermuda I capacity principles with minor changes.[66] Typically, Bermuda II tried to solve the problem of overcapacity on the North-Atlantic by imposing an

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65. In fact, the British aimed at splitting U.S.-U.K. air traffic equally between American and British carriers. However, in this attempt, the British were unsuccessful. See Salacuse, "The Little Prince and the Businessman: Conflicts and Tensions in Public International Air Law", 45 J. Air L. & Com. at 836 (1980); Haanappel, op. cit., note 33, at 40.

66. For the analysis of the Article, see infra Chapter VI, Section I.

obligation on the Parties to avoid overcapacity and undercapacity and setting up a consultative mechanism to deal with the problem. Although the British did not succeed in obtaining their initial goal of intergovernmental predetermination of capacity and frequency, the regulation of capacity in the new Agreement is certainly more restrictive than that found in Bermuda I. The old 1946 Bermuda Language said, in effect, to airline management: "Go ahead and decide your frequencies and capacity, but remember not to over do anything or you may be called to account afterward". The new 1977 Bermuda formula seems to be saying: "Go ahead and decide what you'd like your frequencies and capacity to be, but remember that before you can operate them the foreign government has a right to challenge them, and you may end up being allowed only part of your desired increase".[67] Thus, Bermuda II placed a strong restraint on managerial discretion.

With respect to tariffs, Article 12 of Bermuda II makes a distinction between tariffs set by IATA and those fixed by the airlines.[68] In both cases, the system of

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67. O'Connor, An Introduction to Airline Economics, Praeger, New York at 47 (1982); id.

68. See infra Chapter VII, Section II.

"double" governmental approval of tariffs is still required. With regard to the designation of carriers, the principle is a system of multiple designation with a fairly complex system of exceptions.[69] Furthermore, under Bermuda II, it can be said that the United States lost practically most of its fifth freedom traffic rights to Europe but obtained in return unlimited blind sector rights beyond London into Europe. The British carriers also gained four new routes.[70] Finally, provisions relating to charters were included for the first time in a scheduled bilateral air transport agreement.[71]

Before discussing the various reactions to the new Bermuda II Agreement, it may appear proper to draw a philosophical distinction between the two Bermuda Agreements. Bermuda I was, as evidenced, established to regulate bilateral commercial relations between the United Kingdom and the United States, to open up the skies for a system of regulat-

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69. Each country designates only two carriers on the New York/London and Los Angeles/London routes. However, on all other city pairs which include London there is single designation per route. See also infra (footnote 108).

70. Brown, "Compromise Marks Bilateral Pact", Aviation Week & Space Tech. at 26 (June 27, 1977).

71. See infra Chapter V, Section III (footnote 73).

ed freedom and to provide new opportunities for both Parties in a liberal spirit.[72] Bermuda II sought, in contrast, to restructure already existing aviation relations and to combine old principles with new regulatory techniques relying less on self-regulatory forces.

The initial reaction to Bermuda II by the highest officials of both Parties was a promising one. Shovelton, the Chief of the United Kingdom delegation, described the Agreement as remarkably liberal and fair to each side. He also urged that both "the U.S. and the U.K. should follow the guidance of Bermuda II in each of our nation's negotiations with other countries".[73] British Secretary of State for Trade, Edmund Dell, believed that "this Agreement will open a new and expanding era. It will provide significant new opportunities for the airlines of both sides and promises real benefits to the consumer".[74] On the other hand, Alan Boyd, the Chairman of the American delegation, termed it "very satisfactory to the U.S.... It will provide

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72. Matte, Treatise on Air Aeronautical Law, ICASL, Montreal at 237 (1981).

73. Cited in Gray, "The Impact of Bermuda II on Future Bilateral Agreements", 3 Air Law at 18 (1978).

74. Cited in Shovelton, op. cit., note 60, at 54.

for growth in a growing market".[75] American Secretary of Transportation, Brock Adams, stated that the new Agreement supported the principle of competition in the international marketplace. He believed in certain respects more competition was permitted "under the new Agreement than under the old".[76] It is worth noting that President Carter himself hailed Bermuda II as being:

> "consistent with the objective of healthy economic competition among all carriers... (and by saying that)...its quality, its fairness, and its benefits to the consumer and to the airlines should make it last as long as the original 1946 Bermuda Agreement."[77]

Some commentators considered that the Bermuda II Agreement could have an influence on future bilaterals particularly in the field of capacity, tariffs and fifth freedom traffic rights.[78] From the official point of

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75. Brown, op. cit., note 70, at 27.

76. Statement of U.S. Secretary of Transportation on the signing of Bermuda II, in Bermuda (July 23, 1977).

77. Hearings on International Aviation before the Subcommittee on Aviation of the Senate, Commerce Comm., 95th Cong., 2nd Sess. 84 (1978).

78. Adriani, "Some Observations on the Newly Born Bermuda II", 2 Air Law at 190 (1977); O'Connor, op. cit., note 67, at 47; Aviation Week & Space Tech. at 26 (July 18, 1977).

view in the United States, it soon became very clear that the new Agreement was considered to be a response to the particular Anglo-American aviation relations existing at that time. It was argued that one of the underlying "political motives" in Bermuda II could have been President Carter's concern that a cessation of United States - United Kingdom air services would force British Prime Minister James Callaghan's Labor government to resign.[79]

No sooner had the Bermuda II Agreement been signed than outcries were raised by most American airline officials. Some United States carriers claimed that the new Agreement transferred "net economic benefit from the U.S. flag systems to the British flag. That was the purpose of the British denunciation of the old Agreement".[80] Other carrier officials urged the United States should have allowed air services to terminate rather than submit to British demands, realizing how politically and economically severe the service cut-off would have been for the British with the consequent decrease in United States tourism.

The position held by many American observers was

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79. "Pact Seen Dangerous Precedent", Aviation Week & Space Tech. at 25 (July 18, 1977).

80. Brown, op. cit., note 70, at 27.

that the United States had demonstrated by its compromise with the United Kingdom that it could be "blackmailed" into agreements, simply by a threatened cessation of air services.[81] The Bermuda II compromise, it was charged, would encourage other States with which the United States had bilateral air transport agreements to denounce them in order to get better concessions from the Americans as the British did. This sharp reaction to Bermuda II was not only opportune for the United States but also urgent. In fact, the "blackmail" predicted by some had in one sense already begun. At the time of the signing of Bermuda II, the United States was already scheduled to resume bilateral negotiations with Japan later in the same year in order to redress the grievous imbalances in the old bilateral of 1952.[82] It was said that the Japanese might use Bermuda II as the jumping off point.[83] With Bermuda II as a precedent, it

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81. Aviation Week & Space Tech. at 25 (July 18, 1977).

82. These negotiations were scheduled to be held in Tokyo from 6-19 October 1977. Aviation Week & Space Tech. at 26 (August 1, 1977).

83. Gray, op. cit., note 73, at 18. In this respect, Japan Airlines President landed Bermuda II in the areas of capacity, routes, designation and fifth freedom rights as "a stepping stone in the forthcoming negotiations between Japan and U.S.". Aviation Week & Space Tech. at 27 (June 27, 1977). Similar strategy

appeared difficult to deny to the Japanese the compromises the United States had already given the British.

It seems the American opposition to the Bermuda II Agreement centred not so much upon how much the British received as compared to the share of the American carriers, but on the negotiating body, the form the Agreement took, and the anti-competitiveness of the Agreement.[84] As soon as the complete text of the Agreement became available, it triggered demands for Congressional hearings and raised the possibility of a court challenge of the validity and constitutionality of the pact. Many members of the Congress were so disturbed by the outcome of the negotiations that they argued that Bermuda II should be classified as a treaty instead of an executive agreement so that it would require the advice and consent of the Senate before binding the United States.[85]

In this respect, it is worth mentioning that for United States purposes, bilateral air transport agreements

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was also being envisaged for the U.S.-Italy talks. See Ellingworth, supra note 63, at 31.

84. MacDevitt, op. cit., note 19, at 273.

85. See, in general, letters from Senator Kennedy to President Carter (July 18, 1977), reprinted in Aviation Daily at 135 (July 27, 1977).

are executive agreements[86] rather than treaties.[87] This means that these bilaterals are signed under the executive power of the President and not submitted to the Senate for consent to ratification. Although these agreements are signed under the executive power of a President, their validity does not expire with the President's Administration.[88] The difference between a treaty and an executive agreement is, in fact, a matter of domestic American constitutional law. It is certainly practical to have bilateral air service agreements concluded as executive agreements and thus avoiding unnecessarily cumbersome and time-consuming procedures; "since such arrangements normally contain

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86. See, in general, Lissitzyn, "Bilateral Agreements on Air Transport", 30 J. Air L. & Com. at 248 (1964); 40 Opinions of the Attorney - General at 451-454 (1940-1948); Tantirujananont, The Position of International Aviation Agreements in National Law, unpublished thesis, McGill University, Montreal at 53-64 (1982); Cohen, "Self-Executive Agreements", 24 Buffalo L. Rev. at 137 (1974).

87. The status of bilaterals may vary from nation to nation. They may take the form of formal treaties and need ratification by Parliament or take the form of less formal inter-governmental agreements which do not need the formality of ratification, or even the form of an exchange of diplomatic notes.

88. Lissitzyn, "The Legal Status of Executive Agreement on Air Transportation", 18 J. Air L. & Com. at 30 (1951).

specific provisions for services on particular routes and between particular terminals, they must be flexible and subject to modification without much delay".[89]

The question of the legal status of bilateral air transport agreements in the United States evolved, inter alia, after the conclusion of Bermuda II. In Greater Tampa Chamber of Commerce v. Neil Goldschmidt, Secretary of Transportation,[90] the United States Court of Appeals discussed the challenges made against the legality of Bermuda II. In this case, the plaintiffs-appellants filed a complaint alleging that Bermuda II was an invalid agreement and asked for declaratory and injunctive relief against the Secretary of Transportation, the Secretary of State and the United States. They identified as the injury which motivated the suit that Bermuda II was "anti-competitive" and

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89. Id. at 21.

90. Greater Tampa v. Neil Goldschmidt, (U.S. Court of Appeals for the District of Columbia Circuit), CCH Aviation cases, Vol. 15 at 17, 956 (Feb. 8, 1980). It is interesting to note here that the legality of Bermuda II was recenlty strongly challenged by the British on the grounds that "it has become virtually unworkable", due to the fact that "it can be overridden by U.S. antitrust laws". See Brown, "British Transport Minister Decries Bermuda II Pact", Aviation Week & Space Tech. at 26 (Nov. 5, 1984). This conflict, however, was later solved after personal intervention by President Reagan. See infra Chapter VII, Section II (footnote 90).

therefore diminished the quantity and quality of trans-atlantic air service available to them.

The Court of Appeals dismissed this case for lack of standing since the complaint failed to allege facts showing a substantial likelihood that a grant of relief would redress the asserted injuries. In addition, the Court held that there was no substantial likelihood that the Senate would refuse to ratify the Agreement if Senate ratification were necessary, and even if the Senate declined to ratify the Agreement, there was no evidence that the United Kingdom would accept terms other than those included in Bermuda II. In this respect, the writer endorses the decision taken by the Court of Appeals, because, if the Court had to rule that bilaterals were treaties and thus needed ratification, it might have severely disrupted the international air transport system. But one may indeed wonder if it is still justifiable to consider bilaterals, which nowadays cover a variety of economic regulations relating to air transport, as executive agreements.

In short, the Bermuda II Agreement, in some ways, proved to be the -

> "most anticompetitive understanding ever entered into by the United States, as it gave up in large part, multiple designation and established controlled designation. It drastically curtailed fifth and sixth freedom rights for U.S. carriers.

It established a complex regime for capacity and schedule limitations".[91]

In the writer's opinion, the main reason that Bermuda II was being so strenuously challenged in the United States was that the government chose to lay all of its tenets out on the bargaining table instead of hiding them in separate memoranda of understanding and informal executive agreements.[92] This point of view has further support in the statements of State Department and Transportation Department officials who observed that many agreements with foreign countries (particularly in South America and the Soviet Union) contain more restrictive capacity and scheduled clauses than Bermuda II does. More specifically, a Transportation Department official stated that "every bilateral agreement we have contains some sort of restrictive

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91. Driscoll, NACA, opening testimony at International Aviation Hearings before Senate Aviation Subcommittee, 95th Cong., 1st Sess. at 63-88 (1977).

92. In fact, the bilateral agreement does not always reflect the complete content of the air transport negotiations. For example, if a country negotiated the agreement on the principle of predetermination, a secret memorandum may vary that principle to one of absolute free competition; the converse is also true. See Moursy, International Air Transport and the Chicago Convention, unpublished thesis, McGill University, Montreal at 178 (1983); Gardner, "U.K. Air Services Agreements 1970-1980", 7 Air Law at 2 et seq. (1982).

clauses".[93]

The reaction to Bermuda—II by the United Kingdom was, of course, not the same as the Americans. It was evident that the British accomplished a great deal in the Agreement. Many of the new provisions put the British carriers on more of an even par with American airlines.[94] Although the opposition conservatives in Britain labelled the Agreement as a failure, the same belief was not the general consensus.[95] Most agreed that Bermuda II was the "British Revolution of 1976", as was described by Hill.[96] According to the British Secretary for Trade, this Agreement "would result in more opportunity for British airlines, less waste of resources, and real advantage to air travellers".[97]

Notwithstanding the diversity of the views expressed by both sides, a more comprehensive analysis of Bermuda

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93. Ellingsworth, "Bermuda Pact Sparks Opposition", Aviation Week & Space Tech. at 27 (August 1, 1977).

94. Hill, op. cit., note 49, at 127.

95. Journal of Commerce at 1, 4 (June 24, 1977).

96. Hill, op. cit., note 49, at 111.

97. Reed, "U.S. Views Air Pact with Britain as Victory for All", The Times (London) at 1 (June 23, 1977).

II would involve the developments and changes in the aviation policies of both nations and the situation of the interests affected by the Agreement. This entails the political influences as they impact their international aviation programmes. Shakespeare once said "policy sits above conscience". Do politics sit above policy? The question should preferably be left unanswered.

SECTION V - FROM BERMUDA II TO THE UNITED STATES LIBERAL AIR TRANSPORT AGREEMENTS

Generalities

It is evident that influential interests in the United States had not been satisfied with the Bermuda II Agreement. Within three months after its signature, the Aviation Subcommittees of both the House and Senate held hearings on the Agreement and the future direction of American international air transport policy. There was a sense of urgency because negotiations with Japan, as previously pointed out,[98] then appeared imminent and there was great concern that precise guidelines were needed to

98. See supra note 82.

avoid a second Bermuda II with the Japanese - a result that was clearly unacceptable to Congress. Once the full details of Bermuda II were made clear to President Carter and his policy advisers, the White House "was less than pleased" with the results of the Agreement.[99] The justification for this reaction by the President was explained as Carter's minimal background in aviation and hence his inability to realize the full anti-competitive impact of the Agreement until it was publicly criticized. Subsequently, President Carter wrote to Kahn, the CAB Chairman, on October 6, 1977, as follows:

> "The work you are about to undertake in negotiating bilateral agreement with Japan is of great importance.... Our central goal in international aviation should be to move toward a truly competitive system. Market forces should be the main determinant of the variety, quality and price of air services.... Our policy should be to trade opportunities rather than restrictions."[100]

This statement by the American President in 1977 set the scene for a dramatic shift in United States international air transport policy. Within less than a year of the

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99. Aviation Week & Space Tech. at 29 (September 12, 1977).

100. Extract from letter from President Carter to CAB Chairman Khan (October 6, 1977).

conclusion of Bermuda II, the Carter Administration in reaction began negotiating liberal bilateral air transport agreements with a number of nations to encourage competition through low competitive prices and to eliminate all regulatory restrictions concerning capacity, frequencies, routes and charter flights.[101]

The first liberal agreement was concluded with The Netherlands in early 1978.[102] Agreements with other countries (such as Israel, Korea, Papua New Guinea, Germany and Belgium) followed. At the end of 1979, the United States had signed about twelve of such liberal agreements with different countries including Jamaica, Fiji, Singapore, Thailand, Costa Rica and Taiwan.[103] It is also worth noting that Bermuda II was amended by way of Exchange of Notes in order to liberalize its ratemaking and charter

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101. For an up-to-date list of all liberal bilaterals, see Driscoll, "Deregulation - The U.S. Experience", 9 Int'l Bus. Law at 158 (1981); Haanappel, op. cit., note 33, in Appendix III.

102. Protocol relating to the Netherlands - U.S. Air Transport Agreement of 1957, Washington, March 31, 1978, T.I.A.S. 8998.

103. See Harbison, Liberal Bilateral Agreements of the United States, unpublished thesis, McGill University, Montreal at 12 (1982).

provisions.[104]

On March 5, 1980, a new Protocol of Consultation was signed between the United States and the United Kingdom to complete and amend Bermuda II.[105] The new agreement in principle worked out a timetable, whereby each of the countries could choose service points on the territory of the other for future operation. Sixteen new services between both countries (eight per country) would be authorized by 1984. These services were to be selected by each of the Parties on the basis of two points for operation in 1981 and only one point a year in 1982, 1983 and 1984.[106] These were the gateways to be served by direct non-stop flights. Whereas under Bermuda II multiple designation was only allowed on the New York-London and Los Angeles-London routes,[107] the amended Agreement extended multiple desig-

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104. See, in general, T.I.A.S. No. 8964 (1978); T.I.A.S. 8965 (1978); T.I.A.S. 9231 (1978); T.I.A.S. 9722 (1979).

105. T.I.A.S. No. 10059 (1980).

106. The CAB selected Pittsburg and Baltimore as the first two new gateways. Wessbergh, "Sequel to Bermuda II: New Negotiations between the U.S. and the U.K.", 15 ITA Bull. at 360 (April 21, 1980).

107. See supra note 69.

nation to the Boston-London and Miami-London routes.[108] With respect to tariffs, the two Parties agreed to pursue their policy of liberal ratemaking. However, the Bermuda II capacity clauses were left intact during the negotiations. As no changes were made concerning the question of rights beyond the partner's countries, the Americans expressed some disappointment at the new text. Finally, the 1978 Agreement concerning charter services between the two countries, which expired on March 31, 1980, could not be renewed.[109]

The 1980 negotiations were the first attempt at a general adjustment to the Bermuda II Agreement of 1977. It gave both partners substantial satisfaction. The analysis of these negotiations reveals that the British won the Gatwick battle,[110] and the Americans made a few more

108. Bornemann, "United States Route Cases", 9 ITA Bull. at 216 (March 2, 1981).

109. The interim system was, therefore, to continue on the basis of national regulations, but with the principle of reciprocity and balance being respected as far as possible. See infra Chapter V, Section II.

110. During the negotiations, the UK succeeded to promote the use of the second London airport (i.e. Gatwick). See Peguillin, "Trend in Air Freight in the North Atlantic", 5 ITA Study at 20 (1981).

moves on its new liberal deregulation policy,[111] with some prospect of reasonable progress on certain basic aspects, in particular tariffs. Finally, it should be noted that Bermuda II was further amended on November 9, 1982, granting for an interim period the British airlines rights for an additional point beyond the United States to South America and extending permanent fifth freedom rights for United States carriers between Shannon, Ireland, and Prestwick/Glasgow, Scotland.[112]

Other liberal agreements concluded by the United States during the period 1980-1982 are those with The Netherlands Antilles, Finland, New Zealand, Jordan, Philippines, Barbados and El Salvador. At the present time negotiations continue, but liberal bilaterals are slow in coming out. It is sometimes said that the United States has come to the end of the road as far as foreign acceptance of liberal agreements is concerned.[113] The end of 1980

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111. Chapter III deals in detail with the recent developments in the economic regulation of air transport in the United States.

112. For more information, see Aviation Week & Space Tech. at 27 (November 15, 1982); Kean, "Bermuda III", 8 Air Law at 117 (1983).

113. Ott, "U.S. Stiffens Negotiations Stance", Aviation

reveals stagnation in the conclusion of such agreements. Since that time only Barbados and El Salvador have concluded new liberal bilaterals with the United States.[114]

It is, in fact, highly unlikely that the full force of their competitive provisions will be acceptable to the majority of States. Nonetheless they have characteristics which will ensure their impact on the international air transport structure for the foreseeable future; some of their elements will inevitably find their way into other bilateral agreements and national policies. It is, therefore, worth examining briefly the most important features of the new United States "open skies" regime. Most of these characteristics are analyzed in the chapters to follow.

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Week & Space Tech. at 28 (April 9, 1984); infra Chapter III, Section III.

114. U.S.-Barbados Agreement, April 1982, T.I.A.S. No. 10370; U.S.-El Salvador Agreement, November 1982, T.I.A.S. No. 10488.

General Characteristics of the United States Liberal Bilaterals

The new American liberal policy aims at concluding agreements that rely on "market forces" to determine capacity, frequency, entry, and, above all, pricing. In exchange for the acceptance of these rights by foreign countries, the United States is willing to grant major route concessions as consideration.[115] The new bilateral agreements thus exchange "opportunities rather than restrictions".[116]

During the period 1978-1982, the United States concluded more than twenty liberal bilateral air transport agreements with different countries. Several forms of agreement have been used to introduce the various liberal regimes. These include "Agreed Memoranda of Understanding", "Exchanges of Diplomatic Notes", "Protocols" in addition to the comprehensive form of full "Air Services (or Transport) Agreement". It is, of course, not so much the form of the

115. Driscoll, op. cit., note 101, at 158; Rivoal, "The New U.S. Open Skies Policy, ITA Bull. at 101 (February 5, 1979).

116. Wassenbergh, "Towards a New Model Bilateral Air Transport Services Agreement", 3 Air Law at 198 (1978).

agreements which is important, but their contents. However, it should be realized that liberal bilaterals may differ considerably from one to another. The differences may be quite substantial or may be a matter of detail. There is no formal classification, but some agreements are totally liberal, whereas others are only liberal in certain respects, e.g. as to pricing, but not to capacity and charters. Also, some superficially less liberal agreements become more liberal in their application, for instance where their neighbouring markets are regulated with few restrictions; the converse is also true. In general, liberal bilaterals have the following features which correspond to the objectives set by the United States:

1. Multiple Designation

The principle of multiple designation refers to the designation by a State of more than one national carrier to operate on individual international routes. Although before the Second World War, Pan American was actually treated as a "chosen instrument", the Americans finally rejected this concept in international air transport.[117] A United

117. Stoffel, op. cit., note 39, at 132.

States objective was now "flexibility to designate multiple U.S. airlines in international air markets".[118]

There is no doubt that multiple designation provides more opportunities to the American carriers to compete in international markets. Contrary to most nations of the world with only one or sometimes two international airlines (chosen instrument(s)), there are many carriers in the United States (both scheduled and charter) which are engaged in international air services. The American Policy of 1978 explained this as follows:

> "The designation of new U.S. airlines in international markets that will support additional service is a way to create a more competitive environment and thus encourage improved services and competitive pricing."[119]

Multiple designation was allowed under the Bermuda I scheme but, with the exception of the United States after the mid-1960's, single designation became the norm. The Bermuda II Agreement had been explicit in imposing designation restrictions, which the Americans were now anxious to avoid in any future agreement. It is worth noting here that

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118. U.S. Policy for the Conduct of International Air Transportation Negotiations, August 21, 1978, 14 Weekly Composition of Presidential Documents at 1412-1463.

119. Id. (Explanation of Objectives).

each of the liberal bilaterals differs, first, from Bermuda I in providing for designation for both scheduled and charter carriers.[120] This now provided for greater stability for charter-designated airlines, which had in the past been authorized in a broad variety of informal methods, permitting equally informal ad hoc disapproval.[121] The more modern agreements affirm the traditional United States policy respecting multiple designation:

> "Each Party shall have the right to designate as many airlines as it wishes to conduct international air transportation in accordance with this Agreement and to withdraw or alter such designations."[122]

Finally, one has to take into account the influence of the multiple permissive route awards policy adopted by the United States since deregulation[123] on the designation of carriers. Under this new form of route authoriza-

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120. Note: Nowhere in the texts is charter defined.

121. See infra Chapter V, Section I.

122. See, e.g., U.S.-Barbados Agreement, Article 3(1), supra note 114. However, to keep the distinction between the two forms of operation, these new agreements contain two annexes; Annex I deals with the scheduled services while Annex II covers the charter operations.

123. This policy was first formulated domestically in CAB Order 78-4-121 (the Oakland Service Case) and then was exported to international markets.

tion that applied to scheduled services, designation is to be not only multiple but also permissive. However, no public service obligation is imposed on the scheduled airline to perform the specific service authorized. This means first that a large number of potential entrants may be designated and secondly that incumbent airlines may exit and re-enter markets as well.

This permissive aspect is presumably considered to be within the prerogative of any country designating its carriers. However, by diminishing the public service responsibility of scheduled operations, it is highly likely that the system will erode the more traditional scheduled operations and multistop services, through emphasis of point-to-point pricing advantages.[124] Insofar as this permissive concept is a departure from recognized norms of "scheduled" behaviour in all other bilaterals which have been negotiated since 1946, this position may be questionable and has never been resolved. It is a creation of the United States CAB and extends to international routes a controversial domestic policy. A good illustration of multiple and permissive route awards is the United States-

124. See Cruz, Chairman of Philippine Airlines, Testimony in CAB's IATA Show Cause Order Proceedings Docket 32851.

Benelux Low Fare Proceeding,[125] decided shortly after the conclusion of liberal bilateral agreements with Belgium and The Netherlands.[126]

2. Liberal Route Structure

Air Transport routes, in general are granted only if there is a benefit to the country involved. According to the traditional United States air policy, routes were granted if they could produce "an equitable exchange of economic benefits, expressed in terms of route rights having approximately equal market value".[127] The International Air Transportation Competition Act of 1979 speaks of "rights" or "benefits of similar magnitude".[128] This evaluation, however, is apparently put aside in the many cases where

125. CAB Docket 30790; Order 78-6-97 (13 June, 1978).

126. In that Proceeding the CAB awarded scheduled U.S.-Benelux routes to a large number of American carriers, some of which were former charter only airlines, CAB Order 79-10-16 (August 29, 1979).

127. Loy, "Bilateral Air Transport Agreements: Some Problems in Finding a Fair Route Exchange", in Freedom of the Air, Ed. by McWhinney and Bradley, Sijthoff at 179 (1968).

128. See infra Chapter III.

routes are granted for political, military or other non-aviation considerations.[129]

Routes - in the form of bilateral grants - play an important part in "buying" the new system. The Americans, in their liberal agreements, have granted new gateways in exchange for the acceptance by third countries of the liberal pricing and capacity policy. Some of the strongest criticisms of the United States policy from within have been directed at these "route-giveaways", the trading of "soft" for "hard" rights.[130] In fact, the net result of this trade might only favour third countries.

A liberal route structure, stricto sensu, is based on the complete freedom of flight exchange between the contracting Parties.[131] In this regard, the United States Policy of 1978 was implicitly aimed at greater access for American carriers. The objective was expressed in terms of:

> "Encouragement of maximum travelar and shipper access to international markets by authorizing more cities for non-stop or

129. See Wassenbergh, op. cit., note 3, at 26; supra note 32.

130. Aviation Week & Space Tech. at 28 (April 9, 1984); Senate Subcommittee Hearings.

131. Cheng, op. cit., note 35, at 393.

> direct service, and by improving the integration of domestic and international airlines service."[132]

In the liberal bilaterals this free route structure is only granted to American airlines which may serve foreign countries from any point in the United States, via any intermediate point and to any point beyond. In return, the foreign carriers are allowed to serve additional cities in the United States. In some agreements additional gateways for scheduled air service are granted in the form of "rover-points". Under this form, the bilateral agreement grants to a foreign country a certain number of unspecified gateways in the United States, to be selected by that foreign country with the possibility of changing them upon relatively short notice.[133] Other liberal agreements grant to foreign countries specified new gateways in the United States to be phased in over a certain number of years.[134]

In general, most liberal bilateral air transport agreements state that "each designated airline may, on any

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132. Supra note 118.

133. See, e.g., U.S.-Jamaica Protocol of 1979 (Article 3).

134. The U.S.-West German Protocol of 1978 provides (in Article 3) that all the future routes will not be granted unless all the provisions of the Protocol are observed.

or all flights and at its option, operate flights in either or both directions and without directional or geographic limitation, serve points on the routes in any order, and omit stops at any point or points outside the territory of the Party which has designated that airline, without loss of any right to carry traffic otherwise permissible under this Agreement",[135] provided the service begins or terminates in the territory of the contracing Party designating the airline.[136]

3. Free Exchange of Scheduled Sixth Freedom Traffic Rights

No limitation on the carriage of sixth freedom traffic for scheduled international air services,[137] i.e. traffic carried by an airline from one foreign country via its home country to another foreign country. For example,

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135. Annex I, Section 2, of a U.S. Model liberal agreement, cited in Bogosian, "Aviation Negotiations and the U.S. Model Agreement", 46 J. Air L. & Com. at 1035 (1981).

136. Id. Annex I, Section 3.

137. This is another concession to small countries which do not have much of their own traffic (e.g. Belgium and The Netherlands) for accepting U.S. liberal policies. See infra Chapter III, Section III.

United States originating traffic which The Netherlands' carrier KLM would pick up in New York City, carry to Amsterdam and onwards from there on a connecting flight to another point in Europe or elsewhere.

4. Free Determination of Capacity, Frequencies and Types of Aircraft

Free determination by the designated airlines of both contracting States of capacity, frequency of flights and types of aircraft to be used, both for scheduled and for charter air services, and unhindered by the ex post facto capacity review clauses of the Bermuda I-type agreement.[138]

5. New Pricing Clauses

Encouragement of low tariffs (fares and rates), set by individual airlines on the basis of the forces of the marketplace, without reference to the Tariff Coordinating Conferences of IATA (the use of which, by the way, is not specifically forbidden; the liberal agreement between the United States and Germany, as shown later in this study, is

138. See infra Chapter VI, Section II.

exceptional in that it specifically provides for the possible use of the IATA Conferences). Also, there is minimal governmental interference in tariff matters, both for scheduled and for charter services.[139]

6. Prohibition of Discriminatory and Unfair Competitive Practices

With pricing and capacity virtually without control, it became essential that the carriers operating under liberal agreements should enjoy equal access to each others mar ets (e.g., be able to use computer reservation services on the same terms as their competitors). Consequently, these agreements prohibit discriminatory and unfair competitive practices.[140]

7. Inclusion of Provisions on Charter Flights

Country of origin charterworthiness rules, sometimes (like in the agreement with Belgium) supplemented by the rule that charters performed by the carriers of one contracting Party out of the territory of the other contrac-

139. See infra Chapter VII, Section III.

140. Infra Chapter VI, Section II.

ting Party may also be performed on the basis of the national charter rules of those carriers ("double country of origin" or "country of designation rule"; e.g., this means, as discussed later, that Belgian charter carriers can perform United States originating charters either pursuant to American or to Belgian charterworthiness rules).[141]

To conclude this section, it may appear appropriate to briefly mention the major reasons for entering into liberal bilaterals with the United States. It seems that many nations which have accepted such open competitive policy have done so for a price. At times this price has been the desire of certain countries to receive first time access to the United States, or to have liberal access to various American gateways for their carriers - particularly in the sunbelt (e.g. Los Angeles, Miami, Atlanta). Other countries, however, have been attracted to these new agreements because they impose no restrictions on the carriage of

141. In other words, the availability of inexpensive charter service is encouraged and charterworthiness is generally governed by the country of origin rule. See infra Chapter V, Section IV. Finally, one has to remember that these U.S. liberal agreements also call for a promotion of competitive cargo services. See the U.S.-Belgium Protocol.

sixth freedom traffic.[142] In addition to the question of traffic rights, it appears that fear of diversion of traffic to neighbouring nations which already had concluded liberal bilaterals with the United States, may have played a role or sometimes may have put pressure on certain States to also accept a liberal bilateral.[143] Generally, one can assume that foreign countries will only enter into liberal bilateral air transport agreements if such action is to their advantage, i.e. for the commercial benefit of their own national airlines.

PRELIMINARY CONCLUSION

The Chicago Convention of 1944, coupled with the Bermuda I Agreement of 1946, established a basic framework for international aviation in the post-World War II era. A survey of aviation history reveals that the post-war bilateral air services agreement has generally drawn its form

142. See, e.g., Belgium, Singapore and The Netherlands liberal bilaterals.

143. Germany, e.g., entered into a liberal bilateral with U.S. after the conclusion of the liberal agreement with The Netherlands. See Chapter III, Section III.

from the Chicago model[144] but has derived its substance with respect to economic rights from the Bermuda I Agreement. In fact, the framework had major gaps, but nonetheless, it worked fairly well for over thirty years, until new forces arose calling for its revision.

The Bermuda II Agreement of 1977, however, failed (unlike its predecessor Bermuda I) to become a model for future worldwide bilateral air transport agreements. This may be so because Bermuda II was concluded in the midst of many secondary bilaterals, whereas Bermuda I was agreed at a time when there were very few agreements in force. In addition to that, Bermuda II was considered to be geared almost exclusively to the United Kingdom-United States market. Finally and more importantly, the United States, after the conclusion of Bermuda II, became strongly committed to a more freely competitive policy in international air transport than that contained in the Bermuda II Agreement.

Under the new American "open skies" policy, some twenty liberal bilaterals have been concluded by the United States in the period 1978-1982. In general, a liberal agreement might work well for the North Atlantic. However, it is certainly not acceptable on a worldwide basis. This

144. See supra, Chapter I (footnote 74).

liberalization has been introduced mainly on routes between industrial countries or between them and the "new industrial countries" (South-East Asian countries in particular) because such countries generate the bulk of the traffic. Third world countries operate mostly in other markets and are often high-cost operators which makes it extremely difficult for them to adopt liberal policies. These recent trends are discussed in greater detail in the Chapter to follow.

CHAPTER III

DEREGULATION - IS IT CONTAGIOUS?

"A recession is when you have to tighten your belt; depression is when you have no belt to tighten; when you've lost your trousers, you're in the airline business."

- Sir Adam Thomson

SECTION I - INTRODUCTION AND BACKGROUND

General View

From time immemorial, man has dreamed of flying. Greek mythology tells the narration of Daedalus who, to escape prison in Crete, made wings for himself and his son Icarus. Daedalus flew safely to Sicily, but Icarus was lost at sea when his wings melted from rising too close to the sun.[1]

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1. Kane & Vose, Air Transportation, Sixth Edition at 2-1 (1977). On the history of aviation, see, in general, Johnson, Rights in Air Space at 7 et seq. (1965); Gibbs-Smith, Aviation: An Historical Survey at 105-158 (1970); Kuhn, "The Beginning of an Aerial Law", Am.

Many centuries passed before man finally did ~~fly~~. It was only 200 years ago that the Montgolfier brothers invented the first practical ballon; and the first manned flight took place on the western outskirts of Paris on November 21, 1783.[2] The first air voyage in the United States was almost 10 years later.[3] Another 110 years were to pass before the first flight in a power-drive machine. On December 18, 1903, at Kitty Hawk in North Carolina, Orville Wright was airborne for 12 seconds, and later that day his brother Willbur was aloft for 59 seconds, for a distance of 852 feet.

During the some 80 years that followed, the airplane and air transportation have become routine and commonplace. While a few of commentators occasionally marvel at the technological advances, they are mostly taken for granted. Convenience, comfort and cost have become the modern-day concerns.

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J. Int'l L., Vol. 4 at 111 (1910); Brooks, The World's Airliners (1962).

2. Id. It was witnessed by Benjamin Franklin who, when asked what use it was, made the famous reply: "What use is a newborn baby?".

3. The flight was made by Jean Pierre Blanchard (a Frenchman) from Philadelphia, Pennsylvania to Woodbury, New Jersey on Jan. 9, 1793. The ballon lifted up in the presence of President Washington.

It is no secret to note that along the way, as has happened with other modes of public transportation, governments stepped in to regulate and control. Regulatory control of air transportation may, for instance, be inspired by national defense considerations, national economic infrastructure considerations, considerations pertaining to foreign earning power and national prestige considerations.[4] It should also be kept in mind that in economic systems which do not adhere to the free enterprise doctrine, government regulation of air transportation may be simply explained as part of the overall governmental involvement in the economy as a whole.

The United States government experimented with a variety of approaches from 1918, when airmail service was inaugurated by Army pilots, to 1938 when the Civil Aeronautics Act became law. For the next 40 years, the public utility type provisions and policies of that law, as administered by the Civil Aeronautics Board (with occasional intervention by the American President in decisions affecting international air transportation) shaped the development of air transportation service and the air transport

4. For a good discussion of these considerations, see Gidwitz, The Politics of International Air Transport at 19-32 (1980).

industry.[5]

During those 40 years, a veritable explosion of growth and service improvement ensued in the United States. But gradually, more and more academic economists began to question whether the public would be better served by a more competitive regime, and in 1976-77 the CAB itself began to ease its tight controls on entry and pricing. In the wake of a rapid build-up of Administration and Congressional fervor, the Airline Deregulation Act was passed in October 1978.[6] In this sense, one has always to remember that United States deregulation, be it domestic or international, has been a "bipartisan" effort, drawing political support from both Democrates and Republicans.

The underlying philosophy of the Deregulation Act of 1978 was that "free market forces" would better assure adequate and efficient air transport service for this now

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5. For an interesting discussion of the history of U.S. aviation policy, see Lowenfeld, Aviation Law, Matthew Bender, New York, 1972 (2nd ed., 1981).

6. The Airline Deregulation Act of 1978, Pub. L. No. 95-504, 92 Stat. 1705, codified in 49 U.S.C., Para, 1301 et seq. See also "Aviation Law: Recent Developments: The Airline Deregulation Act of 1978", Harv. Int'l L.J. at 385 (1979); Dubuc, "Significant Legislative Developments in the Field of Aviation Law", 45 J. Air L. & Com. at 21 (1979).

mature industry.[7] Under the Act, on a phased basis, the various regulatory controls have been relaxed and eliminated; and the CAB itself was disbanded at the end of 1984.[8] In terms of government intervention, the domestic airline industry is now no more regulated than are shoe stores or computer manufacturers.

With respect to international air service, however, the United States shares authority with other countries, because (unlike international shipping rules) each sovereign has sole and complete jurisdiction over its own territory.[9] Therefore, no air carrier may embark or disembark traffic at any airport without the sovereign's consent, and it must comply with the terms and conditions issued by or agreed with that sovereign. As a consequence a vast network of intergovernmental bilaterals underlays all international air service, and United States Congress comprehended that it could not effectively deregulate unilaterally. In addition, Congress recognized that the "open" market that, assumedly, exists within the United States, assuredly does not exist

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7. See Sandell, "Deregulation - Has it Finally Arrived?", 44 J. Air L. & Com. at 809-810 (1979).

8. See The Gazette, Section A at 1 (Jan. 2, 1985).

9. Article 1 of the 1944 Chicago Convention. See supra, Chapter I.

outside.[10] Foreign governments typically own and assist, or at least protect, their flag airlines, and often regulate and restrict the commercial opportunities of non-national competitors. Thus, the 1978 Deregulation Act dealt only peripherally with international air transportation. Surprisingly, however, Congress in early 1980 passed the International Air Transportation Competition Act of 1979,[11] which emphasized its desire for a more competitive international regime.

Dealing with international air transportation, one should also mention that even before Congress acted, there was a procompetitive drive that reached into the international arena. Although there were earlier spasmodic efforts, it was not until 1977 that the American government initiated a major campaign to induce other governments to ease their restrictive attitudes by offering them in exchange increased access to the huge United States market-

10. See Taneja, U.S. International Aviation Policy at 56-60 (1980); Nammack, "U.S. International Aviation Policy: Same Goal, New Attitudes", Air Transport World at 23 (May 1982).

11. International Air Transportation Competition Act of 1979, Feb. 15, 1980, Pub. L. 96-192, 94 Stat. 35. See also Wessberge, "The New U.S. Legislation on International Air Transport", 44 ITA Bull. at 1027 (Dec. 24, 1979); Dubuc & Jones, "Significant Legislative Developments in 1979 in the Field of Aviation Law", 45 J. Air L. & Com. at 942 (1980).

place.[12] Despite widespread skepticism about United States aviation policy, a number of countries - primarily those that felt their national air carriers had more to gain than to lose - moved partway toward the American objectives of "open skies".[13]

The 1978 Deregulation Act, which mainly dealt with domestic air services, realized the requirement for a period of adjustment to the new objectives, and provided for gradual elimination of regulatory controls, with "sunset" of the CAB set six years in the future.[14] Shortly after the Act's passage, however, deep studies on the "success" and "failure" of deregulation began to appear, with some concluding that it was too soon to tell - particularly in the light of such external factors: the intervening recession; the temporary grounding of the DC-10's; the air traffic controller's strike; and massive fuel cost increases in

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12. See Lowenfeld & Mendelsohn, "Economics, Politics and Law: Recent Developments in the World of International Air Charters", 44 J. Air L. & Com. at 480, 488-492 (1979).

13. For those countries and the general characteristics of the U.S. liberal bilaterals, see supra, Chapter II, Section V.

14. 49 U.S. C.A., Para. 1551(a)(4) (Supp. 1979).

1979.[15] But now, some 7 years have passed; the CAB closed shop on December 31, 1984; and any distorting impact of the "external" factors has greatly moderated. It is timely to assess the results of domestic deregulation and increased international competition.

To better understand the implications of developments and trends emerging from the deregulated environment, it is essential to have a clear picture of what preceded. There are, in the writer's view, at least two reasons why a discussion of United States deregulation of aviation should be preceded by a brief description of the pre-deregulation regulatory system in place in the United States for a period of some 40 years. First, deregulation was in part a reaction to perceived "excesses" of the regulatory period. Secondly, and more fundamentally, American regulatory system, even before deregulation, was more flexible and less stringent than other systems in the world. The following discussion thus summarizes that 40-year experience with the regu-

15. For a discussion of the various arguments for and against deregulation, see, e.g., Dempsey, "The Rise and Fall of the CAB - Opening Wide the Floodgate of Entry", in Bradley & Haanappel Eds., Government Regulation of Air Transport at 303-308 (1982); Lazar, Deregulation of the Canadian Airline Industry: A Charade, Key Porter Books, Toronto at 26-30 (1984); Brenner, Leet & Schott, Airline Deregulation, ENO Foundation for Transportation, INC., Westport at 10-12 (1985) (hereinafter cited as ENO Study on Deregulation).

lated system that has been discarded, and the major developments during those four decades.

The Forty-Year Regulatory Scheme

After earlier floundering, a stable policy of air regulation began with economic regulatory provisions of the Civil Aeronautics Act of 1938. Forty years of experience under the Act set the stage for the current era of deregulation.

The Civil Aeronautics Act of 1938[16]

The industry's pleas for controls on entry and price competition clearly repeated a pattern recurring throughout the history of economic regulation in the United States. In the late 19th century, the railroads supported the Interstate Commerce Act as a device for protecting their market position. Large truckers and barge operators used similar arguments to limit price competition and obtain route protection in the 1930's. The legislative history of the Civil Aeronautics Act simply comported with one of the

16. 52 Stat. 973 (1938) (current version at U.S.C. Para. 1301-1542 (1976)). The name of the Act was subsequently changed to the Federal Aviation Act.

principal theories of economic regulation: that, as a rule, restrictive legislation is secured by the affected industry and is designed and administered primarily for its benefit.[17]

The main impetus for paving the way to pass this comprehensive statute was the industry's desire for protection and financial stability. Government control and economic regulation were therefore regarded, at that time, as necessary to foster the growth of an infant industry. In this sense, "the proponents of more comprehensive air carrier regulation found unity in their fear of uncharted future".[18]

The 1938 Act created the Civil Aeronautics Authority, an independent regulatory agency composed of five members (with no more than three from the same political party), appointed by the President subject to the advice and consent of the Senate. The Civil Aeronautics Authority would be redesignated as the Civil Aeronautics Board (CAB)

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17. Stigler, "The Theory of Economic Regulation", 2 Bell J. Econ. & Mgmt. Sci. at 3 (1971). It is believed that Stigler oversimplified, indeed distorted in some cases, the reasons for these laws. However, his interpretation was generally accepted by the deregulation movement.

18. Jones, "Licensing of Domestic Air Transportation", 30 J. Air L. & Com. at 115 (1965).

in 1940. Since then, the CAB had the responsibility of administering the economic regulations of the airlines.[19] The Board was guided by a Declaration of Policy in the exercise of its powers and duties. The following policies, inter alia, were to be considered in the public interest and in accordance with public convenience and necessity:

> (a) The encouragement and development of an air transportation system properly adopted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;
>
> (b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure the highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by, air carrier;
>
> (c) The promotion of adequate, economical and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;
>
> (d) Competition to the extent necessary to assure the sound development of an air transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;
>
> (e) The regulation of air commerce in such manner as to best promote its develop-

19. 49 U.S.C. Para. 1321 (1976).

ment and safety; and

(f) The encouragement and development of civil aeronautics.

These guidelines and the other economic provisions of the 1938 Act were, almost without change, reenacted in the Federal Aviation Act of 1958.[20] Together the 1938 and 1958 Acts and the Board they created, formed the backbone of the regulatory system which dominated the American air transport industry from 1938 to 1978. This system has often been referred to as one of "regulated competition",[21] i.e. in the words of the 1938 and 1958 Acts "competition to the extent necessary to assure the sound development of an air transportation system."

The above-quoted guidelines (Declaration of Policy), however, were strongly criticized by many as being both vague and inconsistent.[22] Criticisms stemmed from

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20. Pub. L. No. 85-726, 72 Stat. 731 (codified at 49 U.S.C. Para. 1301-1542 (1976)).

21. See, e.g., Haanappel, An Analysis of U.S. Deregulation of Air Transport and its Inferences for a More Liberal Air Transport Policy in Europe, Council of Europe, Doc. AS/EC(36) 3 at 6 (May 21, 1984); Callison, "Airline Deregulation - Only Partially a Hoax", 45 J. Air L. & Com. at 966-969 (1980).

22. See, e.g., Caves, Air Transport and Its Regulators, MA, Harvard University Press, Cambridge at 126-127 (1962); Dupre, "A Thinking Person's Guide to Entry/Exit Deregulation in the Airline Industry", Transp. L.J. at 303 (1977); Sandell, op. cit., note 7, at 801.

the fact that the Authority/Board was expected to both promote and regulate air transportation. It was pointed out that achievement of some of the expressed goals, such as that of sound economic conditions, might directly conflict with other objectives, such as the prevention of unjust price discrimination. This conflict left the CAB with considerable discretion in its administration of the Act. Board's decisions were final, subject to court review, but even here the Act provided that the "findings of fact by the CAB , if supported by substantial evidence, shall be conclusive." This was an essential barrier to efforts to overturn CAB decisions, particularly since the "findings" in most route and rate proceedings (which were at the heart of the regulatory scheme) were predictive or judgmental in character.

Other sections of the 1938 Act dealt with controls over exit and entry, fares and routes. The CAB's authority over entry into the airline industry was rooted in its power to issue a "certificate of public convenience and necessity"[23] which was required before an airline might engage in the business of public air transportation. The Policy

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23. The CAB had limited authority to grant U.S. (but not foreign) airlines "exemptions" from the certificate requirement, and from certain other requirements of the Act.

standards discussed above were used in deciding whether or not the certificate was required by public convenience and necessity.[24] In addition, the applicants were required to convince CAB that they were "fit, willing and able" to perform the proposed transportation "properly". Any abandonment or suspension of service also required prior Board approval.[25]

As to tariffs, the Act required every carrier subject to Board regulation to file its tariff schedule with the CAB to keep it open for public inspection and to observe it so long as it was in effect. Tariffs could only be changed on 30 day's notice unless the Board permitted a more rapid change.

Finally, route control was exercised by placing restrictive conditions on the certificates issued by the

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24. The 1938 Act did contain a "grandfather" provision to assure the award of certificates to existing air carrier for operations they were performing. It is a significant and often criticized aspect of CAB policy that, between 1938 and 1978, no new "trunk" (i.e. major) carriers were certificated to engage in scheduled air transport. In the meantime, some of those existing "trunk" carriers merged with the result that in 1978 there were eleven such carriers left, of which the "big four" were American, Eastern, TWA and United.

25. However, the CAB did not have authority to restrict the rights of airlines to change schedules or equipment. As to CAB policy toward non-scheduled ("supplemental") airlines, see infra Chapter V, Section II.

Board. Certificates specified the points between which the transportation was authorized and the type of service to be rendered.

While rate and route regulation had the most direct and visible impact on public service, the CAB also exercised a broad range of other economic controls over the air transportation industry. Hence, it could (and did), prescribe in detail the accounts and records to be maintained by airlines, and the reports to be submitted. Agreements between airlines had to be filed with the Board, whose approval was required for certain specified interlocking relationships, and for air transport related mergers,[26] consolidations and acquisitions of control. At the same time, however, CAB approval of such agreements granted immunity from the general antitrust laws.[27] The CAB also was authorized to

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26. Mergers were most often inspired by the "failing business doctrine", i.e. a strong carrier taking over a flatering one. The major value of a merger for the stronger carrier was to obtain the route authority, the route network of the weaker carrier. For a discussion of this concept and the other agreements, see Intravia, American Aviation Policy: Capacity, Competition and Regulation, unpublished thesis, McGill University (1977).

27. Antitrust statutes, such as the Sherman and Clayton Acts, prohibit commercial practices (e.g. price-fixing agreement, capacity agreements etc...) in restraint of trade and make them subject to both civil and criminal penalties. For regulated airlines these agreements, normally illegal, could, however, become permissible

investigate and terminate "unfair or deceptive practices or unfair methods of competition in air transportation".[28]

It should, however, be noted that regulation of international air services differed from domestic air services. Most significantly, CAB decisions with regard to international route applications of both United States and foreign carriers were subject to "the approval of the President".[29] The Supreme Court eventually held the President's decision to be unreviewable. In addition, foreign carriers applications were generally bottomed on pre-existing bilaterals that granted route rights to the airline designated by the foreign governments.[30] This alone was almost invariably considered sufficient to meet the statutory standard applicable to the grant of foreign airline route applications (that the proposed transportation

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if approved by the CAB upon a "public interest" test. See, for instance, "Show Cause Order", infra, Chapter VII, Section I.

28. See infra Chapter VI, Section II.

29. For more details, see O'Connor, An Introduction to Airline Economics, Praeger Publishers, New York at 8, 30 et seq. (1982). In this respect, one has to remember that foreign carriers were not permitted to engage in domestic traffic (i.e. cabotage).

30. Technically, foreign airlines applied for and received "permits" rather than "certificates".

"will be in the public interest").

As with its authority over international routes, the CAB had to share international rate authority with foreign governments. The obvious complexities were greatly ameliorated, in practice, by broad worldwide acceptance of the International Air Transport Association (IATA) as a forum for meetings and rate agreements among international carriers, subject to approval by interested governments.

Pre-Deregulation Major Developments

During the period from 1938 to 1978, the CAB had, on the whole, faithfully and competently carried out its vision of the basic statutory directives of the 1938 Act. It succeeded in expanding scheduled service to every city of appreciable size in the United States, encouraged route and service competition among the existing carriers, and promoted the growth of the industry. With few exceptions, the defects in such regulatory scheme were not the result of erroneous Board policy, but were instead inevitable products of the Act itself and the Board's difficulties in reconciling the conflicting mandates imposed on it by Congress.[31]

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31. Kelleher, "Deregulation and the Practicing Attorney",

In fact, the 40 years of regulation witnessed truly phenomenal growth in both domestic and international air transportation.[32]

Domestically, United States carriers received, over the years, many new route authorizations. The number of certificated domestic route miles of the leading carriers[33] had remarkably increased during this period. The number of American city pairs connected by convenient carrier service grew in step with expanded route miles.

Internationally, limited service was provided in 1938 by a handful of scheduled United States carriers (primarily Pan American Airways and its related companies) and some 6 significant foreign-flag carriers. By 1978 these numbers had increased to 21 American - and 73 foreign-flag carriers.[34]

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44 J. Air L. & Com. at 268-270 (1978).

32. Most of the following data are taken from the CAB Report to Congress (Fiscal Year 1978); ENO Study on Deregulation, op. cit., note 15; Mandell, Financing the Capital Requirements of the U.S. Airline in the 1980's, Lexington Books, Toronto (1979).

33. I.e., American, Delta, Eastern, Northwest, TWA and United.

34. See supra note 32. It should be noted here that a substantial number of U.S. and foreign charter carriers also operated internationally in 1978.

Air passenger traffic grew at an amazing rate. The number of passengers (domestic and international) carried by United States carriers increased from a little over one million in 1938 to almost 267 million in 1978. Also, in 1978, foreign carriers carried some 16 million passengers to or from the United States.

With increase in average length of journey, there was an even greater growth in United States carrier revenue passengers miles, from 533 million in 1938 to 219 billion in 1978.[35]

There is no doubt therefore that the air transport industry grew to be one of the nation's major industries. Over the four-decade period, revenue increased from $58 million to $22.8 billion. Total airline assets rose from $100 million in 1938 to over $17 billion in 1978.

From another angle, the air transport industry also became a major employer. Total direct airline employment increased from about 13,000 to well over 300,000. Furthermore, hundreds of thousands of employees held jobs in the manufacturing of civil transport aircraft, engines, and accessories; at airports; in travel agencies; and in the vast range of other related service, supply and support

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35. One passenger travelling one mile is equivalent to one revenue passenger mile.

activities.

In this regard, one has to remember that the air transport industry had met the Congressional objective of assisting the "national defense". As reported by the CAB in its 1942 Annual Report to Congress:

> "Pearl Harbor brought real meaning and new force to the national defense standard so wisely written into the Civil Aeronautics Act during peacetime...."

The air carriers, domestic and international, went on war-time footing, and contributed remarkably to the war effort. Consequently, they helped break the Berlin blockade, provided important lift in the Korean and Vietnam wars, and provided emergency and evacuation assistance in dozens of other critical situations around the globe. The formal Civil Reserve Air fleet, available with crews for military callup at defined stages of national emergency, contained in 1978 some 298 commercial aircraft, of which 216 were large intercontinental units.[36]

Significantly, technological development was spectacular, not only in aircraft but also in the air transport system infrastructure as well. Concentrating just on air-

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36. The U.S. air transport system, by far the largest in the world, was indeed the best in just about every respect. And this contributed, in no small measure, to the worldwide supremacy of the U.S. aerospace industry, exporting as it did many billions of dollars worth of aircraft, engines, parts, etc....

craft, however, this four-decade period witnessed evolution from the propellor driven 21-passenger DC-3 to the 400-seat widebodied Boeing 747 jet that in addition to a full passenger load has cargo capacity equal to the full load-carrying ability of five DC-3's. Aircraft non-stop range, with full payload, grew to over 6,000 miles. Accompanying these developments, were great improvements in safety, speed, comfort, and overall convenience for the users of air service. A truly integrated "air transport system" was developed that enabled the public to buy tickets from virtually any airline for travel on multiple airlines, and to check baggage at point of origin for delivery at destination regardless of how many airplane or airline changes were made enroute.

Over the four-decade period of air regulation, there were also changes in the structure of the United States airline industry. A number of the original "grandfather" trunk-line carriers merged with or were acquired by other airlines;[37] there were no bankruptcies among them. During the same period, new categories of carriers, as well as new carriers, were licensed, including, 8 local service and 3 all cargo companies, and 10 charter airlines by 1978. This latter group played a significant role in offering lower priced transportation and developed a strong presence

37. See supra (footnotes 24 and 26).

in certain markets, particularly for transatlantic flights.[38]

In only one respect did the airlines perform poorly. Compared with other broad industry groups, the airline business was not very remunerative. Coincidentally, 1978, the last year of regulation, was by a wide margin the most profitable year yet experienced by the industry.[39]

Notwithstanding problems and inadequacies that existed, few could reasonably deny the brilliant success of the 1938 regulatory scheme. There was a high level of public satisfaction with United States airlines. A United States News and World Report survey revealed that out of 21 defined categories of United States industry, the airlines were rated the highest for "giving the customer good value for money".[40]

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38. For more details, see infra Chapter V, Section II.

39. See ENO Study on Deregulation, op. cit., note 15, at 7.

40. See "Public Trust in Business: It's Increasing But-", U.S. News and World Report at 28 (June 27, 1977).

SECTION II - THE ADVENT OF UNITED STATES DOMESTIC DEREGULATION

Despite of the remarkable developments that had taken place under the regulatory scheme created in 1938, and wide public satisfaction with the airline system, air regulation gradually came under increasing criticism, particularly from academic economists. This gained momentum in the mid-1970s and, between 1977 and 1979, a veritable revolution was accomplished in both domestic and international United States air transport policy. This Section is an overview of the developments in the American domestic aviation industry; the next will examine the feasibility and the desirability of exporting the principles of an internal policy to the international arena.

The Steps Towards Deregulation

Although deregulation of the industry had never been seriously considered by Congress until mid-1970s, the problems resulting from the system under the 1938 Act had been discussed since the Truman Administration. The basic issue, as might be expected, was the relative desirability of free competition in this industry, as compared with the tight government control of entry, exit, pricing and other

competitive matters. A study by Lucille Keyes in 1951 concluded that there was no available evidence of any need, or valid argument, for federal control over entry, or for government protection of individual carrier revenues.[41] She was later to write that protective regulation was no more essential to assure "the provision of an adequate supply of air transport services...than it is necessary to secure an adequate supply of soaps, doorknobs, or automobiles".[42]

Richard Caves, in his classic study of air transportation in 1962, concluded that "the air transport has characteristics of market structure that would bring market performance of reasonable quality without any economic regulation.[43]

In 1972, a study by William Fruhan contended that the CAB actually exercised more direct control over a carrier's competitive position and "relative profitability than management does". With pricing removed as a competitive tool, the airlines have been forced to compete in terms

41. Keyes, Federal Control of Entry into Air Transportation, MA, Harvard University Press, Cambridge (1951).

42. Keyes, "A Reconsideration of Federal Control of Entry into Air Transportation", 22 J. Air L. & Com. at 197 (1955).

43. Caves, op. cit., note 22, at 171.

of scheduling and inflight amenities, such as meals, movies and onboard pubs.[44]

Notwithstanding increasing criticisms and occasional Congressional grumbles that led to minor regulatory changes, it was not until 1975 that certain factors began combining for a successful push to deregulation. Traditional American distrust of government regulation in general became focused on air transportation through various economic, political and regulatory developments.

Adversity struck the industry in 1970, when a large increase in capacity (resulting from the advent of wide-bodied jet aircraft) coincided with a serious economic recession. This, in turn, led to widely criticized CAB regulatory policies, including a four-year moratorium on all new route cases, and approval of a series of agreements among carriers to limit capacity over certain major routes.[45] In the meantime, CAB pricing policies were increasingly viewed as fostering inefficiency, higher costs

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44. Fruhan, The Fight for a Competitive Advantage at 51-67 (1972).

45. See, in general, Basedow, "Common Carriers: Continuity and Disintegration in U.S. Transportation Law", 18 European Transport Law at 352-54 (1983); Intravia, op. cit., note 26.

and higher prices.[46] Critics pointed to the experience of several intrastate carriers in Texas and California (not regulated by the CAB) that charged lower per mile fares for comparable distances than the CAB regulated airlines, and operated more profitably.[47]

After 1970, inflation became a major concern for the whole nation and, due to increasing fuel cost, particularly for the airline industry.[48] There were of course external factors - most notably the OPEC coup of 1973 with respect to oil prices, and the disintegration of the international monetary system. But there was also a loss of confidence in the economic managers, whose predictions and formulae seemed to bear less and less resemblance to what

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46. A major target of attack was the tendency of some airlines to engage in schedule competition, which reduced load factors (occupancy rates).

47. See, e.g., Jordan, Airline Regulation in America: Effects and Imperfections at 112 et seq. (1970); Keeler, "Airline Regulation and Market Performance", 3 Bell J. Econ. & Mgmt. Sci. at 399 et seq. (1972); Breyer, "Analyzing Regulatory Failure: Mismatches, Less Restrictive Alternatives and Reform", 92 Harv. L. Rev. at 588 (1978-79).

48. In September 1974, President Ford convened a "Summit Conference on Inflation" which unanimously recommended deregulation as means of lowering prices. See Behrman, "Civil Aeronautics Board", in Wilson Ed., The Politics of Regulation at 102-103 (1980).

people could see and feel.[49] In general, airline operating costs soared, while traffic was again hurt by recession. One result was a series of fare increases.[50] Deregulation promised one remedy among others in the form of lower transportation fares.

In the United States, the post-Watergate public had become sceptical of the practices of "big government" generally and of economic regulatory agencies in particular.[51] It was an ideal environment for deregulation theories to gain support. Therefore, it was not surprising that on taking office in January 1977, President Carter followed the advice of his White House aviation advisors to support strongly the domestic aviation deregulation movement already under way for its twofold political value: a regulatory agency could be dismantled, fulfilling election promises of "small government", while at the same time voters would be pleased by cheaper air fares.

But even before Carter's election, two influential

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49. See Lowenfeld, "Deregulation of Aviation in the United States", in Kean Ed., Essays in Air Law at 156 (1982).

50. Average domestic passenger mile increased form 5.50¢ in 1967 to 7.79¢ in 1976. 38% of that increase occurred in the single year 1973 to 1974, see the CAB Report to Congress 1977.

51. See Lowenfeld, op. cit., note 5, at 5-2.

reports were released towards deregulation. One was a special CAB staff study on regulatory reform, dated July 1975. It advocated an end to the rigorous regulation of fares, rates and entry by the CAB:

> "...protective entry control, exit control, and public utility-type price regulation under the Federal Aviation Act are not justified by the underlying cost and demand characteristics of commercial air transportation. The industry is naturally competitive, not monopolistic."[52]

The study recommended that protective entry, exit and public utility-price control in "domestic air transportation" be eliminated within three to five years by statutory amendment. It is worth noting here the specific reference to "domestic air transportation". In fact, the last paragraph of the introductory portion of the Report clarified this point by stating that "attention has been directed primarily to the 50-State non-specialist industry.... The study has not focussed upon international air transportation, where the institutional and legal framework is of an entirely different nature".

At about this same time, an influential study was released by the Subcommittee on Administrative Practice and Procedure of the United States Senate Judiciary Committee,

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52. Reprinted in 41 J. Air L. & Com. at 601 (1975).

headed by Senator Edward Kennedy.[53] The Report recommended that the focus of the nation's aviation policy should shift from promoting the well-being of the aviation industry to making its service economically available to more of American public. To achieve this end, the Report stated that "increased competition would force down prices...if carriers were free to set prices...firms would experiment in offering consumers different combinations of price and service." The CAB practices, the Report concluded, while effective in promoting industry growth, technological improvement and reasonable industry profits, had not been effective in maintaining lower prices.

With the sudden mushrooming of anti-regulation sentiment, in October 1975 President Ford made public proposed legislation on regulatory reform under the title "Aviation Act of 1975". The legislation was aimed at stimulating price competition, eliminating entry barriers to new markets and altering the basic function and purpose of the CAB.[54] Although the proposed Act was not adopted by

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53. Oversight of the CAB Practices and Procedures: Hearings Before the Subcom. on Administrative Practice and Procedure of the Senate Com. on the Judiciary, 94 Cong., 1st Sess. (1975) (hereinafter cited as Kennedy Hearings).

54. Proposed Aviation Act of 1975, S. 2551, HR. 10261, 94th Cong., 1st Sess. (1975).

Congress, it started the legislative process that culminated in the Airline Deregulation Act of 1978.

It should also be noted that even before the 1978 Act's passage, the CAB itself, as earlier shown, had begun its own administrative journey on the road to deregulation. First, the Ford Administration in March 1975 appointed John Robson as Chairman of the CAB to succeed Chairman Robert Timm, who had been a strong advocate of increased regulation and an enthusiastic supporter of the capacity limitation agreements. With Robson in office, the CAB started to relax its regulatory policies. Supplemental airlines were given greater opportunities by expanding the scope of permissible charters. The CAB also permitted greater carrier flexibility to reduce fares. These first cautious moves gained indeed enormous momentum under Chairman Alfred Kahn, appointed by President Carter in June 1977. Schuman, who was influential in choosing Kahn, said she was convinced by his:

> "seven page exposition on the airline industry, why it is regulated, how it is regulated, and why it ought to be deregulated...he was the perfect fellow who had the theory, a fine economist, as I am sure most of you know, but he could describe this issue in a way that some poor, tired overworked young woman could even understand."[55]

Although Kahn left office only in late 1978 (to become

55. Mary Schuman, Aviation Daily (Sept. 4, 1977).

Chairman of President Carter's anti-inflation program), his efforts at the CAB will not soon be forgotten. He was never slow to tell the public and the airlines, what he hoped to do:

> "So what I am trying to do, to put it in the broadest possible terms, is to remove the meddling, protective and obstructionist hand of government, and to restore this industry, insofar as the law permits, to the rule of the market."[56]

Under the leadership of Kahn, the CAB commenced its first major low-fare route case, in which it expressly requested parties to explore whether the authority to enter a market should be permissive and whether more than one applicant should be granted authority in each city-pair market.[57] A year later, the CAB went further and proposed to award multiple authority to all qualified applicants by non-hearing show cause proceedings, eliminating the lengthy hearings of the comparative selection process and the restriction of entry to a single carrier.[58] There was also far greater receptivity to fare reductions. In this regard, the CAB had decided (by the late fall of 1977) not to intervene through promulgation of discount fare policies and had adopted the view that allowing airlines to implement their own pricing strategies could significantly improve the

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56. See Aviation Week & Space Tech. at 37 (Mar. 6, 1978).

57. Chicago-Midway Low-Fare Route Proceeding, 78 CAB 454 (1978).

58. Oakland Service Case, 78 CAB 593 (1978).

economic performance of the industry.[59] Chairman Kahn stressed this point by stating:

> "The law prohibits departure from tariffs, but departure from tariffs are good for competition. Rebating as we see it is a consequence of non-competitive rate levels, and the best theoretical remedy is to reduce fares."[60]

The Administration's stance added support for deregulation, but the movement was also helped by improved industry profitability. Some attributed the industry's profitability to limited deregulation of the CAB-regulated carriers.[61] One has to admit, however, that during the period from 1976 to 1978 the industry was merely experiencing its traditional cyclical upturn after the sharp downturn in 1975.

There was, of course, major resistance from most air carriers to any significant relaxation of regulation. Their main concern was that deregulation, consisting of nothing more than "untried theories and unbridled rhetoric", would disrupt the industry, doing away with the system which

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59. See Bailey, Graham & Kaplan, Deregulation the Airlines - An Economic Analysis 121 (1983).

60. Cited in Business Week at 128 (July 24, 1978).

61. See, e.g., Kelleher, "Deregulation and the Troglodytes - How the Airlines Met Adam Smith", 50 J. Air L. & Com., No. 2 at 302-303 (1985); Sandell, op. cit., note 7, at 808.

had taken almost 40 years to develop.[62] Opposition also stemmed from airline labor unions and financial institutions with investments in the industry. Their arguments covered a broad range of concerns, including:[63]

- deregulation would jeopardize safety and interlining as well as waste fuel;[64]
- concentration of services on denser routes would lead to overcapacity on those routes and a diminution of services on less popular ones, especially to and from small communities;
- more competition would reduce the number of passengers per flight and services would be wastefully duplicated;
- destructive and predatory price competition could occur and only the major carriers could weather these circumstances;
- reduced ability to re-equip and to finance other available technological advances; and
- adverse impact on airline employees.

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62. Taneja, Airlines in Transition at 1-2 (1981). In response to these criticisms, Kahn said: "That's our dilemma", supra note 60.

63. The following arguments are taken from IATA Study on Aviation Deregulation, Geneva at 6-8 (Dec. 1983); Taneja, op. cit., note 10, at 29 et seq.; Sandell, op. cit., note 7, at 808 et seq.

64. Although these criticisms are rarely heard today, the other arguments mentioned hereafter are still being expressed.

Notwithstanding the validity of these arguments, the Congress continued to hold discussions and hearings relating to economic regulations of the domestic air transport industry.[65] Realizing the momentum achieved by the deregulation movement, many air carriers changed positions and began to support deregulation. According to a former Chairman of the CAB, the airlines "had to join the deregulators or perhaps go down trying to lick them".[66] The result was that the advocates of deregulation won and both the House and the Senate passed their own versions of the regulatory bills, which ultimately led to the Airline Deregulation Act of 1978.[67]

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65. It is significant to note that while what finally emerged as the 1978 Airline Deregulation Act, a mini-deregulation bill was passed by Congress with little fanfare or public notice. This was the deregulation of domestic all-cargo service, which became law in November 1977. In short, the Air Cargo Reform Act liberalized air carrier (route) entry for all-cargo scheduled air services and relaxed regulatory controls over air cargo rates. Moreover, in March 1978 another deregulation law dealing with cargo was passed, which gave supplemental carriers the same immediate opportunity to obtain certificates for scheduled all-cargo service that was made available to scheduled carriers by the 1977 law.

66. Browne, "The Strong Air Ocean", in Air Service in the 1980s - Setting the Stage at 5 (Sept. 30, 1980).

67. See supra note 6.

The Deregulation Act of 1978

The basic principle of deregulation is the removal of the hand of government from the market. Its essential aim is to allow the free play of competitive forces, tempered only by strict application of antitrust and consumer protection laws. In this sense, deregulation of United States domestic aviation meant dropping government control over entry/exit, supply and pricing as well as eliminating the State's regulatory authority. The economic theory on which it is based was summed up by Kahn in 1977 as "wherever competition is feasible, it is, for all its imperfections, superior to regulation as a means of serving the public interest...."[68]

The 1978 Deregulation Act deals primarily with domestic air transportation. There was still major practical recognition of the fact that no one government could by itself deregulate international service. As a consequence, United States Congress established a new "Declaration of Policy" applicable only to domestic operations; the pre-existing policy statement continued to apply to internation-

68. Alfred Kahn, CAB Chairman, Testimony to House Public Workers Committee's Aviation Subcommittee (Oct. 5, 1977).

al operations.

The overriding theme of the 1978 Act was competition. There was to be maximum reliance on competition to bring about the objectives of efficiency, innovation, low prices and price/service options, while still providing the needed air transportation system. "Competitive market forces" and "actual and potential competition" were "to encourage efficient and well-managed" carriers "to earn adequate profits and to attract capital". One member of Congress expressed the reason for the change in attitude in this way:

> "Historically, aviation was a fledgeling industry which needed help and financial guarantees, and the public needed controls for safety. But we're 40 years from that point and there is no need for the CAB to be overly protective of a $100 billion industry."[69]

At the same time, however, Congress was responsive to small community needs and pressures, and called for "maintenance of a comprehensive and convenient system of continuous scheduled interstate and overseas airline services for small communities and for isolated areas in the United States, with direct Federal assistance where appropriate".[70]

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69. Cohen, "Regulatory Report/CAB's New Chairman Charts an Independent Course", 7 Nat'l J. at 1566 (1975), quoting Rep. Norman Y. Mineta.

70. Pub. L. No. 95-504, Para. 3(a), 92 Stat. 1706 (1978).

Restrictions on domestic scheduled service entry were to be gradually eliminated over the following several years, with complete elimination at the end of 1981. From 1978 to December 31, 1981, a transitional period, certificates to engage in scheduled air transport were issued to United States airlines upon the finding that certificate applicants were "fit, willing and able" to provide the air transportation in question and that such transportation was not inconsistent with the "public convenience and necessity". Further, the 1978 Act stated a presumption of such "consistency". The burden was on any opponents of the applicant to demonstrate any inconsistency with the "public convenience and necessity".

From the end of 1981, certificates have been issued upon a mere finding of the applicant being "fit, willing and able" without any reference to "public convenience and necessity". "Fit, willing and able" is a unitary concept and meant that the applicant possesses the necessary managerial skills and technical ability to operate safely, that he has submitted a sound financial plan and sound air service proposals and that he is willing to abide by the law and regulations. In this regard, it should be noted that from the end of 1981, certificates no longer specify terminal and intermediate points to be served by airlines. Also, since that time and except for "essential air transporta-

tion"[71] carriers may withdraw service on routes at will. In fact and for all practical purposes, all air carriers (and virtually all would-be-carriers) are now free to serve, or to cease serving, any and all domestic routes and cities.

Congress did recognize the need to assure continued service to communities that might otherwise have been abandoned or provided an unacceptable service level under deregulation. The traditional subsidy program for local service carriers, which was directed more toward sustaining carriers than to maintaining specific service to small communities,[72] will be phased out by the end of 1985, and a new program of subsidy to guarantee "essential air transportation"[73] to specific communities was established. All cities named in any certificate are automatically eligible, and unless the city is served by at least two airlines, the CAB (or now the Department of Transportation (DOT)) is required to determine what and how much service is "essential". "Essential air transporation" at any given city is

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71. Explained below.

72. For a good discussion on the effects to these locations, see Miller, Handbook on the Airline Deregulation at 14 et seq. (1981).

73. See also infra at 152.

defined as scheduled service, at specific minimum frequency and at fair rates, to one or more other cities with which it has a community of interest. Whenever it is found that a city will not receive essential air transportation without subsidy inducement, applications to perform subsidized service must be sought, and an award made at an established rate of compensation. Under the 1978 Act, this program is to continue until 1988, but under budget pressure the Reagan Administration has proposed its termination in 1985.[74]

As to tariffs, the 1978 Act distinguished between the period 1978 to the end of 1982, and 1983 and beyond. In the transitional period, the CAB retained suspension and prescription power over domestic air fares. Such power, however, could, save for certain exceptions, not be used if a proposed fare increase or decrease fell within a suspension-free "zone of reasonableness". That zone was determined by reference to the semi-annually adjusted "Standard Industry Fare Level" (SIFL) and ran from 5% above the SIFL to 50% under the SIFL. This means that the CAB, within this zone, could not suspend as unreasonable any fare as much as 5% higher or 50% lower than the SIFL.[75] From

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74. Eno Study on Deregulation, op. cit., note 15, at 9.

75. The lower boundary of the "zone" might have been further reduced by regulation. The CAB adopted such a

January 1, 1983, CAB domestic fare control was completely abolished. With it came an abolition of control over certain ancillary conditions and practices, such as conditions of contract and carriage. Also, the duty of carriers to provide for joint fares and rates with other air carriers and the CAB's control thereof came to an end.

The 1978 Act also substantially reduced the CAB's authority over aviation related antitrust matters including mergers, acquisitions, agreements and interlocking relationships. For those transactions still requiring CAB approval, the standard for approval was more closely aligned to general antitrust principles. For example, the Act retained CAB authority to approve airlines mergers and inter-carrier agreements, and to relieve them from the operation of the antitrust laws. However, procedures and conditions under which this was possible were tightened.[76] Finally, the Act specifically prohibited capacity reduction and price-fixing agreements between carriers in domestic air transport.

It is also significant that due to strong labor

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regulation in 1980, resulting in full downward fare flexibility.

76. See Haanappel, op. cit., note 21, at 16; Miller, op. cit., note 72, at 15-16.

opposition to the 1978 Act, an employee protection program was established. This program provides, inter alia, for temporary monthly assistance payments to airline employees who were employed in 1978 and are deprived of employment or adversely affected in pay as a result of an airline bankruptcy or major contraction during the period 1978-1988.

To conclude this sub-section, it is appropriate to repeat that the most dramatic of the 1978 Act's provisions, was the CAB's demise ("sunset"). On January 1, 1985, the CAB ceased to exist altogether, and its authority that it possessed including that over foreign air transportation was transferred to the United States DOT. First, however, late in 1984, Congress made some changes to the 1978 Act, mainly to assure continued consumer protection and to transfer authority over mergers and agreements to the DOT rather than to the Department of Justice (DOJ).[77]

Post-Deregulation Major Developments

Since the above-mentioned regulatory reforms pertained particularly to industry entry and exit, and to airline pricing, and since they were intended to benefit both airlines and users, it seems appropriate to discuss the

77. See Flight International at 1025 (Oct. 20, 1984).

developments of United States domestic aviation deregulation under the following headings: changes in industry structure; airline pricing levels; and airline costs and operating performance.

Changes in Industry Structure

Prior to 1978 deregulation, the airline industry's structure composed of four main groups of carriers:[78]

- Trunk lines: carriers serving the principal high density routes, and in particular the long-haul routes.
- Local service lines: carriers serving only short-haul routes. While some of these routes had high traffic volume, most were of comparatively thin traffic volumes.
- Intrastate jet lines: carriers particularly operating within the states of California and Texas. By avoiding interstate routes, they were able to operate scheduled service without a CAB route certificate.
- Commuter airlines: carriers operating only short-haul routes with small piston or turbo-prop aircraft. By limiting themselves to aircraft of 30-seat size or less, these lines were exempted from the need for CAB route certification.

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78. In addition to the following groups, there were two specialized categories of carriers - one concentrating on charters, and one concentrating entirely on all-cargo operations. The charter group has largely shifted into scheduled service since deregulation.

Since the 1978 deregulation onwards, United States airlines have essentially been free to fly where they want and when they want. The number of certificated scheduled airlines has gone up from about 36 in 1978 to about 98 in 1983.[79] Of these "new entrants" 22 are brand new; the others are former intrastate carriers having entered interstate air transport markets; former "supplemental" airlines having received authority to engage in scheduled air transport; and former commuter carriers having expanded their route networks.[80] As a consequence, the designations of the various groups of carriers had to change in keeping with the radical changes in their scope. The terms "trunk" and "local service" were abandoned. In their place, new categories of carriers were based strictly on gross revenue.

Since January 1981, United States domestic airlines have thus been reclassified as follows: "major", "national" and "regional" airlines. The "majors" are all former "trunk" carriers, plus Republic and U.S. Air.[81] The

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79. See, e.g., Meyer & Oster, Deregulation and the New Airline Entrepreneurs, the MIT Press, Cambridge, Massachusetts London (1984).

80. It should also be noted that between 1977 and 1982, the number of carriers certified for all-cargo operations increased from 10 to 109.

81. Republic was born out of a merger, and US Air is a

"national" group includes some former large "local service" carriers, such as Frontier, Ozark and Piedmont; former intrastate carriers, such as Air California, Air Florida, Pacific Southwest and Southwest; and also two former "supplementals", Capitol and World. The "regional" group is primarily composed of former commuter airlines and a number of "new entrants".

The net result has been a significant shift in the market position of former trunk lines and other carrier groups. Specifically, the increase in the number of certificated airlines has caused a decline in traffic share of the former "trunk" carriers; their share of the American domestic air passenger transport market went down from 90.8% in 1978 to 80.5% in 1983.[82] At the same time, the share of the former "local service" carriers went up from 6.5% to 10.2%; that of the "intrastate" carriers from 2% to 3.6%; that of the commuter carriers from 0.8% to 1.0%; and the share of the "new entrants" amounted to 2.8% in 1983.[83]

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very successful former "local service" carrier.

82. ENO Study on Deregulation, op. cit., note 15, at 18 (Table 4).

83. Staff of the Civil Aeronautics Board, CAB Draft Report at 13 (Table 1.2) (1984) (hereinafter cited as 1984 CAB Draft Report).

In other words, roughly one-third half of the trunk market share loss was picked up by former "local service" carriers, and the remaining was divided between former "intrastate" carriers and "new entrants".

To keep these market share shifts in perspective, it should be recognized that the previous shares were so dominated by "trunk" airlines that even after the sharply disparate growth rates of deregulation, those carriers still remain in a position of dominance. Therefore, the 1983 trunk market share of 80.5% is still a reasonable measure of dominance by normal standards.[84]

In fact, the newly classified major and national airlines have concentrated their efforts at creating "hub-and-spoke" operations.[85] An airline will feed traffic into its major hub(s), and if the hub(s) is (are) not the destination of the traffic, the airline will carry it onwards via the hub(s) to its ultimate destination. Commuter carriers will also carry short-haul traffic to hubs and deliver it over to major or national airlines for onward

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84. Also, some of the strongest financial results during 1984 were recorded by the largest carriers, and their equipment and route expansion programs indicate that they will retain and probably increase their dominance.

85. For more details on the "hub-and-spoke" operations, see Haanappel, op. cit., note 21, at 19 et seq.

medium - or long-haul transportation. In this respect, the main advantage of the highly developed airline hub-and-spoke operation is that it provides an enormous "multiplier" effect as to the number of city-pairs an airline can serve with a given amount of flight mileage. There are, of course, also some negative aspects of these operations. The very objective of getting as many inter-connections as possible forces highly peaked, and potentially highly congested, waves of nearly simultaneous arrivals and departures of dozens of flights.[86]

"Hubbing", i.e., air routes from all directions running to one and the same airport, has altered route patterns considerably. There has been an important increase in air service between large and medium hubs, between medium and small hubs, and particularly between medium and medium hubs.[87] However, there has been a decrease in air service to nonhub destinations.[88] This reflects the

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86. For the various advantages and disadvantages of these operation, see Haanappel, op. cit., note 21, at 19 et seq.; ENO Study on Deregulation, op. cit., note 15, at 77 (Figure 9) et seq., 84 et seq.

87. In the last category a 17.4% increase over the period 1977-82.

88. The most dramatic decrease has been one of 21.2% (1977-82) between nonhub and nonhub destinations.

development of small community to small community traffic being carried via transfer points at hubs. As to small community air service generally, the "essential air transportation program" (mentioned previously) has so far maintained service to "eligible" communities. To a large extent, such service has often been taken over from the certificated carriers by commuter carriers.[89] Recently, however, there have been indications that many communities receiving subsidized service will lose service completely upon the expiration of this subsidy, if it is not replaced with some other form of assistance. Thus, a January 1984 testimony of the National Association of State Aviation Officials stated that "unless these markets are stimulated by the use of better (larger, more comfortable) airplanes, and unless the carriers are provided with promotional expertise and funding, most present EAS (essential air service) communities will lose all scheduled air service in 1988".

Finally, the most controversial aspect of the structural changes is the continuing turnover of airlines within the industry with new airlines starting up, while

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89. As of Oct. 1982, 88 out of the 555 "eligible" communities were receiving subsidized air service. Out of 203 "non-eligible" communities, however, no less than 102, or 50% lost air service between 1977-82. See Hardaway, "Transportation Deregulation (1976-84): Turning the Tide", in Transp. L. J., Vol. XIV, NO. 1 at 144-46 (1985).

other carriers are dropping out. The greatest volatility in this respect has been among commuter airlines;[90] but there also has been considerable turnover among jet carriers. As summarized by the President of American Airlines:

> "Between 1978 and the end of 1983, the number of scheduled interstate carriers in the U.S. increased from 36 to 123. Carriers certificated since 1978 now carry about 10% of all domestic airline passengers. During the same period, 34 carriers went bankrupt and another 69 airlines ceased operations. Of these totals, scheduled airlines of some substance accounted for 15 of the bankruptcies and 10 of the closures."[91]

The situation, however, still remains fluid. The true dynamics of the structural changes cannot be accurately gauged by simply comparing one date with another. In the meantime, the outlook for a continuous injection of "new entrant" airlines has become more dim. The ease of entry has been weakened by the lessened enthusiasm of investors, in the face of the high mortality rate of the newer airlines. Recent experience has shown that most of the new airlines have found it a greater challenge than originally contemplated, to overcome the market identity and other advantages of the larger carriers. It is, therefore, quite

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90. See supra note 79 at 139 et seq.

91. Speech delivered by Robert L. Grandall before the Wings Club, Sept. 1, 1984.

possible that the industry will in a few more years "shake down" to a small number of strong major airlines, a few "specialized" regional carriers and a commuter industry that remains independent, but with varying degrees of affiliation with larger carriers. Perhaps this format could provide the equilibrium that allows the industry to remain profitable - but it is unclear what this type of industry will mean in terms of the fare levels and services for the public.

Airline Pricing Levels

A comparative analysis of pricing in the airline industry is difficult because of the number of independent economic factors that must be taken into account. A few such factors are the general inflation rate, particular rates of inflation (such as fuel), recessionary pressures and technological advances. Many studies examining all these factors have concluded that regulation caused artificially high fares. Keeler's 1972 study of coach fares revealed that fares were 45 to 84% higher than what the unregulated competitive fares would be.[92] The 1975 Kennedy Hearings revealed that regulated fares were 40 to 100% too high, and that excess fares amounted up to $3.5

92. Keeler, op. cit., note 47, at 421.

billion.[93]

Therefore, the widely-held public impression is that deregulation would lower airline fares. That impression, however, is only partially valid. The fact of life in such an environment (as discussed below) is that deregulated fares are lower on some routes, but higher on others as a result of deregulation. Fares have been in a continuing state of change since deregulation, often varying dramatically from one date to the next for the same trip. On some routes, fares have been reduced by deregulation to levels below those of 1978 - but on other routes, fares have doubled or more in this same period.

In general, deregulated airline pricing can be classified into three major periods: (a) the 4½ years from the start of deregulation through mid-1983; (b) the period from mid-1983 to mid-1984; and (c) the period from mid-1984 on.

During the first period, airline fares in aggregate never caught up with the inflation of airline unit costs - because of fare wars and other forms of yield erosion.[94]

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93. See Kennedy Hearings, op. cit., note 53.

94. For specific details of the relationship between cost and yield trends during this period, see ENO Study on Deregulation, op. cit., note 15, at 33-34 (Table 7 and Figure 4).

In the first full year of deregulation (1979), yield increases were much below the fuel-triggered jump in costs. This yield gap narrowed in 1980, but then widened again through 1981 to mid-1983. Particularly noteworthy was the extreme impact of widespread fare wars in the first quarter of 1983, which prevented airlines charging fares which reflected true operating costs. According to economists, the net effect of fare wars has for sustained periods held overall average yields below the level needed to fully cover all costs.

From the consumer's point of view, the lag in fares through mid-1983 meant, of course, that fares were lower than would have been justified by costs. This has sometimes been pointed to as a consumer benefit. It must, however, be recognized as at most a transient benefit, since below-cost pricing cannot be sustained indefinitely, except at peril to industry viability.

Following the disastrous financial losses of the first half of 1983, fare wars abated, and yields started climbing.[95] Gradually during the second half of this year, the gap between yield and cost increase narrowed, and was fully overcome by the end of 1983. In the first quarter of 1984, the gap had not only been eliminated, but yield

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95. 1984 CAB Draft Report, op. cit., note 83, at 20.

increases actually moved ahead of inflation costs.

In the following quarters of 1984, new outbreaks of competitive price cutting caused yields to start to soften again, although not nearly to the degree evident in early 1983. The agressive expansion of certain low-fare services by new entrants (particularly by People Express) cut into yields on many major routes. However, at least through the fall of 1984, this had not developed into full-fledged fare wars.

The preceding brief discussion, dealing with overall industry-wide averages, leads one to say that some passengers have been getting great bargains, while others are forced to bear substantial fare increases. Unfortunately, the volatility of deregulated airline pricing makes it difficult to present a detailed fully accurate picture of all of the route-by-route variations; one can only present illustrative comparisons.

This volatility is indeed so great that large carriers get massive computer runs every morning, to find out on which routes competitors changed their fares the day before, and to decide on what competitive response to take. In this respect, a front-page article in the Wall Street Journal (August 24, 1984) correctly described the daily pricing chaos:

> "Delta assigns 147 employees to track maze of prices.... On a typical day, the

> tariff department compares at least 5,000 industry pricing changes against Delta's more than 70,000 fares.... The day begins at 7am EDT, when a Delta computer begins disgorging a list, sometimes several hundred pages long, showing the new fares filed the prior day with Air Tariff Publishing Co. On a recent Monday, the list showed United Airlines with 5,282 (changes), Republic Airlines with 2,946, and Eastern Airlines with 3,709."

In this environment, any comparison of fares developed at one point in time will be out-of-date within days, or at most weeks. The terms and conditions of fares also vary widely from market to market, further complicating comparison. It is, however, generally believed that, on a per-mile basis, fares tend to be lower in long-haul than in short-haul markets. Secondly, fares tend to be higher on low-density than on high-density routes. Thirdly, fares tend to be lower in more competitive than in less competitive markets. Finally, fares tend to be higher in business markets than in tourist markets. As to fare types, it became evident after deregulation that most passengers prefer to travel at discount fares which, of course, are much lower than coach (i.e. domestic economy) fares.[96] It should also be noted that, except during fare wars when unrestricted discounts are offered, discount fares tend to

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96. Discount traffic as percent of total reached 87% in March 1983. See ATA data, as reported by Salomon Brothers, Airline Newsletter at 5 (Sept. 24, 1984).

be subject to restrictions. They are often capacity controlled, i.e. only a certain percentage of available seats is reserved for discount fare passengers; they are often subject to advance booking and payment requirements; and they may be subject to minimum stay requirements. On the other hand, unrestricted low fares are often offered by no frills "new entrants". These low fares may distinguish between higher peak-period and lower off-peak period prices. Moreover, some airlines offer reduced connecting fares in markets where non-stop service is available, so as to encourage passengers to travel via their hubs. Finally and of particular importance, many airlines have instituted "frequent traveller" bonus programs. Under these programs, frequent travellers enroll in the programs of one or more individual airlines and become eligible to "earn" future free or reduced travel in proportion to the amount of mileage they build up on trips with those carriers.[97]

Fare variation has become an on-going phenomenon of deregulation. Some growing awareness of this has been evident in comments in the general press. For example, New York Times stated in its September 21, 1984 issue:

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97. In fact, these programs encourage travellers, particularly frequent business travellers, to use one and the same airline, whenever possible. For the disadvantages of such programs, see Travel Weekly at 1 (Aug. 16, 1984).

> "Although the nation's major airlines are making a big noise in slashing prices on some of their heavily traveled routes, they are quietly raising prices on a number of other runs."

Similarly, it was pointed out:

> "Despite the great visibility in the press of the fare activity taking place in key markets, these markets account for roughly 25% of system traffic. The fact remains that the vast majority of 'invisible' markets in this country are not attacked by low-fare carriers."[98]

It seems unlikely that the disparity in pricing between different routes will, over time, be eliminated in the airline free market. As for fare wars, and their debilitating impact on profitability, one can only speculate on the future outlook. For a time in 1983/84, it appeared that the industry had learned a sufficiently painful lesson on this score, to produce a welcome lull in fare wars. The mid-1984 resumption of yield erosion, however, again raises the possibility that there are fundamental pressures in this industry that lead to recurrent uneconomic pricing in the free market.

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98. "First Boston Research", Airline Newsletter at 2 (Sept. 20, 1984).

Airline Costs and Operating Performance

Commenting on the relationship of deregulation to airline performance, it was stated early in 1984 that: "As a result of these (deregulatory) changes, the airline industry is becoming more efficient as competition requires carriers to make the most productive use of their resources."[99] This agrees with widely held views, and there is some basis for this conclusion. At the same time, however, there is an element of over-statement in attributing this short-term cost-reduction experience (shown hereafter) to the deregulated environment. The fact is that some of the less visible but nevertheless significant changes brought about by deregulation have affected costs and performance negatively.

It was pointed out that, between 1978 and 1983, average cost per seat-mile for the industry increased from 4.72¢ to 7.00¢ - an increase of almost 48%.[100] This was close to, but slightly below, the rise in the Consumer Price Index (CPI)[101] which increased by about 53% during the

99. CAB Report to Congress (Jan. 1984).

100. See ENO Study on Deregulation, op. cit., note 15, at 26 (Table 5).

101. The CPI is a statistical measure of the change in the

same 5-year period. The fact that the airlines were able to keep their seat-mile cost increase below the level of general national inflation was a significant accomplishment, considering the special significance of fuel cost to airline operation and the extraordinary jump in fuel prices that started in 1979.

During the same period, the average price of airline fuel more than doubled (from 39¢ to 89¢ per gallon). The total fuel bill increased from $4 billion in 1978 to $8.6 billion in 1983 for the major and national airlines.[102] As a percentage of total operating cost, fuel increased from 20% in 1978 to 25% by 1983.

In the face of the major jump in this cost element, airlines have made important efforts to cut their costs and increase productivity. Recent emphasis has often been placed on cutting the costs of labor. This can be illustrated in part by the fact that many of the "new entrant" airlines have had non-unionized labor (pilots, cabin crew,

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price of goods and services in major expenditure items such as clothing, health, food, housing, recreation and transportation for all urban consumers is used here for broad perspective of overall inflation during this period.

102. 1984 CAB Draft Report, op. cit., note 83, at 20; Office of Economic Analysis, CAB, "Competition and the Airlines: An Evaluation of Deregulation" at 8 (1982) (hereinafter cited as 1982 CAB Report).

etc.) costing up to 50% less than unionized labor. Such dramatic differences in labor costs were highlighted in a recent article:

> "Last year the 'majors' and the 'nationals' paid each worker an average of $42,000; by contrast a group of 'new entrants' - Pacific Express, People Express, Muse, Midway and Jet America - paid only $22,000. The average People Express pilot gets under $30,000 a year; his counterpart at TWA, with no more responsibility, gets about $104,000."[103]

This, of course, gives the non-unionized airlines an essential cost-competitive advantage over the unionized carriers. Moreover, as a partially related element, deregulation has encouraged employee equity ownership of airlines. For example, part of the explanation for People Express' success has been attributed to the fact that stock ownership is a requisite for employment, giving every employee an equity stake in the company.

Overall domestic United States productivity, apart from cost decreases, has also gone up in terms of load factors (i.e. the percentage of available aircraft seats occupied by passenger). For the period 1978-83, the average load factor for American domestic carriers was 60%, i.e. almost 5% higher than the average load factor between 1974-

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103. See The Economist at 5 (Aug. 25, 1984).

78.[104] In this sense, it is evident that higher load factors have been obtained, inter alia, by the use of deep discount fares, particularly in "bad" years; by real traffic growth, especially in "good" years; and by voluntary carrier restraint in adding new capacity.

Deregulation, however, has had a disappointingly mixed record with respect to the costs associated with so called "service rivalry". This refers to the cost of amenities and other aspects of service, including the cost of scheduling rivalry. Advocates of deregulation claimed that this new regime would essentially reduce the incentive for service rivalry; which was viewed as wasteful and costly.[105] It was predicted that, with deregulation, the freedom to compete in price would obviate the need to compete via service features and amenities. On the contrary, deregulation has not developed in line with that expectation. Recent experience has shown that price cuts by one airline have usually been matched by other competitors on the route, so that price alone does not remain a clear and distinguishable formula for selecting one airline over another. And hence airlines continue to find it useful to stress schedule frequency, in-flight amenities, and other

104. See Haanappel, op. cit., note 21, at 25-26.

105. See, e.g., Hardaway, op. cit., note 89, at 142.

service features, as the basis for attracting customers. A good example of this common theme can be taken from an April 1985 advertisement by Continental Airlines (aimed at People Express' low fares):

> "But our standards are much higher. Continental's low fares include great food and the kind of personal attention you can only get from a major airline...and we even give you the extra legroom you need on a long flight."

There are also a variety of other operations aspects in which the pressures of deregulation have tended to increase, rather than reduce, costs.[106] To cite but a few examples: (a) deregulation has caused a substantial increase in air traffic congestion and flight delays, which in turn have cost the airlines millions of dollars for extra fuel and crew time; (b) as shown earlier, the chaos of deregulated pricing has forced airlines to increase their staffing to keep up with the mass of daily fare changes; (c) the complexity of deregulated pricing has also increased the reservations workload; and (d) since deregulation, the intensified carrier competition (seeking favored treatment from travel agents) has led to increased commission rates.

As to the crucial issue of airline profitability, it should be noted that the financial picture since deregu-

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106. For full details, see ENO Study on Deregulation, op. cit., note 15, at 29 et seq.

lation has varied. For most of this period, however, industry earnings have been depressed. Higher fuel prices and a period of economic recession during the first years of deregulation have contributed to the industry's poor financial results. Thus far, the deregulated environment has also been characterized by destructive fare-war competition, contributing to yield erosion and operating losses.

To be specific, the first 5 years of deregulation (through 1983) presented a financial picture drastically worse than ever before experienced. Overall domestic airline performance went down from a record high in 1978 (12.9% rate of return on investment) to a record low in 1982 (3.3% rate of return on investment).[107] The airline financial performance began to grow brighter in the latter part of 1983.[108] For the 12 months ending September 30, 1984, the industry achieved an operating profit of over $2 billion.[109] Airline profits are also expected for 1985, although it is as yet uncertain whether these profits will be sufficient to cover the huge interest payments which carriers owe on debts accumulated during the "bad" years.

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107. 1982 CAB Report, op. cit., note 102, at 73.

108. U.S.A. Today at B-1 (Jan. 9, 1984).

109. ENO Study on Deregulation, op. cit., note 15, at 52 (Table 16).

So far only overall carrier performance has been discussed. In fact, performance varies widely from one airline to another, and sometimes for individual airlines from year to year. At one extreme, there have been a few airlines that have consistently done very well during this entire period of deregulation (e.g. Southwest, U.S. Air, Piedmont). At the other extreme, there have been a number of carriers whose losses pushed them into bankruptcy (e.g., Florida Airlines, Braniff International, Air Florida). Finally, there have been carriers experiencing periods of loss, followed by favourable turnarounds (e.g. American, United, New York Air). And, there have been carriers that have continued to be in a precarious position (e.g., Pan Am, Eastern).

As a conclusion to this section, one has to admit that deregulation is likely to remain controversial. Even though some 7 years have passed since airline deregulation, United States carriers still remain in transition from a highly regulated economic environment to one that is much less regulated. Deregulation has had the effect of spurring competition and providing more price-service options. Passenger fares have been reduced for some routes, but significantly increased for others. There has been reduction in labor costs and continuing movement toward greater efficiency. In less visible ways, however, deregulation

also has led to cost inefficiencies in some areas of airline operation. The airline industry has not reached an equilibrium point, and there remains much uncertainty and misunderstanding over the deregulatory impacts being experienced. This is true for United States domestic, as well as international, air transportation.

SECTION III - EXPORT OF DEREGULATION

United States initiatives towards international deregulation of air transport is more difficult to analyze than domestic deregulation. This is primarily so, because in international air transport the American government cannot act unilaterally, but must act in conjunction with other governments which may or may not share United States philosophy of the economic regulation of aviation. Therefore, the applicability of well established principles of international law and the need for foreign government cooperation have in fact made United States attempts to deregulate its international market less formal and more fragmented than on the American domestic sense.

Towards Procompetitive Strategy in United States Bilaterals

Having reluctantly signed the Bermuda II Agreement, the Carter Administration, as discussed in Chapter II, grew to view it as excessively protectionist, providing an unfair advantage for the British airlines. In addition, encouraged by the CAB's de facto deregulation of the domestic industry and the initial success of Laker's Skytrain in the London-New York market,[110] the American government began to shift the emphasis of its international aviation policy to maximize consumer price-service options through a fully competitive environment. This approach assumed that only the efficient United States airlines would survive and a strong American international air transport industry would therefore be maintained.[111]

In developing its procompetitive, laissez faire domestic aviation policy, the Carter Administration founded seven specific goals to be achieved in the negotiation of

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110. See, e.g., Weber, "Laker Airways v. the Ten Governments of the EEC", Annals of Air and Space Law at 257 et seq. (1981).

111. Taneja, Airline Planning: Corporate, Financial and Marketing at 112 (1982).

international bilateral air transport agreements:[112]

(a) To meet the needs of consumers, new and greater opportunities should be created for innovative and competitive pricing by individual airlines.

(b) Restrictions on charter operations and rules should be eliminated or at least liberalized.

(c) Restrictions on capacity, frequency, and route and operating rights for scheduled airlines should be eliminated to the extent possible.

(d) Discrimination and unfair competitive practices faced by American international carriers should be eliminated.

(e) Multiple United States airlines should be designated in markets that can support additional service.

(f) The number of gateways should be increased.

(g) The opportunity to develop and facilitate competitive air-cargo services should be increased.

These policy objectives were established to provide a general framework for American negotiators to use in forming specific strategies that would lead to the development

112. U.S. Policy for the Conduct of International Air Transportation Negotiations, August 21, 1978, 14 Weekly Composition of Presidential Documents at 1412-63.

of competitive opportunities.[113] The dynamics of the marketplace are supposed to provide to the consumer improved service at low prices resulting from economically efficient operations. Improved service and low prices are supposed to stimulate growth in traffic which, in turn, should contribute to the profitability of the industry. Finally, it should be noted that the preceding objectives had no binding legal force and, in this sense, some commentators have drawn attention to what they call "la faiblesse juridique" of this doctrine as applied to international air transport.[114] This situation had changed when these objectives were reiterated in the International Air Transportation Competition Act of 1979 (discussed below).

In fact, de jure deregulation in the international arena was initiated on March 31, 1978, when the United States signed its first "liberal" agreement with The Netherlands. Since then, the Americans have concluded some twenty liberal bilaterals. The general characteristics of these agreeements were discussed in Chapter II. It should, however, be noted that liberal agreements were relatively

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113. For further details, see Merckx, "New Trends in the International Bilateral Regulation of Air Transport", 17 European Transport Law at 117 et seq. (1982).

114. See, e.g., Naveau, Droit du Transport Aérien International, Bruxelles at 149 (1980).

widely accepted in Europe, where there was already so much competition in fares and service that a number of European governments believed their airlines would gain more from increased access to the American market than they would lose from a little more competition. Four Western European countries have entered into liberal agreements with the United States, i.e. The Netherlands, Belgium, Germany and Finland.[115] However, between the United States and other Western European nations traditional Bermuda I type bilaterals prevail. In fact, a number of major civil aviation States, in Western Europe and elsewhere, have resisted entering into liberal agreements with the Americans, i.e. for instance, Canada, France, Italy and Japan. Regardless of the fact that Canada has no liberal agreement with the United States, in the Spring of 1984, former Transport Minister Axworthy announced to the House of Commons a new Canadian air policy that incorporates some of the liberalized entry and pricing provisions of American deregulation without leaving Canadian passengers to the vagaries of a completely free market.[116] Most importantly, the

115. It should be noted that Bermuda II (between the UK-US) has, through several Memoranda, been considerably liberalized.

116. For further information, see "Canada Enacts First Phase of New Deregulation Policy", in Aviation Week &

Mulroney government is apparently moving toward complete domestic airline deregulation including, inter alia, the abolition of the Canadian Transport Commission (CTC).[117]

It is often said that United States negotiators have developed a strategy, commonly called "divide-and-conquer", to achieve the goals of American international aviation policy. Leaving aside the world community's rejection of the fundamental premise of United States policy, even stronger criticisms were raised at the method of implementation of this policy. In a lecture at MIT on June 17, 1981, CAB Chairman Cohen clarified the dynamics of the policy:

> "If one country is free to arrive at an aviation policy of its choice, it follows that two nations similarly inclined might agree to bilateral aviation relations so organized. The U.S. has adopted a procompetitive policy at home and has pursued a similar competitive policy with its partners abroad.".

This implementation strategy has, in fact, irritated many countries and has significantly reduced the chances of

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Space Tech. at 33 (May 14, 1984); "Deregulation Goes International", id. at 11 (July 2, 1984); Thoms, "Air Deregulation Comes to Canada", 6 Canadian Law Newsletter at 8-10 (July 1984).

117. See "Tories Unveil Massive Transport Deregulation", in The Gazette at A-1 (July 16, 1985); Desmarais, "Deregulation: One Year Later", Canadian Aviation at 25-28 (June 1985).

obtaining worldwide acceptance of the American philosophy.

Despite continuous denials by the United States, the international community maintained that American strategy was one of "divide-and-conquer". This hypothesis was substantiated early in 1979 by the contents of a CAB "internal document leaked to the trade press".[118] This internal memorandum discussed the potential use of market leverage to convince recalcitrant countries to adopt the American procompetitive policy. It also assumed that if a "Board Authority" was conferred on small aviation countries who were not able to grant reciprocal trade or other commensurate aviation benefits to American firms, it would result in major countries changing their civil aviation policies and "surrendering to the United States".[119] For example, Belgium could be used to put pressure on France and Italy; Korea could pressure Japan; etc.... Levine explicitly stressed this point when he stated that "a liberal comprehensive agreement (or a partial one that includes the acceptance of public charters with interchangeable country-of-origin rules a la Belgium) would provide the competitive

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118. Levine, "Civil Aeronautics Board Memo.", Aviation Daily (Mar. 8, 1979).

119. See also Majid, "Recent U.S. Aviation Policy: Need for Multilateralism Emphasized", City of London Law Review at 55 et seq. (1984).

market structure that would put the most short-term traffic pressure on both France and Italy".[120]

It is no secret now that the strategy was to pressure the recalcitrant nations into accepting the United States policy rather than experience diversion of traffic to the close, alternative destinations. This argument had particular application to Europe, where much of the North Atlantic market has traditionally been composed of American vacationers whose objective was to "see Europe". Whether such travellers arrived in Paris or Brussels was relatively less significant than the price of their airline tickets or tour packages. With excellent ground transportation within Europe and the relatively short distances involved, it was possible to take side trips to most Western European capitals.

The effect of United States liberal bilaterals has been mixed. On the negative side, most nations have not dropped their resistance to the free-for-all competitive environment. On the positive side, West Germany did change its position on multiple designation, and the United Kingdom made some concessions to the American policy in revision of the Bermuda II Agreement.[121] However, France and Italy

120. See supra note 118.

121. See supra, Chapter II, Section V. It should, however,

still remain hold-outs. Finally, in the Pacific, a liberal bilateral negotiated with South Korea has not changed Japan's attitude toward the American procompetitive policy.

The International Air Transportation Competition Act of 1979

Since it is beyond the capacity of any one nation to deregulate international air transport, United States emphasis was confined to a policy of increased competition. In early 1980 Congress passed, and the President approved, the International Air Transportation Competition Act of 1979.[122] According to the Senate Report, the Act was intended to institutionalize the competitive bilateral aviation policy practiced by the United States by providing a permanent policy for concluding bilateral negotiations.[123] In a very real sense, the legislation was

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be noted that even countries such as Israel, Jamaica and The Netherlands Antilles, which for various aspects (often unconnected with aviation) embraced U.S. new strategy in its initial phase, have sought to impose some capacity restrictions through renegotiation of their bilaterals with the U.S. in the early 1980's. See, e.g., Aviation Daily (May 31, 1983).

122. See supra note 11.

123. Senate Report, Commerce, Science and Transportation Committee, No. 96-329, Sept. 24, 1979, 2 U.S.

anticlimatic; it was basically a ratification of Carter Administration procompetitive policies, with Congress showing more concern for fair competition and the economic condition of the American carriers.[124]

The 1979 Act, however, was more cautious and realistic than the Administration's policy. In extending the procompetitive policy statement of the 1978 domestic Deregulation Act to international service, Congress recognized that the existence of a free and open international marketplace could not be assumed, and added new protective language. Thus, in placing "maximum reliance on competitive market forces" to provide the needed air transportation system and to encourage the financial well-being of efficient carriers, the Act went on to state, as a caveat:

> "...taking into account, nevertheless of material difference, if any, which may exist between interstate and overseas air transportation, on the one hand, and foreign air transportation, on the other."[125]

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Congressional and Administrative News at 356 (1980).

124. Congress had long been concerned about unfair and discriminatory fees and practices of foreign governments. For such practices and the Fair Competitive Practices Act of 1974, see infra Chapter VI, Section II (Fair Competition in International Civil Aviation).

125. The 1979 Act, Section 2(3) (amending Section 102(a) of the Federal Aviation Act of 1958).

And the following was added to the domestic policy factors that the CAB was now to consider for international as well as domestic:

> "The strengthening of the competitive position of United States air carriers to at least assure equality with foreign air carriers, including the attainment of opportunities for United States air carriers to maintain and increase their profitability, in foreign air transportation."[126]

The 1979 Act also enumerated, for the first time, "Goals for International Aviation Policy". While these goals supported increased service and competition, Congress also directed that the Executive Departments (and the CAB), in granting foreign carriers increased access to United States markets, require that such rights be "exchanged for benefits of similar magnitude for United States carriers or the travelling public with permanent linkage between rights granted and rights given away."[127]

Again recognizing reality, Congress identified as a negotiating goal "the elimination of discrimination and unfair competitive practices faced by United States airlines" in foreign air transportation. In addition, the 1979 Act contained other sections giving American aeronautical

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126. Id. Section 17(1) (amending Section 1102 of the 1958 Act.

127. Id. Section 17(8).

authorities, subject to Presidential approval, strong power to retaliate against all these practices. In this regard, it should be noted that such retaliatory action might, for instance, lead to the suspension of a foreign carrier's permit or to a limitation on its operations.[128]

As to ratemaking, the 1979 Act strengthened American power to suspend and reject international air tariffs (fares, rates and conditions pertaining thereto).[129] For foreign airlines, suspension and rejection of tariffs might take place upon a simple "public interest" test. It is significant, however, to note that the Act also established a suspension-free "zone of reasonableness" for international passenger fares within which there might normally be no suspension of fare increases or decreases. The zone has been determined by reference to a semi-annually adjusted Standard Foreign Fare Level (SFFL) and extending from 5% above the SFFL to 50% under the SFFL.[130]

Finally, the 1979 Act tightened the procedures and

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128. This issue is discussed in further detail in Chapter VI, Section II, under the subtitle "Fair Competition in International Civil Aviation".

129. See the 1979 Act, Sections 14, 15, 16 and 24.

130. For more information, see Schaffer & Lachter, "Developments in U.S. International Air Transportation Policy", 12 Lawyer of the Americas at 595 et seq. (Fall 1980).

conditions under which inter-carrier agreements for international air transportation might be approved and relieved from the operation of the antitrust laws. The same had already been done, as discussed earlier, for domestic aviation in the Airline Deregulation Act. However, price-fixing agreements in international service implicitly remained allowed, if, of course, approved. Also, "international comity" and "foreign policy considerations" were taken into account when it came to inter-carrier agreements for international air transportation.

With the above brief review in mind, it is clearly evident that the International Air Transportation Competition Act was less significant in extending competition and creating pressures for low fares in international arena than were the policies and efforts of the Carter Administration. However, in view of the stated aims of United States international aviation policy and the practical implementation of the CAB's retaliatory powers, it is difficult to avoid the conclusion that American attempts to institute "free trade" policies, in international aviation were, at least tempered by, the strong pursuit of national self-interest.

Feasibility of Transferring Domestic Policy - Analysis and Evaluation

In practice, the United States was widely perceived as having selectively applied deregulation policies in its international markets. The American Administration's emphasis on "liberal" bilateral air service agreements and the exercise of the CAB's retaliatory powers in international markets were seen as the means of furthering the interests of American carriers. It was felt, however, that the United States has been preaching "the gospel of deregulation with evangelical zeal".[131] The reason for that, according to one commentator, is simple:

> "...deregulation U.S.-style will rewrite the rules of the game to favor the U.S. With the vast fleet at their command, its carriers can quickly redeploy their aircraft to seek out the most profitable routes and, mercifully, leave some crumbs of market shares to the smaller, less formidable airlines."[132]

(1) At the international level, airlines are operating with a government framework - the Chicago Convention,[133] and about 2000 bilateral air treaties which

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131. Cruz, Philippine Airlines Chairman and President, Speech to the International Aviation Club (June 19, 1979).

132. Id.

133. See supra, Chapter I, Section III.

establish the terms of trade in international aviation markets. These arrangements which are linked to the sovereign control of airspace govern conditions of entry, supply and price in aviation trade. In this unique climate, there are "so many nationalistic factors at work that it is entirely unrealistic to believe that unregulated competition would be an acceptable framework for the airlines industry."[134]

(2) At the global level, United States aviation policy has apparently flung the international airline industry into turmoil. Free-for-all competition does have a certain theoretical appeal, establishing an environment that could lead to innovation and low fares. Air transportation services, however, has many of the characteristics associated with public utility, and in many nations it is both an integral part of the economy and an instrument of foreign policy. As a consequence, the national airline, the national traffic and the coveted routes need to be protected. Each nation sets different national objectives and creates appropriate policies and plans to achieve these objectives. In the case of international airline operations, not only are national policies and plans coordinated to meet the

134. Wheatcroft, Presentation to Air Transport Association's Economic and Finance Council (Nov. 5, 1981).

requirements of other infrastructure elements (e.g., aircraft, airports, air traffic control systems, etc...), but they also attempt to balance competition, consumer benefit and the economics of the airline industry.

(3) To better understand the unique aspects of international aviation, consider a developing region versus a developed region. In a developing country, the national-flag carrier often provides a vital and viable mode of communication, earns the critically needed foreign exchange, provides employment and serves the (extremely limited) originating passenger traffic. In such a case, competition will undoubtedly be harmful.[135] If a United States carrier is forced into bankruptcy or a merger, the results are not, of course, the same as if the flag carrier of a developing nation were to go out of business or be forced to join the flag carrier of a neighbouring State. Now consider the case of a developed region, e.g. Europe. An international airline faces a dilemma in such a market. No one can deny the attractiveness of low fares and high frequencies, but a given airline serving both intra-European markets as well as providing service to, from and via Europe, would need to maintain strong and stable feeder traffic through

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135. See, e.g., Giraudet, Air France Chairman, Lloyd's of London Conference (Jun. 4, 1981).

its network and gateway (usually the capital). Thus, this airline will need protection from competition its feeder services to channel transit passengers to and from European points.

(4) The international aviation community does not accept total deregulation in international operations mainly because of the fear of possible economic domination by some carriers. All nations, as shown above, have a direct interest in aviation services as "importers" or "exporters" (through national airlines);[136] they are concerned to one degree or another with such factors as trade balance, safety, public service, foreign policy and defense. For these reasons, it is hardly likely that these nations, particularly the smaller ones, will risk the livelihood of their carriers for the sake of "open skies", a policy once described by Sir Lenox Hewitt (Chairman of Qantas) as "...descended from economic thuggery on its father's side and from old-fashioned anti-trust idealism on its mother's and...conceived on the wrong side of the market."[137]

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136. "Importers" means "when the nation's own citizens travel on foreign carriers", while "exporters" is the opposite "when foreign citizens travel on national carriers or through tourism receipts and expenditures". See IATA Synopsis on Aviation Deregulation, Geneva at 22 (May 1984).

137. Sir Lenox Hewitt, "A World Airline Perspective and

(5) In short, the whole system and philosophy of the American policy is centred on the forces of the marketplace, carriers having the capability and flexibility to adjust readily to the demands of the market will be the winners. But there is a big "IF" - if there are equal opportunities for the contestants. Even in free and fair competition the "fittest" who survives gets bigger and bigger and ultimately is likely to overshadow the less efficient and smaller ones. A continuous effort is, therefore, required to keep pace with the marketplace and competitors, since inability to do so can be "suicidal" in the kind of business like aviation.

(6) Since improvement of the system is the principal objective of change, the application of United States deregulation concepts to international aviation must seek to achieve the positive features of American deregulation, primarily route rationalization and some low fares, while avoiding effects detrimental to the overall system, such as overcapacity, tariff wars/irrationalities and financial difficulties. In contemplating such deregulatory change, the supportive nature of the unique features in United States aviation -private, multi-carrier system, huge finan-

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Deregulation - Quo Vadis?", Address to an International Aviation Conference organized by Lloyd's of London Press at 2 (May 25, 1979).

cial/market resources, a single sovereign State political commitment to free market principles - must be taken into account. Thus, as shown earlier, the extent to which reliable lessons can be drawn from the controversial effects of deregulation in American domestic and North Atlantic markets, (where many American carriers compete), may be limited. As observed by Boullioun, Vice President of the Boeing Corporation:

> "As long as the U.S. domestic system remains in its chaotic state, other nations are unlikely to follow our lead or trust additional changes in our bilateral negotiating positions. So, it seems to me that the U.S. international aviation policy of open skies is at best premature."[138]

(7) The acceptance of deregulation principles by most nations would mean the replacement of a regulatory system emphasizing the preeminence of national interests with one specifying competition as the major objective of the system. In this sense, the adoption of the joint principles of free competition and strong antitrust enforcement (fundamental to deregulation) would necessitate the agreement of new codes of international conduct and novel institutions to oversee the operation of these principles, particularly in respect to competitive malpractice, subsidy allo-

138. Cited in OTT, "Boeing Official Decries Industry's Condition", in Aviation Week & Space Tech. at 29 (Oct. 31, 1983).

cations, carrier bankruptcies, etc. In addition, if the free entry regime were to be introduced, States would need to establish international agreements to ensure that non-tariff barriers to international trade were minimized. It is, however, apparent that making any substantial changes to the system through the attainment of an international accord on these controversial matters would be extremely difficult. As a result, increased protectionism is the most significant trend likely to occur, especially if each State's carrier(s) is unable to obtain a fair share of its national market. It was once stated by one commentator:

> "Protracted attacks on the market share of a national airline will in the long run generate a revival of protectionism. We all publicly agree that protectionism is a bad thing; we all deep down know that it is a bad thing. But all of us will yield to protectionism when it appears to be the only practical alternative to fend off unbearable competitive pressure."[139]

Given some of these problems, one must seriously question the wisdom of simply transferring the domestic procompetitive policy wholesale to international air services. From a theoretical point of view, total deregulation may be ideal; from a practical point of view, less regulation is better than more regulation. The question, then, is one of degree. Given the multiple and divergent objectives

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139. Alitalia Chairman Nordio's Speech to Ninth Annual Air Transport World Awards (Jan. 20, 1983).

of various air carriers, the aim should be to create and maintain a workable competitive environment (i.e. regulated competition), one in which government-owned or-controlled carriers and private carriers can coexist.[140]

Recent Shifts in United States International Aviation Policy

Since the designation of an airline on an international route with "low fares" forced other airlines into an uneconomic competition, carriers of many nations incurred losses and since other nations were not ready to see this situation persisting continually, many airline experts in the United States, and abroad, began to highlight the unworkability of the policy.[141] States, like Brazil, were not reluctant to denounce the Agreement with the Americans, if the United States carriers were insistent on introducing unrealistically low fares, rather than surrendering to the American policy.[142] To save the United

140. See infra, "Preliminary Conclusion" (footnote 197).

141. See OTT, "New International Policy Urged", Aviation Week & Space Tech. at 30-32 (May 11, 1981).

142. OTT, "Aviation Shift Emerges", Aviation Week & Space Tech. at 21 (Dec. 21, 1981).

States-Brazil relations from further deterioration, President Reagan directly intervened and wrote a letter to the CAB Chairman asking him not to insist on the policy of low fares; a first sign of change from the system initiated by the Carter Administration.[143]

It is in this light that one ought to see the shift in negotiating strategy, announced by the Reagan Administration in May 1982.[144] Instead of aiming at full-scale "liberal" bilterals, the emphasis would be on partial deals (limited agreements) taking care of immediate problems. Also, granting additional American gateways to foreign airlines would no longer be quasi-automatically exchanged for the acceptance by foreign countries of a liberal pricing and charter regimes. This led Connor, a top policy official in the Reagan Administration, to think that "now is the time to take stock, to review the so-called liberal bilateral agreements and to try to determine what the values are. We are developing data to better understand what the different

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143. Id.; see also supra note 121.

144. See "International Aviation Negotiations - Reagan Administration Pursues New Strategy of Negotiations", Aviation Daily (May 28, 1982); "U.S. Changes Emphasis in Bilateral Negotiations", id. at 278 (Oct. 21, 1982).

types of agreements really mean."[145] Another "official" in the same Department even publicly disapproved the aviation policies of Ford and Carter Administrations by proclaiming that "both policies attempted to convert other governments from a higher regulated approach in international aviation to a free enterprise system, allowing carriers largely to ship for themselves."[146]

It should, however, be remembered that the general trend of "liberalism" remained intact in the "modified policy" of the Reagan Administration, at least officially. The United States "commitment to open competition and the free market remains constant. It is, in fact, ...(that) U.S. international policies are changing; the philosophy and objectives are not."[147] Indeed, save for legislative intervention it must remain intact, since "liberalism" or international deregultion has now, as stated earlier, been embodied in United States legislation: the International Air Transportation Competition Act of 1979.

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145. Cited in Nammack, "U.S. International Aviation Policy: Same Goal, New Attitudes", Air Transport World at 24 (May 1982).

146. Cited in Kozicharow, "U.S. Alters International Aviation Policy", Aviation Week & Space Tech. at 28 (Nov. 8, 1982).

147. Supra note 145, at 23.

It is often stated in the United States that the policy of deregulating international air transport is sound, but that the implementation of the policy has been wrong. An influential Congressional Subcomittee held extensive hearings in 1981 and 1982, when the picture was dark for major American international carriers, to explore the consistency of this implementation with the goals established by the policy.[148] The August 1983 Congressional Report provides, as shown below, a useful statement of Congressional concerns at that time.[149]

Following a brief background statement, summarizing the Carter Administration's efforts to establish more service and fare competition, the Report examined whether the economic position of the United States-flag carriers had been weakened, and what difficulties had been experienced in carrying out the policies of the 1979 Act.

The Report first approached the "Weakness in the Bilateral Negotiation Process", noting that foreign nations include representatives of their national carriers as parti-

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148. Report of the Subcommittee on Investigations and Oversight of the Committee on Public Works and Transportation, U.S. House of Representatives (commonly known as Levitas Subcommittee) (August 1983).

149. To better understand the reasons for recent shifts, an emphasis is given here on some findings of the Report.

cipants in intergovernmental negotiations, whereas American carriers are represented only by trade associations, which in turn are limited to observer status. It then reviewed "Unequal Trading of Rights in Negotiations" and concentrated, as an example, on the United States-Netherlands Agreement, in which KLM has a seemingly incontestable dominance in the market between the two countries.[150] It concluded this discussion by stating:

> "The Subcommittee is pleased to have noted that the attitude of U.S. negotiators at bilateral conferences seemed to have hardened since the beginning of our hearings in July 1981 in that they don't seem to give away rights for the sake of having a treaty."[151]

Under the subsection headed "Cost of Adding New U.S. Entrants", the 1983 Report points out that there might be both negative and positive features to the mushrooming of American carrier competitors in any given market. This was followed by an examination of "U.S. Policies Weakening the International Fare Structure", where the Report discussed efforts to destroy IATA ratemaking under the so-called "Show Cause Order".[152] Next the Report considered "U.S.

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150. In 1983, U.S. airlines carried only 2.8% of the 925,000 passengers reported as travelling between the U.S. and The Netherlands.

151. Levitas Subcommittee, op. cit., note 148, at 7.

152. The Report's finding on this issue is discussed in

Unsupported Carriers vs. Government-Supported Foreign Carriers". Perhaps the most balanced statement in this subsection was made by Ambassador Brock, United States Trade Representative, who stated: "Foreign governments pour hundreds of millions of dollars into their civil aviation industry. Our government provides U.S. carriers with no financial support." He then referred to practices, such as pooling, illegal for United States carriers, yet permitted for foreign airlines.[153]

In the "Prevalence of Unfair/Discriminatory Practices" subsection, the 1983 Report expresses great concern about discriminatory practices against American carriers abroad, particularly in respect of ground handling facilities at foreign airports and access for American carriers to computer reservation and agency system abroad.[154] In this sense, the Report found that the United States has historically negotiated "hard rights for soft rights" - giving up routes and schedules of greater economic value than those received, in the interest of lower

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further detail in Chapter VII, Section I (footnotes 39, 44 and 45).

153. Levitas Subcommittee, op. cit., note 148, at 9.

154. For the various types of such practices, see infra Chapter VI, Section II.

fares and new airline entrants. And as a result, "there is not a fair and equitable market for our carriers in international transport". The Report further states that United States carriers are competitive and efficient, but commonly they are competing against the authority and financial strength of foreign governments that desire their own carriers to succeed for a variety of nationalistic reasons in addition to transportation.[155]

Finally, the 1983 Report urged the Administration to make clear "to other countries, our flag carriers and even to our citizens exactly what they would expect from U.S. International Policy". After listing numerous specifics, the Report concluded:

> "In short, we want to insure that there is a fair and equitable market environment for international air travel that provides for profitability for our flag carriers, reasonable rates and quality service for our consumers, and a consistent and firm position to present to foreign governments and their carriers."[156]

It is still too early, however, to tell whether these "Congressional policy objectives" will, in fact, be attained on a long-term, consistent basis. But the hearings

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155. It was also noted that even the U.S. helps foreign carriers indirectly through its support to the "Export-Import Bank" that provides low interest rate loans to them to enable foreign carriers to purchase new equipment.

156. Levitas Subcommittee, op. cit., note 148, at 18.

and Report may well have had at least one consequence: a perceptible slowdown in the promotion of "open skies" policy.

Following the Congressional Report, the American Administration put more effort into enforcing compliance with bilateral air transport agreements than into expanding them. In other words, the trend in negotiating strategy has apparently been to seek more balanced exchanges of economic opportunities for the airlines. The importance given by American aeronautical authorities to the United States-ECAC Memoranda of Understanding, as discussed later in this study, is one example.[157]

In January 1984, Scocozza, a top policy official in the DOT, was interviewed about current United States policy. As reported: "Scocozza said the U.S. has gotten much tougher in responding to U.S. carrier problems in international markets." "In 1983, I think we did get tough with a few countries....'the tougher stance is a refreshing one'." He then continued:

> "Under current international policy, 'no one gets anything they do not deserve'.... Balance of benefits is not a bad phrase anymore. I know it was taboo for a couple of years, but people now have to show on the record that what we are getting is equivalent to what we are giving

157. For the U.S.-ECAC pricing agreement, see infra Chapter VII, Section IV.

them."[158]

Later in the same year, Scocozza threatened that the United States "won't give an inch when we don't see our negotiating partners being forthcoming." The United States, however, can scarcely be called "protectionist". But "the U.S. (for example) will not trade New York City for a point in Ruratania, a fictional country with a population of 10,000, and that country wants to fly through London to pick up London-New York traffic. It's not in the U.S. interest and takes away from our low-cost carriers."[159] Seemingly, the current American posture is to treat each negotiating partner as an "individual case". It is at the same time pushing to expand rights and losen fare-setting with some countries, while trying to retract rights handed out during the Carter Administration in others.[160]

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158. Aviation Daily at 74 (Jan. 16, 1984). CAB board members, at that time, expressed similar positions. Chairman McKinnon was quoted: "...we have to make sure that the U.S. is getting a fair deal, because bilateral relations are not a one way street". Id. at 57 (Jan. 12, 1984).

159. Quoted in OTT, "U.S. Stiffens Negotiating Stance", Aviation Week & Space Tech. at 28 (April 9, 1984).

160. See, e.g., Feldman, "U.S. International Aviation Policymakers Adopt More Pragmatic Approach", Air Transport World at 29-32 (Oct. 1984); Thoms, "The Deregulation Skies - U.S. 'Sunset' Legislation and International Air Travel", Netherlands International Law Review at 413 et seq., Vol. XXXI (1984).

Ultimately, the basic policy issue in international air transportation is how to balance the different, and sometimes conflicting, objectives. The American government has traditionally put high value on what it perceived to be "consumer" benefits. Against worldwide opposition, it sponsored low-priced charter flights. It was virtually alone in establishing direct competition between its carriers.

But even so, the "open competition" policy was an extreme exaggeration of this pro-consumer bias, in its complete disregard of the many broader interests uniformly valued by other governments, and by Congress: a strong, well-equipped air transport system; efficiency and profitability of its airlines; market share and trade considerations; etc. While it was a deviation not likely to be repeated soon, its effects are not likely to be quickly erased. Therefore, in the interest of assuring a strong national-flag industry, the United States policy toward international air transport may find it necessary to back away even further from the initial extremes of "open skies" objectives.

SECTION IV - INFERENCES FOR A MORE LIBERAL AIR TRANSPORT POLICY IN EUROPE

The Winds of Regulatory Reform

Over recent years, increasing attention has been paid to the question of competition in international air services in Europe. Ironically, it is the United Kingdom, the principal opponent of United States free market proposals at Chicago, which is leading this drive towards American-style deregulation. No doubt encouraged by Prime Minister Margaret Thatcher's commitment to returning State-owned British Airways to private ownership and thus reducing her government's direct involvement in the British air transport industry,[161] some privately-owned British airlines have been actively campaigning for a more competitive European fare structure. In late 1979, for instance, Laker Airways asked British aviation authorities for permis-

161. In November 1980, Parliament passed the British Civil Aviation Act, which enables the U.K. government to sell all or part of British Airways to private investors. See Aviation Week & Space Tech. at 33 (Nov. 24, 1980). The sale reportedly will not take place, however, until the economic climate for air transport improves. See "U.K. Airline Review Backs BA", Flight International at 909 (Oct. 13, 1984); "Radical Change for U.K. Aviation Policy", id. at 1028 (Oct. 20, 1984).

sion to fly to thirty-four Continental cities, with fares up to 80% lower than current fares, while British Caledonian requested operating rights for cheap, "no-frills" service to twenty-one European cities.[162] Possibly as a result of this pressure, the House of Lords Select Committee on the European Communities issued a report in early 1980 calling for greater competition in intra-European air travel.[163]

Within the United Kingdom, deregulation has now gone a long way both on fares and on capacity, and further steps are being taken in that direction. Competition has also been established on the cabotage route[164] between the United Kingdom and Hong Kong. So far as international services are concerned, progress towards liberalization depends heavily on the attitude of other governments. While United States policy favours a minimum of regulation, most member States of the European Community (EC) have been reluctant to throw off the chains of the system they

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162. Britannia Airways, British Island and Air U.K. also have sought authority to operate more and cheaper air services.

163. See "British Prompt Common Market Fares Study", Aviation Week & Space Tech. at 29 (June 20, 1980).

164. That is to say, a route within the sole jurisdiction of the U.K. government and restricted to British airlines.

know.[165]

The British government, however, was able in June 1984 to reach an agreement with The Netherlands government which provides that any British or Dutch airline supported by its government may mount new services between the two countries at whatever capacity it thinks appropriate and may charge any fares approved by the country in which the traffic originates.[166] Since then, in December 1984, a two-year, limited experiment in liberalization has been negotiated with the German government.[167] In this regard, the "White Paper on Airline Competition Policy" published in October 1984 makes clear that the British government intends to continue in their efforts to persuade other European nations of the need for liberaliza-

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165. CAA Paper 84009, "Deregulation of Air Transport - A Perspective on the Experience in the United States", London at 38 (May 1984) (hereinafter cited as CAA Paper 84009).

166. For more details, see Feazel, "British, Dutch Aim at Deregulation", Aviation Week & Space Tech. at 29-30 (June 25, 1984); "U.K. Seeks to Liberalise Fares in Europe", in IATA Regulatory Affairs Review, Vol. 13 at 141, 259 (June-Sept. 1984).

167. The pact with West Germany is not as comprehensive as that signed with The Netherlands, but it does embody the same principles. See "Britain, Germany Lift Restrictions on Air Transport Operations", Aviation Week & Space Tech. at 25 (Dec. 17, 1984); id.

tion.[168]

The United Kingdom government has tended to welcome competition which could enable the industry to prosper, and indeed to grow, in European and other markets, while discouraging attempts by the United States to obtain a disproportionate share of the British market. The United Kingdom's position was summed up by its Civil Aviation Authority (CAA) in the following words: "We are regarded as dangerously revolutionary by some on the Continent. The Americans tend to regard us as dangerous reactionaries."[169]

The United Kingdom policies have at least initiated a trend towards a moderate form of deregulation which has been taken up by ECAC and the Council of Europe, while the institutions of the European Economic Community (EEC) have primarily supported a more comprehensive liberalization of European air transport, subject only to the application of

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168. On 5 October the U.K. Department of Transport tabled a White Paper on "Airline Competition Policy" which sets out the decisions on the CAA's review of "Airline Competition Policy".

169. Cited in European Air Transport Policy, House of Lords' Select Committee on the European Communities, 7th Report, Session 1984-85 at X (Mar. 26, 1985).

the EEC competition rules.[170]

In June 1980, ECAC set up a task force to study competition in intra-European air services and to suggest appropriate solutions to various problems, including routes, capacity and tariffs. The outcome was a report published under the title of "Competition on Intra-European Air Services" (COMPAS) in 1982.[171] It noted that approximately 90% of European bilateral air transport agreements contained some form or another of capacity restriction and that the 22 ECAC member States, of which 19 provided data, had pooling agreements accounting for about 75-85% of intra-European air transport.

The COMPAS study suggested some possible changes of the regulatory framework. There must be more flexibility in tariff and capacity regulation and in route entrance, in order to raise the level of competition on intra-European services. "Safety nets" must be provided for since there are differences in the competitive capacity of the European airlines, and that the degree of liberalization that would

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170. Since it would be beyond the scope of this thesis, a brief discussion is only given to intra-European international air transport in the framework of the ECAC and EEC.

171. Report on Competition in Intra-European Air Services, ECAC Doc. No. 25 (1982).

be acceptable to governments is not the same on all routes. It should also be noted that the "zones of freedom" that would be created for tariffs would look very much like the zones established (as discussed in Chapter VII, Section IV) in the United States-ECAC Memoranda of Understanding. The system provides for the establishment of flexible pricing zones open to airline initiative and not subject to government oversight, provided however that zone widths, reference fare levels and all rates falling outside the zones are to be agreed between governments. Finally, the COMPAS Report was used as a basis for recommendation at the 11th Triennial Session of ECAC, held in June 1982, which requested that member States consider "the possibilities for progressively introducing some additional degree of flexibility and competition" and to examine "the more flexible concepts described in the Report."[172]

During its 12th Triennial Session held in June 1985, ECAC member States have unanimously adopted a "Policy Statement" committing their governments to increasingly liberal regulatory regimes throughout the continent.[173]

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172. See Recommendation No. 6 of the 11 Triennial Session of ECAC (June 1982); "Europeans see Impetus for Easing Regulations", in Aviation Week & Space Tech. at 53 (Nov. 8, 1982).

173. See Feazel, "European Civil Aviation Leaders Commit to

The new policy would allow European airlines more flexibility in setting fares and increased opportunity to enter new markets. It also would reduce the emphasis on pooling arrangements that require them to share revenues with the airlines of other nations. In fact, the "Policy Statement" itself will have no immediate effect on the regulatory regime. But it does open the door to a series of ECAC agreements that embody the new policies. To this end, the outgoing President of ECAC, Noel McMahon, stated that:

> "Steps are already in hand for a review of the 1967 International Agreement on the procedures for the establishment of tariffs for scheduled air services, side by side with an examination of the possibilities for new pricing systems for Europe. The regulation of access and capacity will also be looked at, with particular attention being given to the promotion of viable inter-regional services."[174]

During the last fifteen years, the EEC has also become increasingly active in the field of air transport. The legal basis for this involvement is found in the Treaty Establishing the European Economic Community (Treaty of Rome).[175] All doubts about the applicability of this

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Increased Liberalization", Aviation Week & Space Tech. at 36 (June 24, 1985).

174. Quoted in IATA Regulatory Affairs Review, Vol. 14, No. 4 at 429 (May-Jun. 1985).

175. Treaty Establishing the European Economic Community, signed at Rome on March 25, 1957. See also Sweetman, "The European Commission Looks at Civil Aviation", 34

Treaty to air transport were removed in 1974 by the Court of Justice of the European Communities (ECJ) in the case of The Commission of the European Communities v. The French Republic (the so-called French Seamen case).[176] The ruling gave the Commission new resolve to promote its procompetitive views. In 1978, it succeeded in convincing the Council of Ministers to let it investigate civil aviation.[177] In June 1979, it cautiously recommended to the Council deregulation for the European air transportation system.[178] In its Memorandum No. 1, the Commission not

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Interavia at 1143 (1979); Kozicharow, "Common Market Faces Airline Decisions", Aviation Week & Space Tech. at 36 (Feb. 25, 1980); Toepke, "EEC Law of Competition: Distribution Agreements and their Notification", The International Lawyer, Vol. 19, No. 1 at 117 (Winter 1985).

176. See Case No. 167/73, Recueil, 1974, at 359. In this case, the Commission asked the ECJ to rule on whether a French law limiting general employment on a naval vessel to the ration of three Frenchmen to one non-French national contravened the Treaty of Rome's provisions on transportation. The Court struck down the law and, in dicta, stated that the general rules of the Treaty were applicable to air transport as well as to sea transport. See generally Weber, "The Application of European Community Law to Air Transport", 2 Annals of Air and Space Law at 233 (1977).

177. See Sweetman, op. cit., note 175, at 1143.

178. Commission of the European Communities, Air Transport: A Community Approach, in Bulletin of EC (Supp. May, 1979) (hereinafter cited as Memorandum No. 1).

only proposed fare reductions and more flexible services; it also questioned the current principle and practice of bilateralism, suggesting that any European airlines should be allowed to compete on any intra-Community route if it can offer cheap service for a fixed period.[179] A year later, recognizing that the subject of scheduled passenger air fares in the Community was "worthy of comprehensive study", the Council invited the Commission to examine in detail intra-Community fares. The Commission's Report appeared in July 1981, concluding that "one of the fields for future action for the European Community should be to achieve a less rigid tariff setting procedure for intra-Community air travel".[180] Almost simultaneously, the Commission proposed a regulation that would give it the necessary powers to investigate and punish infringements of the Community's antitrust laws by airlines.

Another significant move towards liberalization was the passing by the Council in 1983 of a Directive on scheduled inter-regional air services, which is designed to give opportunities to more airlines to operate routes outside the trunk routes between the main European airports. The

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179. Id. at 17-19.

180. Commission of the European Communities, Report: Scheduled Passenger Air Fares in the EEC at 50 (July 23, 1981).

Commission itself recognizes in its Memorandum No. 2 of February 1984,[181] however, that its "original proposal has been considerably watered down" and that "it is questionable how much effect (the Directive) will have in its modified version." Although Memorandum No. 2 contains certain features of earlier Commission proposals, it purports to favour an evolutionary approach towards increased flexibility within Europe. Therefore, deregulation on United States lines is especially ruled out as unlikely to work in the present European context.[182]

Within the context of the new Memorandum, the scope of the proposed procedural regulations has been modified so as to cover only international air transport between Community airports, and not all international transport to and from such airports. In addition, a proposed Council regulation has been included in the package of measures which would enable the Commission to grant block exemption to agreements in this sector relating to capacity sharing, revenue pooling and consultation on tariffs.[183] In the

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181. Commission of the European Communities, "Progress Towards the Development of a Community Air Transport Policy", COM. (84) 72 Final, Brussels (15 Mar. 1984) (hereinafter cited as Memorandum No. 2).

182. Id. Paragraph 43.

183. The Commission also includes in the Memorandum (Annex

Commission's view, such block exemptions should be subject to conditions and limited to a transitional period and subject to review. Also, they should be linked to the changes in governmental procedures proposed in the Memorandum and could only apply in conjunction with the procedural regulation referred to above.[184]

The main theme of Memorandum No. 2 is to suggest that Europe is ready now for a more open regime favouring more competition between airlines and wider choice for users. The proposed "common air transport policy" has to be approved by the Transport Ministers of the member States. The reason for this proposal was that the European Parliament filed charges with the ECJ alleging that EEC violated the Treaty of Rome by not deregulating air transport, since the Treaty requires free competition also in air transportation as well as in other commercial activities.[185] In

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III-C) the essentials of a Commission Regulation granting such block exemptions which it would intend to issue if the Council approves the above enabling Regulation.

184. For further detail, see, e.g., Thaine, "The Way Ahead from Memo 2: The Need for More Competition a Better Deal for Europe", in Air Law, Vol. X, No. 2 at 90 (1985); "European Commission Civil Aviation Memorandum No. 2", id. at 99 et seq.

185. See Aviation Week & Space Tech. at 30 (Jan. 31, 1983).

this respect, it is significant to note that on May 22, 1985, the Court delivered its judgment by ruling that the member States of the EC have failed to establish a framework for a common air transport policy within which the objectives of the Treaty could be pursued.[186]

Finally, in a most recent action, however, the European Parliament has approved in September 1985 a "go slow" approach to liberalization of airline regulation in Europe.[187] The approach, if approved by the full EEC, would allow nations to delay liberalization for up to 14 years.[188] On the other hand, the decision prompted the EEC bureaucracy to threaten to use existing rules to force increased competition among airlines if regulation is not eased. This would embroil the EEC and individual air

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186. In the judgment, the Court said that the Council of Ministers had violated the EC Treaty by failing to take steps towards a common transport policy and that this Council had not sufficiently liberalized rules on operating transport companies or laid down conditions under which operators could work in countries where they were not residents. See IATA Regulatory Affairs Review, Vol. 14, No. 4 at 430 (May-June 1985).

187. See "Europeans Advise Slow Deregulation Approach", Aviation Week & Space Tech. at 39 (Sept. 23, 1985). It should, however, be noted that the Parliament's decision is only advisory. The EEC's Council of Ministers has final responsibility for liberalization and is to consider proposals at a meeting in December of the same year.

188. Id.

carriers in long and costly court fights.

Evaluation and Analysis

The dissimilarities between the civil aviation industry in the United States and in Europe are well known. Often cited are the higher costs in Europe of fuel, labour, airport and air navigation charges; it can also be mentioned the undeniable fact that in Europe scheduled (international) airlines are commonly State - or partially State-owned, whereas in the United States all carriers are privately-owned. There are, of course, also geographical and infrastructural differences between Europe and the United States, which have an impact on such issues as the average stage length and layout of air routes, and on competition by other modes of transportation. In other words, the European traveller is faced with shorter distances and usually has a reasonably good national rail system as an alternative to flying. Pressures from the European air passenger, more likely to be travelling on business, are not as strong as in the United States. European airlines are horrified for the most part by the prospect of deregulation, and the multiple boundaries and small sizes of European countries and the resulting diplomatic and legal complexities support their skepticism of

completely "open skies" system.

With respect to regulatory regimes, however, two variations between the United States and (Western) Europe seem essential. First, the United States is one (federal) sovereign nation, whereas Europe is composed of a multitude of sovereign countries, cooperating in various multilateral fora of which for civil aviation ECAC (22 member States) and the EEC (12 member States) are the most important ones. Second, the United States domestic aviation market is served almost exclusively by scheduled services, whereas in intra-European international air transport the market is approximately evenly split between scheduled and non-scheduled (charter) services. Scheduled international flights in Europe are mostly conducted on the basis of bilateral agreements, supplemented by the 1967 ECAC "Agreement on the Procedure for the Establishment of Tariffs for Scheduled Air Services",[189] which is based upon Bermuda I type tariff clauses. Non-scheduled international services in Europe are governed by national laws and regulations, and by the multi-

189. It should be noted that ECAC has recently been studying the possibility of a new modified agreement to replace the 1967 Agreement. See Feazel, "ECAC Leaders Expected to Approve Liberalized Regulatory Proposals", Aviation Week & Space Tech. at 28 (June 17, 1985); supra (footnotes 173 and 174). For further detail on the 1967 Agreement, see infra Chapter VII, Section I (footnote 34).

lateral 1956 ECAC Agreement.[190]

Unlike the United States, where it is generally accepted that commercial airlines "exist for the purpose of transporting people and goods according to conventional supply and demand or market condition",[191] many European countries still view their air carriers not only as instruments of transportation, "but also as instruments of economic policy, domestic and foreign political policy, (and) national defense...."[192] Indeed, the Chairman of British Caledonian Airways has recently remarked that "the current European structure and ownership of the airlines is just not built for competition, and evolution, not revolution, is required if progress is to be made."[193] Most European airlines are therefore accustomed to monopolies or near-monopolies on many routes. As a result, although they have achieved the size and operating efficiency necessary for

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190. For the Agreement, see infra Chapter V, Section II (footnote 27).

191. See Gidwitz, op. cit., note 4, at 18.

192. Id.; Doty, "Europeans Still Resist U.S. Air Policy", Aviation Week & Space Tech. at 32 (Oct. 30, 1978).

193. Stated by Sir Adam Thomson. Quoted in Reed, "European Deregulation Unlikely, According to BCAL's Thomson", Air Transport World at 72 (July 1984).

effective competition with American carriers, corresponding reductions in the overall cost of air transportation have not yet been realized and, in the view of Chairman of the Executive Board of Lufthansa:

> "Several (European) airlines will have to live with growing uncertainty about their futures, especially because of their inability to finance their investments. The managers of these airlines will be forced to operate in the face of imminent bankruptcy, permanently dependent on external financing."[194]

Initiatives to "liberalize" or "deregulate" intra-European international air transport may come from the EEC (through the Commission, Council and Parliament, according to their respective jurisdiction). An immediate question arises as to whether a body such as the EEC is indeed suited to regulate European air transport, bearing in mind the concept of national sovereignty of member States and their common interest in a well functioning air transport system. The structure of the EEC, though ideologically consisting of a group of countries with a Parliament, does not make it a federal entity like America. Its member nations have never felt more separate, and if there is to be a united civil aviation policy to replace the web of traditional bilateral

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194. Stated by Heinz Ruhnau. Quoted in Air Transport World at 71 (April 1983).

agreements it will be many years coming. Regardless of what final conclusion might be drawn, European air transport can not be looked at simply from a community standpoint, since intra-European air services affect and are affected by extra-European air services.[195]

The whole problem seems to lie in the fact that there are many channels and bodies in the EC which produce a variety of initiatives and proposals, which lack coordination. The intra-European air transport market is, however, one large market, which extends beyond the boundaries of the twelve EEC States. Thus, European bodies involved in transportation by air should join together and co-operate in the establishment of a coherent system for Europe. The EEC cannot, on its own, work out a series of co-operative agreements among member nations since the Community is a general concept which permeates all of its economic activities.

The writer believes in general terms that gradual evolution and a comprehensive approach to air transport regulation in Europe is essential and must be done in such a way as to ensure continued integration with the worldwide system. In this sense, the long-term objectives to be pursued by the EC with its air transport policy should take into account not only the interests of the passengers but

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195. See ITA Bull., No. 15 at 374 (1974).

also those of other users, the airlines and other parts of the air transport system as well as other aspects of the public interest. Moreover, any rules on competition should recognize that airline coordination and co-operation are in the public interest, are not incompatible with the Treaty of Rome and will help to integrate the European system. Any rules should also avoid extraterritorial applicability which can only lead to increased governments conflicts and intervention in the marketplace. This means a sound and realistic balance between competition and co-operation. Competition is not an end in itself, it is an essential means to maintain dynamism and efficiency pressures in the system. Co-operation is not an end in itself, it is a means to develop, from disparate "National Interest" operations, an integrated international system and to make efficiencies by eliminating duplicate efforts.

Finally, while it is difficult to predict what might happen within Europe, the situation is certainly critical, and as summarized by the Chairman of British Caledonian Airways, Sir Adam Thomson:

> "There is a wind of change building up to blow across the air transport industry in Europe. It remains to be seen whether the reactions of governments and airlines make this a headwind to be struggled against, or a tailwind of opportunity to ride upon."[196]

196. Quoted in Thaine, op. cit., note 184, at 98.

PRELIMINARY CONCLUSION

After seven years of United States aviation deregulation, it still not possible to render a final verdict on whether, on net balance, deregulation is producing a domestic air transport system better or worse than that which previously existed. Similarly, the consequences of increased competition in international air services are by no means completely clear. It is, however, possible to point out a series of specific favourable and unfavourable developments.

The United States domestic airline deregulation experience has shown spectacular (new) carrier performance, but also airline mergers and bankruptcies. It has shown contented passengers on high-density, competitive routes, but sometimes dissatisfied passengers on low-density, non-competitive routes. Free route entry and exit have, on the one hand, caused an over-expenditure into certain markets and, on the other, have meant decrease in service to many smaller communities. Also, airlines have been restructuring their route networks into hub-and-spoke operations. In addition, the carriers have continued to show a tendency for overcapacity. The dust, however, has not yet settled. Eventually, one will probably look more at the overall

picture than at individual airlines and users.

It seems that, at least in the United States, deregulation is here to stay, although the results of full deregulation on the market remain inconclusive. No doubt, the United States will solve any problems arising; it has vast capital resources, many carriers and the highest level of technological capability. The United States has the most sophisticated airline system and the most advanced economy. It has also established administrative mechanisms to cope with the changes. It is one land with one language, one legal system and a political consensus. These are special features which make United States domestic aviation unique.

Any attempt to apply United States deregulation concepts in international aviation markets would have far-reaching implications, because international air transport greatly differs from domestic air transport and is highly diversified; the international aviation system is based on State sovereignty with route entry, supply and fares being controlled through thousands of bilateral and multilateral agreements. For virtually all nations, international aviation is linked to national security, diplomatic relations, international trade, communications and national economic development. Additionally, many international airlines are government-owned or controlled. States will not allow foreign economic considerations and interests to control

such an industry.

If open competition is thought to be a good thing then its advocates must realize that, first of all, they have to create the proper environment within which free-for-all competition can exist. They must overturn the principle of complete and exclusive sovereignty over territorial airspace; they must persuade nations to relinquish control over routes and rights, and fares and rates; they must dismantle the system of bilateral agreements and invent a new legal regime to replace it. It should also be noted that specific features which are fundamental to the United States domestic system do not exist in the international context. The international aviation system does not have the mechanisms to deal with consumer protection, antitrust control, subsidies, mergers on transition management. New machinery and codes would be needed. A new layer of international bureaucracy would appear.

Given the above-mentioned facts, it is doubtful if the international aviation community would agree to a policy of unfettered competition or even to strict government regulation. Rather, it is most likely that this community would ultimately agree to a compromise - "regulated competition" or "enlightened regulation".[197] Within this

197. See supra note 140. For further implications of this

context, it is essential that the market opportunities traded must be equal, to the extent that equality can be ascertained. In addition, the continued coexistence of different concepts and objectives should be taken into account. And above all, the legitimate needs of consumers and carriers as well as other participants in the system should not be underestimated. Possibly in this form, government-owned or-controlled airlines and private carriers can keep pace with this world full of inequalities and diversities.

The Pentagon strategists once said that the United States has to avoid fighting the wrong war, at the wrong time against the wrong side. Perhaps one day it may be said of deregulation that at least its timing was wrong, and that it was inexpedient to use its principles and practices in response to one of the most serious economic and energy crises in modern times.

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method, see Giraudet, Speech delivered to the 1981 IATA Annual General Meeting in Cannes. Cited in ITA Bull., No. 39 at 1017 et seq. (Nov. 16, 1981); Taneja, op. cit., note 10, at 148-150.

CHAPTER IV

TOWARDS A REVIVAL OF MULTILATERALISIM ON THE ECONOMIC ISSUES OF INTERNATIONAL AIR TRANSPORT

SECTION I - TENDENCY TOWARDS MULTILATERALISM

Generalities and Historical Background

On November 1, 1944, President Roosevelt opened the Chicago International Civil Aviation Conference with a message proclaiming that the -

> "rebuilding of peace means reopening the lines of communication and peaceful relationship. Air Transport will be the first availale means by which we can start to heal the wounds of war, and put the world once more on a peacetime basis."[1]

International air transport would, in the words of one of the participants to the Conference, offer "a bright promise of more and easier inter-continental travel, better acquainted and friendlier peoples, and higher standards of

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1. Proceedings of the International Civil Aviation Conference, U.S. Dept. St., Chicago, Vol. I at 42 (1948) (hereinafter cited as Proceedings).

living...".[2] Berle, the Chairman of the Conference and head of the United States delegation, even spoke of civil aviation as a means of fulfilling the "right" of the nations to communicate,[3] implying that air transport was no less worthy of international attention than the fundamental human rights which would soon be enshrined in the Preamble of the United Nations Charter and in the Universal Declaration of Human Rights.[4]

This vision of civil aviation's "mission civilisatrice" was shared, in its broad outlines, by the majority of conferees at Chicago.[5] Indeed, the Chicago Conference of 1944 was convened in order to formulate universal technical

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2. Warner, "The Chicago Air Conference: Accomplishments and Unfinished Business", 23 Foreign Affairs at 420 (1945).

3. Proceedings, op. cit., note 1, at 55, 58.

4. Article 55 of the UN Charter; Universal Declaration of Human Rights, UN Doc. A/810 at 217 (1948).

5. See, in general, Proceedings, op. cit., note 1, at 42-88. A few years after the Conference, the Dutch Representative to ICAO remarked that "the main purpose of the initiators of the Chicago Conference was that a multilateral agreement should be drawn up based on a universal spirit which would show all nations how to foster the development of civil aviation". ICAO "Development of a Multilateral Agreement on Commercial Rights in International Civil Air Transport", ICAO Doc. No. 4510 at 18 (1947) (hereinafter cited as ICAO Doc. 4510).

standards and to establish a worldwide system for the economic regulation of a budding international air transportation network. However, due to conflicting and different philosophies amongst the participating nations, an agreement on a multilateral regime was only reached for the technical freedoms.[6] As stated earlier, the attempts at exchanging commercial air traffic rights on a comprehensive multilateral basis were almost completely abandoned after 1947.[7] In the early fifties, however, the emphasis shifted to multilateralism on a regional basis within regional civil aviation bodies which, as will be seen, involved intense efforts but limited results.[8] Thus, all rules governing the operation of commercial air services would come to be established on an ad hoc, State-to-State basis.[9] In

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6. The first and second freedoms were granted to charters in Para. 1 of Art. 5 of the Chicago Convention and to scheduled services in the Air Services Transit Agreement (Article 1, Section 1). See supra, Chapter I, Section III.

7. See supra, Chapter I, Section III (footnote 83).

8. The most successful results in this regard were achieved for non-scheduled international flights (i.e. the Paris Agreement of 1956 and the 1971 Manila Agreement). See infra Chapter V, Section II (footnotes 27 and 31).

9. As to charter international flights, it should be noted that they are still generally authorized on the basis of unilateral governmental regulations though

other words, it was the system of bilateral air transport agreements which actually became the prime source of norms for the economic regulation of international civil aviation.

Practically speaking, however, bilateralism as a system of regulation sharply contrasts with the basic peculiarities of the activity to be regulated. Scheduled international operation is anything but a typically bilateral activity. It has what may be termed significant "third country dimensions": on the one hand many international air services are performed on routes linking more than two States; on the other the traffic which on such services is carried from one State to another practically always contains traffic originating in and/or destined for third States. To try and regulate such multilateral activity on a bilateral basis among 156 States[10] is inefficient. Any bilateral exchange of rights for the conduct of international air transportation other than in third and fourth freedom

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there are some bilateral and multilateral arrangements for routes or certain types of operation. See infra Chapter V, Sections II and III.

10. At present, there are 156 Parties to the Chicago Convention and these States also form the membership of ICAO. See Milde, "The Chicago Convention - After Forty Years", Annals of Air and Space Law at 119 (1984); ICAO Bull. (June 1985).

traffic between the territories of the contracting States, is bound to be inconclusive until or unless it is certain that third countries concerned will permit such rights to be implemented.[11]

This, indeed is not conducive to a rational planning and an economic operation of international air transportation which is now viewed as "an economic activity with essentially a multilateral character".[12] For this reason, it is believed that the interests of the international aviation community would be better served if the present bilateral policies were gradually replaced by multilaterally - agreed policies, finding their expression eventually in multilateral understandings.[13]

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11. See, e.g., O'Connor, An Introduction to Airline Economics at 48 et seq. (1982); Wessbergh, "New Canada-United Kingdom Agreement", 39 ITA Bull. at 926 (Nov. 17, 1980). The Canadians consider themselves somewhat at a disadvantage since access to western Canada has been granted from the outset to their partners (i.e. the UK), while their (the Canadian) fifth freedom rights depend on approval by other (i.e. third) parties. True, but that is how the system (i.e. bilateralism) works.

12. See "A Policy for International Air Transport in the 1980's", Working Paper presented by the International Chamber of Commerce to the 24th Session of ICAO Assembly. A24-WP/59, EC/12 at 2 (Sept. 21, 1983).

13. Sion, "Multilateral Air Transport Agreements Reconsidered: The Possibility of a Regional Agreement Among North Atlantic States", Va. J. Int'l L. at 160-169

Although the Chicago Convention reinforces the bilateral legal structure,[14] there is one provision in it that is one of the most coherent statements of multilateral commercial policy ever achieved - The Preamble which stipulates, inter alia, that:

> "The undersigned governments having agreed on certain principles and arrangements in order that international civil aviation may be developed in a safe and orderly manner and that international air transport services may be established on the basis of equality of opportunity and operated soundly and economically."

Unfortunately this "equality of opportunity" principle remains a dead letter since the real opportunities for the airlines ultimately vary with the size of the air traffic market over which the governments of their respective home-countries have full control pursuant to the sovereignty principle laid down in Article 1 of the Convention. In other words, all are equal, but some happen to be more equal than others! Only a few "super powers" in aviation will have enough negotiating carte blanche in the bilateral system[15] in order to enhance their opportunities and to

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(1982); id. at 2-7.

14. See Articles 1 and 6 of the Convention; supra, Chapter I (footnotes 62 and 69).

15. Veenstra, "The Plurilateral Air Transport Agreement: A Draft for a Better Regulatory Instrument", in

evolve and sustain for themselves a relatively stable and efficient air transport industry.

It has been therefore correctly remarked that the difficulties in the industry stem (in no small degree) from the contradictions and inconsistencies of national policies, as expressed by national regulations and bilateral agreements.[16] What is urgently needed to remedy this situation is multilateral regulation.[17] Indeed, bilateral agreements, because they are flexible and easily renegotiated, promote a certain amount of instability in international air law. A multilateral approach would undoubtedly be more permanent, less susceptible to change, and therefore norm-creative rather than norm-disruptive.

It follows that States should endeavour to overcome the various obstacles required for the conduct of international air transportation on a broader scale than through bilateral process. The search for a comprehensive multi-

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Wassenbergh and Fenema Eds., International Air Transport in the Eighties at 216 (1981).

16. Guldimann, "Bilateral Agreements as Regulatory Instruments in International Commercial Aviation", in Matte Ed., International Air Transport: Law, Organization, and Policies for the Future at 123-124 (1976).

17. Id.; Sion, op. cit., note 13, at 160; Veenstra, op. cit., note 15, at 216.

lateral solution to international aviation problems would, if anything, have to "proceed progressively, step by step, (by) considering generally accepted practice" to the point where nothing would be left to bilateral negotiations and the nations of the world would be able, "with confidence, to take the final plunge".[18] This multilateral solution is in fact worthwhile as rightly observed by the Canadian representative to ICAO some 38 years ago:

> "Why multilateralism? ...The feeling that I had, speaking for Canada, was not that we wanted uniformity, although that is desirable, inasmuch as I see no end result in uniformity for its own sake. We had a much loftier purpose in mind, and that was of creating a set of conditions that all nations who wanted to fly could use so that they would know in advance what their opportunities were, what the conditions were that they would be up against, so that it would not be possible for one nation to discriminate against another, and grant to another privileges that they would not be willing to grant to others equally entitled to them, so that these things would not lead to frictions between nations and quarrels and eventually be the seed from which might spring a war. For this reason, it is said we wanted multilateralism, not merely uniform clauses (in bilateral agreements)".[19]

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18. ICAO Doc. 4510, op. cit., note 5, at 44.

19. Id. at 35.

Is the Time Ripe for a New Multilateral Approach?

Although over forty years have passed, one still remembers the remark made by the Brazilian delegate to the Chicago Conference that "perhaps the time will never be ripe for the internationalization of aviation".[20] Certainly this seemed true in a day and age when the gross imbalance in world aeronautical potential was impeding multilateral agreement on regulatory principles and when bilateral arrangements appeared to offer the only means of reconciling air transportation policies that differed considerably from country to country. Gertler is in accord with the observation that he believes such an effort for a "multilateral idea" would be no closer to reality now than it was at Chicago.[21] The present writer, however, views current developments in aviation as simultaneously posing a serious challenge to the post-Chicago regime and reopening the case for a multilateral regulatory system.[22] The fact is vast

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20. See Proceedings, op. cit., note 1, at 544.

21. Gertler, "Bilateral Air Transport Agreements: Non-Bermuda Reflections", 42 J. Air L. & Com. at 780 (1976).

22. As will be seen later, the writer concludes that multilateralism in the form of regional agreements are practicable and would lead to a global multilateral agreement in the long run. See infra (footnote 62).

advances in air transport technology, particularly with respect to long-term range, wide-bodied jet aircraft, increased the utility of international aviation to mankind and resulted in a dramatic expansion of the traffic markets far beyond the expectations of the delegates in 1944. In addition, fifth freedom traffic which has always been one of the stumbling blocks reaching a multilateral solution, is apparently less crucial now than in the immediate post-war era when it was indispensable for trunk airlines.[23]

As to international air transport ratemaking, most tariffs of scheduled operations are still theoretically set within the multilateral framework of IATA,[24] albeit subject to individual governmental approval. A multilateral solution would thus merely give legal expression to what in fact is already a multilateral approach. In this respect, it should be noted that the only multilateral agreement which could be achieved in the ratemaking field is the "1967 International Agreement on the Procedures for the Establishment of Tariffs for Scheduled Air Services", which in

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23. Warner, "How Can a Multilateral Agreement in International Air Transport be Attained?", in Studi in Onore di Antonio Ambrosini, Milan at 587 et seq. (1957).

24. With respect to non-scheduled operations, their tariffs are generally determined by the free forces of the marketplace. See infra Chapter VII, Section I.

practice is limited to Europe.[25] Recently, however, the United States and a number of ECAC administrations reached a multilateral understanding with respect to agreed tariff-zones and voluntary tariff coordination for scheduled services on the North Atlantic routes.[26] It is of interest to note that this "Memorandum of Understanding" is "the first multilateral agreement in the United States aviation history".[27] Notwithstanding the American aversion to multilateralism, there is still room for optimism. In addition to this agreement, the head of the United States CAB once clearly stated that achieving a multilateral regime for air transport is one of the American aviation policy goals.[28] Also, Trent (Deputy Secretary of Trans-

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25. For more details, see infra Chapter VII, Section I (footnote 34).

26. For the U.S.-ECAC tariff agreement, see infra Chapter VII, Section IV.

27. Stated by McKinnon, the Chairman of the U.S. CAB. See Ott, "Backing Rises for Atlantic Fare", Aviation Week & Space Tech. at 26 (May 10, 1982).

28. See "Goal of Multilateralism Rushed", Aviation Week & Space Tech. at 25 (Jan. 15, 1979). It should also be remembered that the U.S. held several discussions with The Netherlands attempting to draft a "plurilateral" or multilateral air transport agreement. See Bornemann, "Air Transport Organization and Policy", ITA Bull. at 161 (Feb. 16, 1981); Aviation Week & Space Tech. at 49 (March 3, 1980).

portation) recently said that "the Reagan Administration is committed to finding a multilateral solution" to lessen the economic problems that were facing the airlines on the North Atlantic.[29] In fact, through multilateral pragmatism the United States, along with the other nations of the world, can ensure that air travel on economical rates is available to all sections of the world.

The multilateral ratemaking process was and still is, to a certain extent, endangered by the international deregulation policy (i.e. liberalization of international aviation) which promotes a liberal ratemaking system.[30] Nevertheless, multilateral regulation of both tariff and capacity was firmly defended by most nations within the framework of ICAO.[31]

One should also mention an often overlooked de facto multilateralism which is usually found in the so-called administrative clauses in bilateral air transport

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29. See "US Promulgating Policy on Transatlantic Aviation", Aviation Week & Space Tech. at 47 (Feb. 14, 1983).

30. See infra Chapter VII, Section III.

31. See infra Chapter VI, Section III; Chapter VII, Section V.

agreements.[32] These provisions have actually achieved a remarkable degree of international uniformity and cover many important matters such as compliance with the Chicago Convention, with the bilateral agreement itself, with local laws and regulations, transfer of earnings, exchange of information, local representation, exemption from charges on equipment, fuel, stores, etc., consultation, settlement of disputes and substantial ownership and effective control. Should a multilateral form be possible, it would also be desirable to introduce additional provisions to curb the present trend towards unilateralism in the imposition of conditions governing the operation of the agreed services that often have the effect of stultifying the agreement.[33] It is thus believed that a broad degree of uniformity among a large number of States, even on such matters as administrative clauses, can from the practical point of view, be of a real value.[34]

Finally, it should be kept in mind that transit rights are generally exchanged through acceptance by the

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32. Cf. ICAO, Handbook on Administrative Clauses in Bilateral Air Transport Agreements, ICAO Circular 63-AT/6 (1962).

33. See infra note 44 of this Chapter.

34. Browne, "Adrift on the Air Ocean", 77 Aeronautical J. at 71 (1973).

States concerned of the multilateral "International Air Services Transit Agreement", the so-called "Two Freedom Agreement". The main difficulty centres, of course, on the exchange of commercial rights, including the actual exchange of routes and capacity control. However, it is not (in the words of one well known commentator) impossible "to hope that, in the interest of a general (multilateral) agreement, some compromise between the present divergent views might perhaps be found"[35] on the exchange of such rights.

The revival of multilateralism is nourished by and recommended in the recent academic literature, some of which advocates a worldwide multilateral approach to economic regulation. For example, one author prescribes the establishment of a multilateral system for the granting of traffic rights, the designation of carriers and the distribution of revenues.[36] Another commentator has argued for a revival of the ICAO's 1946 Draft Multilateral Convention on the grounds that it would simplify "the...maze of bilateral agreements", centralize economic planning in an

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35. Cheng, "Beyond Bermuda", in Matte Ed., op. cit., note 16, at 85. The alternative would be to leave the actual exchange of such rights to subsequent bilateral bargaining and individual agreements.

36. Gleditsch, "Towards a Multilateral Aviation Treaty", 14 J. Peace Research at 240-241 (1977).

international regulatory board, and result in lower fares for air travellers.[37] Meanwhile, Cheng envisages a multilateral system of a priori regulation of capacity for both scheduled and non-scheduled international air transport, combined with tariff fixing.[38] Whereas those commentators focused their attention on certain prominent aspects of the subject, Guldimann's multilateral scheme[39] is an example of a systematic approach involving all "sub-systems and components" of the regulatory framework for scheduled and non-scheduled air transport. The "natural requirements for any regulatory system" are, in his opinion, stability, predictability, consistency and also easiness of implementation. Finally, other suggested approaches include a multilateral exchange of all five freedoms of the air for non-scheduled air services only,[40] and a multilateral convention for the regulation of user charges.[41]

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37. O'Connor, Economic Regulation of the World's Airlines: A Political Analysis at 131-138 (1971); supra, Chapter I (footnote 78).

38. Cheng, op. cit., note 35, at 95-96.

39. Guldimann, op. cit., note 16, at 119, 123-124.

40. Scoutt & Costello, "Charters, The New Mode: Setting a New Course for International Air Transportation", 39 J. Air L. & Com. at 24-25 (1973).

41. "User charges" are the charges air carriers must pay

This brief review for the possibility of reviving a multilateral approach suggests that such solution is needed more than ever in international air transport law. The current chaos can only be contained on a multilateral basis. One can picture a multilateral regulatory framework dealing with tariffs, capacity and fair competition rules as well as the setting up of an enforcement mechanism with ICAO. Such a framework would still leave a vacancy for bilateral bargaining on the exchange of traffic rights, but would at least have the advantage of creating a kind of uniform economic law of civil aviation, even if only in an immature form.

Obstacles in Achieving Multilateralism

It may seem contradictory to mention a revival of multilateralism when one of the leading scholars has recently observed that "States have been moving from the multilateral via the bilateral to a unilateral approach of the regulation of international civil aviaton".[42] Indeed,

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for the use of airports and airways. See Pogue & Davison, "User Charges in International Aviation", 73 Am. J. Int'l L. at 42 (1979).

42. Wassenbergh, Public International Air Transportation Law in a New Era at 43 (1976).

the brutal fact of life for international air transportation is that "unilateral action by governments with the intention of implementing policy or effecting legal relationships (sic) with other States is on the rise".[43] Since sovereign States are often unwilling to tolerate direct limitations on their ability to implement national air transport policies, such governmental involvement has in turn led to a system of threats and counterthreats aimed at deterring the other party from operating efficiently in the marketplace. Unfortunately, unilateral action breeds unilateral reaction, and it becomes more and more difficult to separate cause and effect.[44]

Current trends and developments in international air tansport, however, indicate a more favourable disposition towards a multilateral solution to problems than was possible at Chicago.[45] In order to preserve an interna-

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43. Dold, "The Competitive Regime in International Air Transportation", 5 Air Law at 140 (1980).

44. One way to solve this problem is to amend or renegotiate bilateral agreements so as to forbid those types of unilateral actions which have come to interfere with the operation of efficient air services between two countries. From the writer's point of view, a more effective solution would be provided by regional air transport agreements which could prohibit certain unilateral actions.

45. Cheng in his report before the Air Transport Commis-

tional order in an increasingly complex and interdependent world, "a new Chicago Conference might (thus) be necessary by the end of this century".[46] On the other hand, one should not be over ambitious in reaching a worldwide multilateral approach in the short run due to the conflicting national policies that now exist in the industry.

In this context, it should always be remembered that "multilateralism" in 1944 meant something quite different to the European, Asian, African and Latin American nations than it did to the United States. While the American delegation to the Chicago Conference sought to use a multilateral Convention essentially to "codify" a free market ethic, other nations saw a multilateral agreement as a way to ensure that the robust United States airline industry would not monopolize international civil aviation. Many governments regarded international air transport as a political matter,[47] and selected one airline as the instrument of this policy; nationalizing and subsidizing it,

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sion of the ICC, Doc. 310/INT/39; supra note 22.

46. Lipman, Speech delivered to the Egyptian Academy for Scientific Research and Technology, Cairo (1984).

47. For a good review of the development of the aviation industry, see Davies, A History of the World's Airlines, London, Oxford University (1964).

covering its expenses and absorbing its losses. This political nationalism constituted another stone-wall. When nations merged their airlines they conceded some of their individual identity and prestige[48] abroad. In this context, however, some commentators have tried to give developing States a sense of guilt for "establishing national airlines to show their flag throughout the world". In a satirical comment, historian Laqueur has written that a viable "modern" State must have a minimum of four attributes: operation of a television-system, a police force of at least 100 men, a budget sufficient to maintain at least one delegate at the United Nations, and a national airline.[49] It is fallacious generalisation to state that any developing country established an airline just to show its flag abroad. In fact, it is the developed States, which attached so much importance to "national prestige" through the airlines. Colonel Moore-Brabazon once stated, in the English Parliament, that:

> "I hate the word 'prestige', but I like to bring it in for the reason that every

48. The term "prestige" might be defined as the opinion which the world holds of the airline's country, the respect in which the nation is held, either in a general sense or in a specific sense as for its technological achievements.

49. Laqueur, "Six Scenarios for 1980", New York Times Magazine at 29 (Dec. 19, 1971).

> English aircraft which travels from one side of the world to the other is a little bit of England. England will be judged by that little bit by those for whom that is the only thing they know of England."[50]

Another example may be taken from the Soviet Union which sometimes promoted its national airline in the hope that the peoples of the world, seeing it (and the Soviet-manufactured aircraft it employed) would be impressed not only with Russian technology but with the ideology of the system.[51] Even Japan hoped that their ability to operate safe and efficient airlines would contribute toward persuading the world of the soundness of their industrial products.[52] The other developed States may not be doing the same thing, but the truth remains that national prestige is no less attached to their airlines. They presumed that the existence of an international airline would in some manner give them added political weight in this relationship with other governments.[53] In addition to the political and prestige considerations, airlines were also seen by most of these

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50. Cited in Lissitzyn, International Air Transport and National Policy at 57 (1942).

51. O'Connor, op. cit., note 37, at 90.

52. Id.

53. See CAB Regulation of Foreign Air Carriers Under Part 213, 4 N.Y.U. J. Int'l L. & Pol. at 239, 242 (1971).

developed and developing countries as important to their national security in that they provided airlift reserves during emergencies.[54]

A competitive multilateral regime which would drive uneconomical airlines out of business in favour of United States carriers therefore was simply not acceptable to the majority of nations represented at Chicago. Many of them based their economies on central planning, rather than market forces, and virtually all viewed such "open skies" policy with suspicion as a doctrine that "merely allow rich nations to become richer at the expense of the poor".[55] As a result, a restrictive tendency in international aviation developed, and in many States, protectionism continues to form the centerpiece of national air transport policy. The international aviation community has grown to include numerous developing States no more willing to allow their airlines to live or die at the mercy of market forces than

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54. Airlines are also used for espionage and, before anything of course, as economic instruments. For a good presentation on the various uses of airlines, see Gidwitz, The Politics of International Air Transport at 21-28 (1980).

55. Salacuse, "The Little Prince and the Businessman: Conflicts and Tensions in Public International Air Law", 45 J. Air L. & Com. at 834 (1980).

the United Kingdom or France were in 1944.[56] In fact, Ghandour (the President of Royal Jordanian Airlines - ALIA) has recently correctly remarked that "the U.S. CAB was formed to protect U.S. air transport in its infancy. Now that U.S. airlines have reached maturity, the 'protectionist policies' are being dismantled. Undeveloped and developing countries still need protection for their airlines".[57]

The years since 1944 also witnessed other dramatic changes in the international economy. A significant shift in wealth from the west - and from the United States in particular - to other parts of the world has taken place. With that alteration has come the emergence of new centers of power which now insist on having a voice and sharing in international lawmaking. The international community has thus shifted from a rather "homogeneous club of western industrialized countries to heterogeneous group"[58] which now includes economies in various stages of development and

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56. See, "The Ins and Outs of IATA: Improving the Role of the U.S. in the Regulation of International Air Fares", 81 Yale L. J. at 1139 (1972).

57. Stated by Ghandour, "IATA Set on a New Course - 34th AGM Approves Important Changes", 34 Interavia at 71 (1979; see also Goedhuis, "The Changing Legal Regime of Air and Outer Space", 27 Int'l & Comp. L.Q. at 581 (1978).

58. Salacuse, op. cit., note 55, at 834.

reflecting divergent ideologies. The dramatic increase in world fuel and energy costs (in the early 1970's) is considered a major factor for this shift in wealth. It has also had a direct and immediate impact on international civil aviation in the form of rapidly escalating operating costs, which when coupled with increased capital outlays, has resulted in reduced carrier profit margins, a powerful force indeed prompting the nations of the world to take unilateral actions to protect their national carriers.

From the above brief presentation, the various difficulties in approaching a comprehensive multilateral framework may be summed up as follows:

(a) As a consequence of decolonization since World War II, numerous new independent States have become members of ICAO. The existence of such States, with so many different traditions, cultures and ideologies, will undoubtedly complicate the process of arriving at a consensus on any issue relating to international air transport.

(b) Aviation is actually entwined in a State's economic and particularly political policy. As long as there is no wider co-operation in these fields, it is unlikely that States will give up this vital political and economic tool to a multilateral approach, as they prefer, to keep them under control through bilateral agreements.

(c) In negotiating bilateral air transport agree-

ments, the governments can control the exchange of traffic rights in favour of their respective carriers, and to establish part of the regulatory framework for the latter's activities. Certain countries can thus gain privileges that they otherwise may not have achieved if they had adhered to a multilateral agreement.

(d) It is unrealistic to expect in the very near future a universal multilateral system given the heterogeneous character of the world aviation community. The difficulties emanate from "the different aeronautical potential of each country, from the variations found when considering each country, as a source of traffic, from the varying importance of each country in international air transport (according to its climatic or geographic conditions) and lastly, what is more important, the substantial differences between the countries already in commercial aeronautics, and those countries... which can only look to the future".[59]

(e) The fact that ICAO is unable to do more than what is permitted through a consensus of its member States, since that is the practical way in which the international community functions today.

A truly multilateral regime, however, is seen as a

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59. See ICAO Doc. 4510, op. cit., note 5, at 46.

long term goal, not a realistic possibility in the short run. The ICAO eventually resigned itself to this view, simply noting that "one of our permanent objectives...is to find a multilateral basis for the exchange of commercial rights for international air transport".[60] In short, it seems that "everyone wants a multilateral agreement; but some of those who want it disagree with one another vigorously on what it should say, or what effects it should have". It has so far been impossible to attain the measure of concession and compromise that would bring the conflicting views together on common ground. The resultant "deadlock can, of course, end: but to end it there must be further modification in positions heretofore maintained".[61]

To conclude this section, while complete multilateralism (encompassing all the nations of the world) is no more likely to pass muster today than forty-one years ago at Chicago, it is the writer's view that multilateralism in the form of regional air transport agreements might be instituted successfully in the prevailing regime of international aviation.[62] Such regionalism could be considered as a

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60. 14 ICAO Bull. at 71, 77 (1959).

61. Warner, op. cit., note 23, at 590.

62. See infra, "The Possible Solution", in Chapter VIII;

transitional process towards a broader multilateralism in the long run, and thus enable the world civil aviation community to approach the uniform, universal regulatory regime sought at Chicago.

SECTION II - REGIONALISM AS AN INTERJACENT ASCENT TOWARDS MULTILATERALISM

Analytical Introduction

The most striking feature of the international scene today, as contrasted with a century or even a generation ago, is the tremendous growth of international organizations of all types.[63] Such an organization might be, inter alia, global or regional in character.[64] The former is open to membership of all States from different

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supra note 22.

63. See Bishop, International Law, Cases and Materials, Third Edition, Brown and Company at 224 (1971).

64. International organization may be classified in many different ways, depending on either its structure or its functions. For exmaple, it can be public or private, functional or general, technical or political etc... See Kunz, The Changing Law of Nations at 469 et seq. (1968); Cheever, Organizing for Peace: International Organization in World Affairs, London at 6 et seq. (1954).

regions, whereas the latter is instituted among a certain number of States gathered together by a certain bond or policy.

In recent years, there has been a growing awareness of the vital need for devising regional mechanisms with a view to ensuring better coordination of economic and social policies. It is felt that certain problems can be better resolved and immediate and speedy results obtained by organizing co-operation at a regional level.[65] One commentator has observed "the widespread application that is being given to the concept of regionalism at the present time. First and foremost, this concept has now received general recognition among international lawyers, international administrators and statesmen as a standard formula or device for solving particular problems."[66] Indeed, the settlement of difficulties impeding an efficient and rational system of commercial air transportation might be facilitated within this formula.

The rapidly changing pattern of economic and social

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65. See, e.g., Krause, International Economics, Boston at 617-631 (1965); Kindleberger, Economic Development (Ed., McGraw-Hill) at 345-360 (1965).

66. Starke, "Regionalism as a Problem of International Law", in Law and Politics in the World Community at 114 (1953).

life, the spread of technological innovations to the hitherto agricultural societies, and the revolutionary improvements in transport and communication have been universally recognized as powerful forces in contributing to the growth of regional economic groups. Usually, the original impetus for the formation of any regional group comes from geographical proximity and deep-rooted historical, political and cultural ties. In fact, the old concept of the self-sufficient national State has given place to new theories[67] under which the economic realities of life make it imperative to pool resources in order to achieve the benefits accruing from the economies of scale, larger markets and greater bargaining power in promoting exports.

In this context, however, one should note that nations (by their nature) live by a "territorial imperative", i.e. "territorial sovereignty". They see therefore their neighbouring countries as a potential threat to their social and economic life. This meant that States (with their territorial sovereignty) in order to maintain their territorial integrity, have the choice between war and peace, between expansionism and co-operation. It has been correctly suggested that the "wars of our time" are caused,

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67. Chuzmir, Regionalism in International Civil Aviation, Manuscript, Harvard Law Library at 1-20 (1966).

inter alia, by economic and social factors, and that regional co-operation in these spheres on a non-political level would contribute to "regional peace" and hence to "international security".[68] Thus, for co-operation, a first requirement is to build up a close peaceful relationship with neighbouring nations.

This peaceful geographical criterion creates the first basis for regionalism, since this form of multilateralism is a geographical phenomenon. The future development of international civil aviation can help to create and preserve friendship and understanding amongst the nations and peoples of the world; its abuse may still become a threat to general security.[69] However, another equally significant requirement of regionalism, as has been shown, is "affinity"; i.e. a similarity in origin, culture, ideology, tradition, or way of life. Finally, an "economic interdependence" and a "common economic interest" must be apparent.[70] For civil air transport, this common

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68. Sir Frederick Tymns, "Freedom of the Air", 70 Journal of the Royal Aeronautical Society at 438-440 (March 1966).

69. See the Preamble of the Chicago Convention.

70. Wassenbergh, "The Future of Multilateral Air Transport Regulation in the Regional and Global Context", Conference on Regionalism in International Air Transport: Co-operation and Competition, held under the

interest can only be the desire of nations to strengthen the mutual aviation relationship and to enhance, through regional co-operation, the quality of their airline industry.

It is worth noting here that nothing in the Chicago Convention prevents the establishment of regional civil aviation arrangements between the contracting States thereto. It would even probably not be incorrect to say that, in one way or another, the Convention encourages the establishment of such regional arrangements. In Article 55(a), the Convention expressly refers to the concept of regionalism, by stipulating that the ICAO Council may -

> "where appropriate and as experience may show to be desirable, create subordinate air transport commissions on a regional or other basis and define groups of States or airlines with or through which it may deal to facilitate the carrying out of the aims of this Convention".[71]

Indeed, during the Chicago Conference of 1944, a framework for multinational co-operation was established in broad terms, and the Chicago Convention devoted one chapter

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auspices of the MIT and Alia, Amman-Jordan at 4 (April 19-21, 1983) (hereinafter cited as Conference on Regionalism).

71. In this regard, it should also be noted that ICAO itself established, on a regional basis, six Regional Offices of Air Navigation Bureau distributed among the different regions of the world.

(XVI) to the subject "Joint Operating Organizations and Pooled Services". The Convention simply states in Article 77, that such arrangements are permitted, but shall be subject to all provisions of the Convention. This Article stipulates, inter alia, that:

> "Nothing in this Convention shall prevent two or more contracting States from constituting joint air transport operating organizations or international operating agencies and from pooling their air services on any routes or in any regions .... The Council shall determine in what manner the provisions of this Convention relating to nationality of aircraft shall apply to aircraft operated by international operating agencies."

As is evident from its wording, Article 77 welcomes transnational co-operation (in more than one form) and is therefore seen, according to one scholar, the solution for one of the fundamental problems of present time, namely, "the transfer of the benefits of modern and expensive technology to developing countries for their enjoyment on an autonomous basis".[72] This Article actually distinguishes between two types of organizations. The most advanced is the "international operating agency".[73] Its aircraft shall

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72. See FitzGerald, "Nationality and Registration of Aircraft Operated by International Operating Agencies and Article 77 of the Convention on International Civil Aviation, 1944", Can. Y.B. Int'l L. at 196 (1967).

73. It has to be remembered that until now, no interna-

be entered on a joint or international register, and the ICAO Council shall determine how the nationality provisions of the Convention shall apply to the agency's aircraft.[74]

The second type is the "joint air transport operating organization". A State may participate in such an organization either through its government or through an airline company designated by the government.[75] The company may be State-owned, or partly State-owned, or privately owned. It should always be kept in mind, however, that since the Chicago Convention gives no concrete definition of either type of organization, the two terms have been

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tional operating agency has been established. Winberg, "The Problems and Advantages of a Multi-Nation Airline", Study presented to the Conference on Regionalism, op. cit., note 70, at 14.2.

74. In 1967, the Council determined the procedure it would apply to any specific plan for joint or international registration presented to it. ICAO Doc. 8722-C/976 (20/2/68). However, it would be beyond the scope of this thesis to go into further details about this problem, but for more information, see, e.g., Cheng, "Nationality of Aircraft Operated by Joint or International Agencies", 32 J. Air L. & Com. at 20 et seq. (1968); Goreish, Registration and Nationality of Aircraft of International Operating Agencies, unpublished thesis, McGill University, Montreal at 149 et seq. (1970).

75. See Article 79 of the Convention. The SAS Consortium, Air Afrique and Gulf Air are examples of such organizations.

used interchangeably.

Article 77 of the Convention also mentions "pooled services". They originate from agreements between airlines for the operation by them of one or more routes and allocation of revenue derived from such operations.[76] The ordinary pool agreements are governed by the general law of contracts, and differ from joint operating organizations in that there is no joint contribution of capital and no merging of operations, and each pool partner works for his own account, bearing the losses and keeping the profits severally. In short, the advantages of such agreements are, generally, that they limit those effects of competition which are detrimental to the public service, that they lead to better utilization of equipment, that they offer opportunities for airlines to extend their traffic markets, and that they enable the airlines to reduce costs. Of course, these potentialities also exist in a joint operating organization, where the routes are served by an operational entity for the joint account of the partners. However, for a joint

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76. For up to date details of these pool agreements, see, e.g., Rosenfield, The Regulation of International Commercial Aviation: The International Regulatory Structure, Oceana Publications, New York (November 1984); Brandel, Recent Trends in European Air Transport Law and Policy with Reference to Routes, unpublished thesis, McGill University, Montreal (1984).

organization, there would exist considerable scope for still better performance due to the greater commonality of interests, provided that separate national pressures do not adversely affect the conduct of business.

It is therefore inevitable that regional co-operative efforts have a legitimate role in the development of sound international air transportation industry. Unfortunately, the "gradual" approach to regionalism in air transport policy is apparently still at the level of the consultative character of inter-governmental regional organizations and the regional inter-carrier organizations.[77] Every State, therefore, should devote more effort to regional co-operation for the sake of the public and the aviation business. Progress towards this end will offer a substantial impetus to economic development of aviation and international co-operation in general as a step towards a broader multilateralism in the long-run.

Significantly, there has been recently general discussion of the various advantages of a regional approach to international aviation problems. One author envisaged the establishment of a North Atlantic air transport agreement might encourage the development of other regional

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77. Cf. Gazdik, "Multilateralism in Civil Aviation", 4 Air Law at 130 et seq. (1979); Wassenbergh, op. cit., note 70, at 9.

regulatory arrangements, and even inter-regional agreements, and thus enable the international aviation community to approach a universal multilateral agreement to economic regulation.[78] Another commentator believed that economic benefits would result from abandoning the bilateral system in favour of a regional approach, since "bilaterally negotiated traffic rights...(are) a serious impediment to achieving efficient operations".[79] According to him, a regional political system of negotiating air rights would bring the operating flexibility that ultimately would result in improved profits and consumer benefits. One scholar has even remarked that "the long-range outlook for the exchange of air traffic rights internationally may be that...a somewhat greater number of services will be internationalized on

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78. Sion, op. cit., note 13, at 161, 198 et seq. For almost the same notion, see Klem & Leister, "The Struggle for a Competitive Market Structure in International Aviation", 11 Law & Pol'y Int'l Bus. at 557, 591 (1979). See also, "U.S. IATA Differences at New York Conferences", 16 Air Transport World at 54, 57 (1979), whereas the Chairman of British Airways suggested that "some international obstacles could be avoided by developing international joint regulatory machinery along the lines pioneered by GATT and EEC, possibly leading to a multilateral approach of the air".

79. Simpson, Head of MIT's Flight Transportation Laboratory, in his Statement before the Conference on Regionalism, op. cit., note 70.

a regional basis".[80] Unfortunately, he predicts, this is not likely to occur until the early 21st century.

As a conclusion to this brief introduction, one should note that regionalism in civil aviation will undoubtedly be fully successful if the neighbouring nations are willing to closely co-ordinate their air transport policies with the aim to integrate the interests of their flag carriers into one regional aviation interest. In addition, the absence of sharp political disagreement among potential participants would be an essential prerequisite for securing such integration: a factor which indeed has, on certain occasions, been decisive in overturning a consensus based on the economic necessity and feasibility of such arrangements.

Forms of Regionalism

One cannot deny the important role that civil aviation plays in the economic and social integration and development of different States all over the world. One of the essential necessities for the growth and well-being of any region in the world, is an efficient transportation

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80. FitzGerald, "Air Law: 1972-2022", 51 Can. B. Rev. at 272 (1973).

system which can be realized through the establishment of regional organizations.

For air transport, regionalism is a code word used to describe a wide variety of multi-country or multi-airline ventures in a particular geographical area.[81] It can include governmental organizations, for example ACAC, AFCAC, ECAC and LACAC. It can include associations of airlines, such as AACO, AAFRA, AEA, AITAL and OAA.[82] Regionalism's wide swathe covers co-operation in air navigation problems, like Eurocontrol, ASECNA and COCESNA.[83] It can also cover technical cooperation, such as ATLAS, KSSU and the

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81. The various forms of regional aviation organiations that now exist, make it difficult to give a concrete definition for the concept of regionalism. However, for general definitions of this term in aviation, see Feldman, "Regionalism Facing Many Challenges as a Replacement for Bilateral System", Air Transport World at 48 (Aug. 1983).

82. In sum, such associations are concerned with traffic, economic, technical and legal matters specific to their airlines. They may operate technical pools for certain aircraft types at regional airports and also conduct common training programs for personnel in specific positions.

83. These governmental bodies were established to unify traffic control system for its member States and achieve improvements in aeronautical communication services and navigational aids.

Arab Technical Consortium,[84] as well as existing or fledgeling joint airline ventures, for example SAS, Air Afrique and Gulf Air. Often today, regionalism implies the concept of Third World States and/or their airlines banding together, within the same area, to try to overcome either (a) their own individual lack of efficiency, resources and traffic, or (b) what they consider to be inequities in an aviation world dominated by big countries and big airlines. For the purpose of this work, some emphasis will only be paid in the following pages on a number of such regional arrangements.

Government air transport regulatory agencies have joined together in several regional bodies in pursuit of coordinated and standardized regional department, efficient use of regional facilities and institution of common regional regulatory procedures. One of the youngest of such bodies is LACAC (the Latin American Civil Aviation Commission). It was established in December 1973[85] with ICAO encouragement as a consultative body, so that its recommendations and resolutions are subject to approval by each

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84. These corporations are organized between airlines for the purpose of providing a joint maintenance and overhaul program for jet aircraft.

85. See ICAO Recommendation C.WA/5925, Appendix B.

State.[86] LACAC is open to all States located in Central and South America, including Panama and Mexico, and the States of the Carribean. Its primary objective is to provide a forum within which to discuss and plan co-operation and coordination of civil aviation activities, in particular, inter alia, orderly development and better utilization of air transport and also foster implementation of ICAO standards in Latin America.[87]

ACAC, the Arab Civil Aviation Council, was founded in 1967 under the auspices of the League of Arab States.[88] Membership is open to all States members of the League. In addition, membership is open to Arab States, not members of the League, if accepted by two-thirds of the members. In fact, ACAC was established on the basis of the provision of Article 2 (paragraph b) of the Arab League Pact relating to close co-operation in the field of aviation by

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86. Statute of LACAC, Mexico, D.F. 14 Dec. 1973 (Article 3).

87. For the LACAC's activities, see Bogolasky, "Air Transport in Latin America: The Expanding Role of LACAC", 44 J. Air L. & Com. at 75-107 (1978).

88. The Arab League Council, at its 43rd Ordinary Session held in Cairo on March 21, 1965, approved an agreement establishing ACAC. The Agreement came into force on the 4th of October 1967, and ACAC held its first meeting on November 6, 1967, at the premises of the Arab League in Cairo.

means of fostering the development of air transport services between Arab States, and promoting co-operation in all aspects of that field. Its aim and objectives are, inter alia, to promote the principles, techniques and economics relating to air transport, and to foster and encourage its development in both Arab and international fields.[89]

The African Civil Aviation Commission (AFCAC) was founded in 1969 and was based upon an earlier Conference which recommended that ICAO should consult with the Economic Commission of Africa (ECA) and the Organization for African Unity (OAU) with a view to establishing an African Civil Aviation Organization.[90] AFCAC's Constitution provides that membership shall be open to all African States, members of either ECA or OAU. It also provides that it shall be only a consultative body, and that its recommendations shall be subject to acceptance by each individual State. In 1978 AFCAC became a Specialized Agency of the OAU to give a formal framework to the promotion of a common African policy

89. For full details on the ACAC's objectives, see "Policy of ACAC in the Field of International Air Transport" approved at the Sixteenth Session in Cairo, ACAC Decision No. S-16-3 (January 24, 1978). For a copy of this Policy, see Rosenfield, op. cit, note 76, Booklet No. 17.

90. See Conference on the Establishment of AFCAC, E/CN./14/448/TRANS/34, OAU/AFCAC/3.

in civil aviation matters.[91] The main purpose of such regional body is to provide the civil aviation authorities of member States, as in LACAC, with a framework for co-operation and negotiation in order to make better use of the African transport system. To this end, the Commission is expected to carry out studies and formulate plans within the area to encourage growth of traffic, standardization of equipment, and to consider the possibility of integration of government policies, as well as the encouragement of application of ICAO standards.[92]

ECAC, the European Civil Aviation Conference, was formally constituted in 1955 as a result of the "Conference on Coordination of Air Transport in Europe (CATE)" convened by ICAO at Strasbourg in April 1954.[93] The Conference is intended to be consultative in nature, and hence any recom-

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91. Under this Agreement, membership in AFCAC or exclusion from such membership is subject to approval by the OAU Assembly. See also "AFCAC-10 Years Later", May 1979, Document Published by AFCAC.

92. On the activities of AFCAC, see the Annual Report of the ICAO Council, in the section on "Participation of Regional Offices in the Activities of Air Transport"; id.; Ndum, Africa's Civil Aviation Law and Policy, unpublished D.C.L. thesis, McGill University, Montreal (1984).

93. ICAO Doc. 7575, Recommendation No. 28. For a copy of this Resolution, see European Yearbook, Vol. II, at 609-611 (1956).

mendations are subject to approval of the individual governments. According to a mutual understanding, it is interesting to note that the status of ECAC with respect to ICAO is of a special nature. It is neither a subordinate or regional body of ICAO (as is contemplated in Article 55 of the Chicago Convention) nor completely independent, but has an intermediate status. It is a separate body, but one that works closely with, and with the partial financial support of, ICAO.[94] It calls its own meetings, sets its own work programs, and determines its own agenda, but depends on ICAO for secretariat service. In short, ECAC's principal task is, inter alia, to review development of intra-European air transport in order to promote coordination; better transport; and to consider any special problems in that field.[95]

One should also mention that economic co-operation on the level of airlines will lead to coordinated air policies of the participating countries. Such regional co-operation between airlines can take the form of a consor-

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94. See ICAO Doc. 7676-ECAC/1, Resolution No. 1, ICAO Doc. 7670, Vol. II of July 1956; Matte, Treatise on Air-Aeronautical Law at 268 (1981).

95. For more details, see Weber, European Integration and Air Transport, unpublished thesis, McGill University, Montreal at 54 et seq. (1976).

tium of carriers and as such create a single "chosen instrument" for the governments concerned of the region, or of multilateral pool agreements, interchange of aircraft arrangements, blocked-space agreements, etc. A successful example of co-operation between airlines is found in the Scandinavian Airlines System (SAS), the multinational air carrier of Denmark, Norway, and Sweden. Historically, the need for the operation of inter-continental air services inspired the three small Scandinavian countries to pool their resources together in one joint stock company as a device for survival in the face of relatively very strong foreign competitors. Thus, in 1946, a Consortium Agreement was concluded among the national airlines for the operation of these services,[96] known as OSAS (SAS Overseas Division). In 1950, however, a new comprehensive agreement was reached that brought into existence the present SAS structure[97] as an integrated operating entity with most of the characteristics of a single company.

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96. See Bahr, "The Scandinavian Airlines System: Its Origin, Present Organization and Legal Aspects", 1 Arkiv for Luftrett at 204 (1961).

97. It should also be noted that the Consortium Agreement was again revised in 1962, primarily with regard to the management functions. For a most interesting illustration on the history of SAS up to now, see Winberg, the former head of Swedish civil aviation, op. cit., note 73.

The various Scandinavian national companies had a keen realization of the fact that "they could further their interests to greater advantage by acting in concert than they could hope to do acting separately".[98] Indeed, the immediate and present results are promising. SAS became the twelfth largest international airline in the 1950's and has continued to be one of the most viable carriers in the world. This success seems to be drawn from its structure. In brief, it is a consortium, owned 2/7 by the Danish airline (DDL), 2/7 by the Norwegian airline (DNL), and 3/7 by the Swedish airline (ABA). Each of the national airlines is a company, the shares of which are owned 50% by private interests and 50% by government. The Parties jointly own all the properties and rights in these proportions, and share any profit and any loss, and are responsible for the obligations of the Consortium in the same proportion. As against third States, they are jointly and severally liable for any obligation which might arise for the Consortium in connection with its activity. The main objective of the Consortium is to carry out, as an entity, commercial air traffic and other business in connection therewith, for the joint account of the three national airlines, under the name

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98. ICAO-"Report on the Scandinavian Airlines System (SAS)", Circular 30, AT/5 at 4, Para. (5).

"SAS".[98] For this purpose, the operating permits for both domestic and international air services, which had been granted to the national airlines by the respective Scandinavian governments, were transferred to the Consortium. One may indeed wonder if it is still possible to expand this solid precedent of co-operation to larger geographic regions for the sake of a rational and efficient air transportation industry.[99]

After having briefly discussed above some of the regional forms in air transport, it may appear appropriate now to try to determine the outstanding achievement of regional co-operation in aviation in respect of current regulatory problems. From this regulatory viewpoint, it may be argued that co-operation between the African States in AFCAC and especially also between the African carriers in AAFRA bears testimony of the will to find constructive solutions.[100] The regional co-operation between the Latin American countries (LACAC/AITAL) still emphasizes the

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99. Atwood, "Regional Aviation Agreements: A Desirable Alternative to Bilateralism", 24 ITA Bull. at 533 (25 June 1979).

100. N.B. The intra-African scheduled air services network, like the present intra-European scheduled network, is politically determined, reason why, on a bilateral basis, mainly (uneconomic) point-to-point services are operated. CF. Wessberge in 3 ITA Bull. (Feb. 1983).

sovereignty of States with respect to aviation, while the European States cannot find a "common air transport policy" because of the extreme "nationalism of a number of them".[101] It can also be stated that Asian aviation co-operation is still in an embryonic stage, whereas East European co-operation remains an instrument of the official policy of the member of States. Seemingly, the regional co-operation between the Arab States "contains many elements of a sound outward looking approach".[102] It is even seen that Arab Cooperative efforts in aviation "will continue on a regional basis...where joint ventures and co-operation between civil aviation administrations and airlines are already well advanced".[103]

It is no secret that Arab States are increasingly considered by world airlines as intermediate nations generating traffic. They are connected with every continent, with the exception of South America.[104] With a vital geogra-

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101. C.F. Gidwitz, op. cit., note 54, at 89 et seq.

102. Wassenbergh, op. cit., note 70, at 18.

103. Cf. Lipman, "Air Transport: The Next 25 Years", IATA Review at 8 (July-September 1984).

104. For the role played by the Arab States as a gateway on major world routes, see "The Middle East, the Gateway to the World", 31 ITA Bull. at 815 et seq. (Sept. 21, 1981).

phical situation on the major world routes, a great number of airlines quite naturally view the Middle East stations as a means of improving their load factors on long-haul routes. The growing economic importance of this region is also an incentive to intensifying services to its airports. In response to this pressure from foreign carriers, Arab airlines are trying to bolster their position through co-operation.

The main success in co-operation is probably to the credit of Gulf Air, whose capital since April 1974 has been distributed equally among its various shareholders which, apart from the United Arab Emirates, are Bahrain, Oman and Qatar.

Regional co-operation in the Middle East is, in fact, no novelty. The Arab Air Carrier Organization (AACO) was established in 1965 on the initiative of the League of Arab States. The objectives of such an organization are not confined only to agreement on fares and rates but call for economic co-operation (through pooling arrangements) and technical co-operation (in maintenance and overhaul) among the Arab Airlines.[105] In addition, there is the Arab

105. For more information on AACO, see "International Organizations", 42 ITA Bull. at 981 et seq. (10 Dec. 1979); "Manual on the Establishment of International Air Carrier Tariffs", ICAO Doc. 9364 at 35 (1983).

Civil Aviation Council which, as stated earlier, was founded in 1967 under the support of the League of Arab States.

Since then, progress has been made towards closer relations between aviation communities. In this regard, one should mention the formation in July 1978 of a technical consortium set up be ALIA (Jordan), Kuwait Airways (Kuwait), MEA (Lebanon) and Saudia (Saudi-Arabia). Such consortium, which started on a firm footing, aims at standardizing the specifications of aircraft acquisitions and sharing and distributing technical services, spare parts, maintenance and training.[106] Another major event was the creation in early 1981 of a joint reservation system for eight Arab airlines (Gulf Air, Kuwait Airways, Alia, Libyan Arab Airlines, Saudia, MEA, Syrian Arab Airlines and Sudan Airways).[107] This body, known as the Arab Electronic Booking Company, was formed to coordinate all passengers reservation activity by means of computer. Also training is another area of co-operation, and the Arab Air Academy exists to train personnel on how airlines can be run and to

106. See Nammack, "Arab Consortium Shows Advances", Air Transport World at 46 (July 1982); id. at 49 (Aug. 1983).

107. Bornemann, "Regional Co-operation", 31 ITA Bull. at 814 (Sept. 1981).

standardize pilot training courses.[108]

There are also other signs that really meaningful Arab co-operation might be coming in the near future. There is an important project for the creation of an Arab airline consortium to operate routes between the Middle East and the United States. The actual studies regarding the feasibility and commercial possibilities of such a consortium for the operation of transatlantic routes were carried out in the autumn of 1978 by a special committee consisting of representatives from a number of Arab Airlines. In June 1980, a decision in principle on the creation of that consortium was taken by the Chairmen of Gulf Air, Kuwait Airways, Alia, Saudia and MEA. The consortium, which would operate under the name of Pan Arab Airlines, intended to fly from Jeddah, Bahrain and Dubai to New York via Amman and Beirut. Also to be served in the United States were Houston, Chicago, Detroit and Los Angeles. According to Alia's Chairman Ghandour, an ardent and pragmatic advocate of regional co-operation in the Middle East, the consortium might extend a number of flights to South America and Japan within the first three years.[109] Negotiations are still underway to

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108. Feldman, op. cit., note 81, at 48.

109. See Bornemann, "Air Transport Organization and Policy", 16 ITA Bull at 166 (Feb. 1981); Ghandour, "Unilateralism Versus Multilateralism: A Dilemma for

form the joint airline. However, the recent established Arab Air Cargo, a joint venture of Iraqi Airways and Alia,[110] might pave the way for the birth of such a potentialy significant consortium.

There is no question regarding the meaningful role of regionalism among the Arab States although it is fraught with impediments of varying kinds and dimensions. For one thing, these countries belong to one region where the pace of economic development is not even. More importantly, political disagreements are still prevalent in the Middle East. It is true that political strife within any region when coupled with such fears as loss of identity make it difficult to predict success for integration.[111] In other words, the air travel market is sensitive to political and economic considerations and tends to shift accordingly.

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International Civil Air Transportation Today", in Wassenbergh and Fenema Eds., op. cit., note 15, at 57.

110. Arab Air Cargo was established in 1982 for the operation of international regular and irregular air freight flights in the Arab and foreign countries. For the Agreement which established this company, see ICAO C-WP/7746 at 11 (3/11/83).

111. The present political divisions between the Arabs may be related to the historical process of the gradual disintegration of the Ottoman Empire. See Longrigg, The Middle East, London at 195 (1963).

However, it is a fact that these countries have a mutual interest in the viability and stability of one another and the need for co-operation within the framework of their region becomes more pronounced in good and bad times alike. It is of interest, therefore, to note that the Council of the Arab League, a political body, has recently resolved that "Arab countries will not close their airspace in the face of Arab air carriers due to political reasons".[112]

In conclusion, there is a genuine interest in regional co-operation, but one cannot be oblivious to the inherent difficulties which retard such a development. Rivalries and jealousies raise their ugly heads, the rich States looking down upon the poor which is the result of

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112. Cited in Feldman, op. cit., note 81, at 49. For a most interesting view on the possibility of reconciling current Arab political disagreements, see Dr. Morad Ghaleb, former Foreign Minister of Egypt, "Resolving the Current Arab Crisis: Achievement of Three Major Objectives", in Al Ahram-International Edition at 12 (Mar. 6, 1985). In this Article, Dr. Ghaleb observed that:

> "No one Arab country can overcome the current crisis on its own...It would seem that the only avenue open for achievement of this end is the formation of regional groupings between the Arab neighbouring nations. An indispensable condition for the success of these efforts, however, is a closely knit coordination amongst such groups."

He then concluded: "This would be the most realistic approach in the first phase of a multitude Arab movement towards the achievement of a process of unity and development."

short-sightedness. In addition, different laws and regulations which obtain and lack of cultural and social hemogeneity of interests and values help to sustain the gap. On the other hand, one should also be optimistic, since the trend of regionalism in aviation has picked up momentum and is gaining more and more support. The fact is that the world is changing and changing fast. Every State is part of such change, which is the core of the current regulatory regime of international air transport. People have a tendency to say "let us be realistic"; and then everyone knows he is going to hear horror stories, reality has become unpleasant, and it seems that is the problem. But it is gratifying to note that, notwithstanding this "fear", the establishment of regional organizations is a promising development. Indeed, where world-wide multilateralism does not succeed, regionalism may have a better chance.

Regionalism in the Global Context

Most of the nations in our world cannot attain full self-satisfaction, particularly in the economic and commercial fields. It is a fact that isolated economies are not efficient for coping with the need of every nation. In addition, technical developments in industry and transport are making the economy of every State, even that of the

greatest and most nearly self-sufficient, ever more sensitive to what happens in other States. Therefore, regionalism may assist the modern State system function more satisfactorily, by carrying out a sort of co-ordination of activities between States.[113]

The difficulties arise, however, when one looks at the world wide picture of long-distance services, the trunk routes between different regions of the world, the wide differences in levels of economic, political, cultural, social development between the regions cannot be ignored. Whatever aviation policy or airline co-operation is built up within any particular region, the economic regulation of air transport services between different regions must take account of these differences. For example, a regime for air transport between North Atlantic States and Europe, or between Europe and the Arab region definitely cannot be applied uncritically to, for instance, air transport services between Africa and Asia or between Africa and Europe, or between North America and Latin America. In this respect, it should also be noted that even within each particular region great differences and unlikeness between

113. Schermers, International Institutional Law, Sijthoff Leiden at 2 (1972).

many States may exist,[114] which prevent a "regional project", both in respect of intra-regional air transport services and with respect to air services to/from other regions. The question could and perhaps should be asked, which "regional project" would result in the better international air transportation system, if all nations (for reasons of their own and depending on their circumstances) follow different regulatory philosophies.

To answer this question, any multilateral framework must consider the disparate aspirations and capabilities of a multitude of countries, and accordingly may have to devise methods to allow certain groups to participate more effectively. Towards this end, it might therefore be necessary to accord certain nations special privileges (i.e. certain "compensation"), similar to generalized preferences granted developing States in international trade.[115] Moreover, rather than seeking a universal framework at the outset, it may be more feasible to concentrate on the creation of regional groupings, either for the aim of exchanging rights among their members or for negotiating as a bloc with outside countries. In this regard, the writer wholeheart-

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114. For such differences, see Ghandour, "Growing Regionalism as a Result of Deregulation", 15 ITA Bull. at 356-357 (1980).

115. Salacuse, op. cit., note 55, at 843.

edly supports the precedent of "SAS", where a group of neighbouring countries elects to organize itself as a single unit for purposes of concluding aviation agreements with third States.[116] It is worth mentioning that regional bilateral negotiation has been actually tried and tested. It will be recalled that when the five countries of "ASEAN" (the Philippines, Malaysia, Thailand, Indonesia and Singapore) feared that "ICAP" (International Civil Aviation Policy of Australia) would result in a loss of substantial stopover tourist traffic between Europe and Australia they all agreed not to deal with Australia on a bilateral basis on the matters, but to band together and negotiate with Australia as one.[117]

It may well be, however, that many States, faced with capital and energy costs, as well as fuel shortages, may eventually join together to organize their air services as an internationally owned public utility, so as to achieve the most efficient use of available resources. In fact,

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116. See supra note 97; infra Chapter VIII, "The Possible Solution".

117. They actually obtained some concessions - not much, but better than what they would have obtained in individual bilateral negotiations. See Cruz, "American Aero-Imperialism: Issues and Alternatives", Speech delivered before the International Aviation Club at 5 (June 19, 1979).

while the large air powers would (of course) insist on maintaining their own national airlines on a traditional basis, smaller nations may find that banding together to form international operating companies is the most efficient and feasible way to participate in international aviation. This potential co-operation can be achieved by establishing a multi-national airline consortium of flag carriers of the region as a "chosen instrument" of the countries of the region for air transport services with the region and for air transport to/from the region.[118]

The relationship of air transport between large and smaller States, whether or not organized in regional blocs, will in many cases be decided by the "compensation" which the large air powers are willing to offer to the less-developed partner. Now nations can be classified as high income, middle income and low income countries, as industrialized, new industrializing and less developed States.[119] The question of "compensation" will arise in unequal situations and depend on the benefit air services offer to the less developed country and the possible adverse impact of foreign air services on the air services of the

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118. Cf. the present efforts to create "Pan Arab Airlines" between five major Arab carriers falls under this category.

119. Wassenbergh, op. cit., note 70, at 15.

national airline. Thus, compensation might be translated into money or airline co-operation. Such co-operation can be translated into assistance, transfer of expensive technology, pools or joint ventures. One thing should always be remembered: air transport is not an end in itself.[120] It is an economic activity which can yield profits or prestige, etc. To yield profits, an efficient regional co-operative effort is one key. Another thing which should also be remembered: regional unity can be strength but it can also be counter-productive. The purpose of solid regional and international co-operation should therefore be to better integrate into the world air transport system and not to become unduly parochial in outlook.

It is difficult, however, to say in what form airline co-operation will be permitted to continue in the future. Presumably outside factors - availability of fuel, cost and cash flow - will exert their influence and restraint. There are no simple solutions but there is hope that there will be intelligent choice and that reason will prevail. There is "nothing permanent except change" - Heraclitus said this some 2,500 years ago. Whatever the political decisions will provide as a framework within which

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120. Hammarskjold, "Recession Lessons and Gearing for Growth", IATA Review at 15 (July-Sept. 1984).

the air transport industry is to operate, people will still want to travel beyond the national, regional and inter-regional boundaries. Some form of limitation on sovereignty and some form of multilateralism will thus be needed.[121] People would still want to change their mind and change their airline.

Times are hard for world aviation, "the sun is setting and it will remain dark if States don't wake up!". As it is, States and airlines are becoming ever less lenient vis-à-vis each other. But one is still sanguine since "winds of change are rising. One form of change is inter-airline co-operation and more pronounced 'regionalism'".[122] It is apparent that the operation of international civil aviation will witness greater co-operation among international carriers in the years ahead. The challenge of international air law will be to find the rules and the structures to facilitate that regional co-operation and to enable all of mankind, in large nations and in small, to benefit from international aviation. In fact, the regional approach is eminently suited to eventually lead to a universal global regulatory regime for international civil

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121. Gazdik, "The Right to Fly: Review at Random", in Kean Ed., Essays in Air Law at 287 (1982).

122. Wassenbergh, op. cit., note 70 at 16.

aviation, adjusted to the various changing appearances. There is an old saying that "the proof of the pudding is in the eating". It could therefore be guaranteed that if a regional approach to the regulation of international air transport is pursued, the end product will not prove too indigestible for governments, airlines or the travelling public.

SECTION III - ICAO'S WORK AND THE REVIVAL OF MULTILATERALISM

ICAO's Involvement in Economic Issues Relating to International Air Transport

Whenever the history of ICAO is discussed, the technical matters of civil aviation always take a more prominent role than those of the economic nature. Certainly no one is opposed, for example, to air navigation safety; nor does anyone object to technological progress. The only difference of opinion about these technical aspects derives from a lack of funds in some of the lesser developed countries to install such systems as required under advanced technology standards.

By comparison, however, economic matters of air transport are frequently a question for polemics and much

debate amongst nations. Every government has its own economic concern which very often has close ties to its political philosophy.[123] Consequently, it is difficult to get a consensus of opinion amongst governments within ICAO.

For this reason, ICAO has, in the past, tended to be given a somewhat reduced role in the economic field of aviation. States have actually treated it more as "a clearing-house for economic and statistical information and used it for the preparation of specific studies on economic matters".[124] A survey of ICAO's role on this economic side, as will be seen in the pages which follow, reveals that its functions are chiefly limited to administrative and consultative tasks.

ICAO was established on April 4, 1947, as an outgrowth of the 1944 Chicago Convention - the cornerstone of legal regulation of international civil aviation for the past forty and so years.[125] By 1948, an agreement was

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123. For the interrelation between economics and politics in the contemporary system, see "International Economics and International Politics: A Framework for Analysis", 29 International Organization at 4-5 et seq. (1975).

124. FitzGerald, "ICAO Now and in the Coming Decades", in Matte Ed., op. cit., note 16, at 52.

125. A provisional organization, known as PICAO, functioned from mid-August 1945 until 4 April 1947, when the

concluded between the United Nations and the ICAO and, with reference to Articles 57 and 63 of the UN Charter, the Organization has become a specialized agency in the United Nations system. ICAO's main bodies are the Assembly, which is open to all member States, the thirty-three member Council and the Secretariat which is divided into five main divisions dealing with air navigation, air transport, technical assistance, legal matters and administrative services.[126]

The Assembly normally meets every three years to review the work of the Organization in the technical, economic and legal spheres and to debate general policy for the coming years. At the triennial sessions, the Assembly can adopt resolutions which although not legally binding upon member States, have an undeniable moral value. It can also deal "with any matter within the sphere of action of the Organization not specifically assigned to the Council".[127] During its first session in 1947, the ICAO Assembly established a Committee, titled the "Legal

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Convention entered into force.

126. On ICAO in general, see Buergenthal, Law-Making in the International Civil Aviation Organization, Syracuse University Press (1969).

127. Article 49(k) of the Chicago Convention.

Committee", charged with the work of the international codifiction of air law and adopted a constitution for that Committee.[128] At the same time, its predecessor, CITEJA (Comité International Technique d'Experts Juridiques Aériens) was dissolved.[129] The main goal of the Legal Committee is to study various problems of private international air law and draft relevant conventions to these matters. It also reports to the ICAO Council and Assembly, upon their request, on questions of public international air law in general, as well as on matters regarding the interpretation of the Chicago Convention.[130]

The ICAO Council, the governing body, has legislative, administrative and judicial functions. In exercising its legislative responsibility, the Council adopts international technical standards which become binding on ICAO

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128. Resolutions A1-46 and A1-48; the current constitution of the Committee is set forth in Resolutions A7-5 and A7-6.

129. See Draper, "Transition from CITEJA to the Legal Committee of ICAO", Am. J. Int'l L. at 155-157 (1948).

130. For a good review on the work of the Legal Committee, see FitzGerald, "The International Civil Aviation Organization and the Development of Conventions on International Air Law (1947-1978)", 3 Annals of Air and Space Law at 568 et seq. (1978); Rosenfield, op. cit., note 76, in Booklet No. 10.

members. Its administrative functions include appointment of the Secretary General and members of various committees and commissions. However, the most important task of the Council directly related to air transport is apparently its judicial powers with respect to the settlement of differences relating to the application or interpretation of the Chicago Convention and Annexes thereto.[131] It may also deal with bilateral air transport agreements which often provide that in the case of a dispute where the Parties fail to reach an agreement to appoint arbitrators, the Council's President may nominate or designate the arbitrators.[132]

The Council's powers for the settlement of international air transport disputes have rarely been invoked.[133] The failure to use arbitration is not due to a lack of disputes. States prefer, for political, economic

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131. See Articles 84-88 of the Chicago Convention.

132. See Larsen, "Arbitration in Bilateral Air Transport Agreements", Archiv Fur Luftrecht at 145 et seq. (1964).

133. The well known cases in which the Council has been called upon to settle disputes under the Chicago Conveniton, are the India-Pakistan case of 1952, the UK-Spain case of 1967-69 and the Pakistan-India case of 1971. The first case was settled by negotiation. The second one was adjourned sine die. The third case gave rise to the judgement of the ICJ which found that the Council had jurisdiction to entertain Pakistan's applications.

and other reasons, to solve their differences through diplomatic channels rather than arbitration. Although there are no authoritative statements in this respect, Bradley has correctly surmised the reasons:

> "Both Parties lose control of the dispute. There is a danger of an adverse decision which would financially have more adverse results than a compromise. Suspicion exists as to the impartiality of arbitral tribunals. It is better to cut one's losses by compromise rather than suffer the losses from unilateral restrictions during the period - not less than twelve months - that the matter is under arbitration. Perhaps the major reason is that the benefit of a favourable decision may be lost by the losing State giving twelve months notice of termination of the agreement."[134]

In addition, Milde, after analyzing the various provisions of the Chicago Convention, found that "it is doubtful whether a body such as the Council, composed of member States, is capable of performing a judicial function."[135] A permanent ICAO arbitral tribunal with compulsory jurisdiction would hence be an improvement over current methods. Such a body might develop a substantial body of law relating to the application of bilateral air transport

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134. See Bradley, "International Air Cargo Services: The Italy-U.S.A. Air Transport Agreement Arbitration", 12 McGill Law Journal at 312 (footnote 5) (1966).

135. Milde, op. cit., note 10, at 126 (1984).

agreements.[136]

In pursuance of Article 54(d) of the Chicago Convention, the ICAO Council has appointed an Air Transport Committee which is limited to representatives of members of the Council. This Committee is concerned with the economic aspects of international civil aviation, facilitation of air transport, problems of multiple taxation and insurance requirements, and compilation of statistical studies on various issues of air transport. Its economic interests include general development of air transport, airport financing, defining the role of charter services and tariffs. The facilitation legislation usually takes the form of standards and recommended practices which are adopted by the Council as annexes to the Chicago Convention. Finally, subsections (c) and (d) of Article 55 empower the Council to conduct research and undertake studies relating to all aspects of air transport.

This brief investigation shows that ICAO's involvement in the economic regulation of international air transport is limited. However, this situation was over-

136. Heere, "Some Observations Concerning the Desirability of Creating an International Court for Aeronautical Disputes", 1 Air Law at 229 (1976).

exaggerated by some major air powers[137] who took the view that "while ICAO and the Chicago Convention focus on safety and navigation, the actual arrangements governing scheduled services are established in a bilateral agreement between consenting governments". In addition, tariffs charged, capacity and frequency of service by airlines of each side, routes flown, the number of authorized airlines and issues such as customs exemptions and general business procedures are all matters covered by these agreements. Thus in their view, ICAO should have no role in these aspects, since it is only a political body responsible for safety and facilitation of civil aviation.[138]

To say that ICAO has no role in the economic regulation of international air transport is not correct. Authorization for the Organization to deal with the economic issues of civil aviation may, inter alia, be inferred from some provisions of the Chicago Convention. In addition to referring to the development of international civil aviation

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137. For example, the U.S., Australia, West Germany and The Netherlands. See Feldman, "ICAO Sidesteps Economic Role in 24th Triennial Assembly", Air Transport World at 18 (Nov. 1983).

138. Andrew's Statement, "International Aviation Policy", Calendar No. 348, 97th Congress, First Session Senate, Report No. 97-253, Department of Transportation and Related Agencies Appropriation Bill 1982, Appropriation Committee, 27th October 1981.

in a safe and orderly manner, the Preamble of the Convention also recited that the establishment of international air transport services "on basis of equality of opportunity" is an objective. The Preamble further provides that such services should be operated "soundly and economically". Article 44 of the Convention which is headed "objectives" (of the Organization) amongst other aims and functions enlists the following:

> (1) Meeting the needs of the peoples of the world for "a safe, regular, efficient and 'economical' air transport".[139]
>
> (2) Prevention of "economic waste caused by unreasonable competition".[140]
>
> (3) Insuring that the rights of the contracting States are fully respected and that every contracting State has "a fair opportunity to operate international airlines".[141]
>
> (4) Fostering the planning and development of international air transport so as to "avoid discrimination between contracting States".[142]

Article 44(i) of the Chicago Convention also authorizes the ICAO to "promote generally the development of 'all aspects' of international civil aeronautics". Article

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139. Article 44(d) of the Chicago Convention.

140. Id. Article 44(e).

141. Id. Article 44(f).

142. Id. Article 44(g).

55(a) of the Convention (probably to provide institutional backing to the regulation of some commercial matters of international aviation) provides that the ICAO Council may "where appropriate and as experience may show to be desirable, create 'subordinate air transport commissions' on a regional or other basis, and define groups of States or airlines with or through which it may deal to facilitate the carrying out of the aims of this Convention". With respect to "traffic and financial reporting", by Article 67, each contracting State has specifically undertaken that "its international airlines shall, in accordance with requirements laid down by the Council (of the ICAO), file with the Council traffic reports, cost statistics and financial statements showing among other things all receipts and sources thereof". Finally, Article 55(c) permits the Council to facilitate the exchange of information on air transport and navigation between the contracting States, and also to communicate to them the results of its own research.

Even though the above-mentioned provisions of the Chicago Convention do not constitute an exhaustive survey, they are sufficient to unequivocally confirm that ICAO is fully authorized to discuss the economic problems of international air transport and make recommendations about them. Indeed, over the past 40 years the Organization has deve-

loped an immense amount of expertise in a number of aspects of international civil aviation which are very closely linked with the economics of air transport. It also has a considerable influence through its organs to persuade the nations to abandon policies which are obnoxious to the wider interest of the international aviation community in favour of the adoption of alternative policies which can ensure the "sound and economic" operation of international aviation.

ICAO's 1977 and 1980 Air Transport Conferences

The International Civil Aviation Organization, the air arm of the United Nations, is no longer the "technical" agency it traditionally has been thought to be. The developing countries (as a majority voting bloc) are pushing the Organization onto economic turf formerly occupied only by IATA.[143] The fact that the process of decolonization has brought many new independent nations into ICAO. Particularly, these "developing" or the so-called "third world" countries had long been pushing for stronger participation by ICAO in economic issues of aviation.[144]

143. See infra Chapter VII, for more details on IATA's activities.

144. See Ellingsworth, "ICAO Parley Isolates Problems",

The first step in this drive, however, took place at the Twenty-First ICAO Assembly in 1974, when the membership passed Resolution "A21-25" entitled "Consideration of Air Transport Problems on a Worldwide Basis".[145] In this Resolution, the ICAO Council was urged to draw up a list of the major economic problems facing international civil aviation that were not already being dealt with through existing ICAO mechanisms on a global basis. The Council, after sending this list to all contracting States for their response, decided to convene a Special Air Transport Conference to be held in 1977.

This proposed Conference was nourished and supported by some scholars as a step towards a revival of multilateralism on the economic regulation of air transport. For example, one commentator felt that this conference "will offer a unique opportunity of making some real progress in developing a multilateral framework for international commercial aviation".[146] Another author hoped that "ICAO will not be deterred by the set backs of almost a generation ago to make a fresh attempt to seek such a multilateral agreement; for it may well turn out to be the legal instru-

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Aviation Week & Space Tech. at 32 (May 2, 1977).

145. Assembly Resolution A21-25, ICAO Doc. 9118 at 79.

146. Guldimann, op. cit., note 16, at 126.

ment required to bring the industry back to an even keel".[147] Whereas a third commentator encouraged the idea of holding such a meeting between contracting States as a device to formulate clear international uniform rules to the existing ambigious regulatory regime of air transport.[148] Meanwhile, ICAO heralded the event as the first major attempt since the 1944 Chicago Convention to review the international aviation system that has dramatically changed in three decades.[149]

It is notable that the United States, IATA and some other industrialized Western European countries opposed the convening of this Conference.[150] They insisted that ICAO should not become involved in airline economic aspects and stressed that the Organization should maintain its technical agency status. In contrast to this, many other nations, particularly the developing countries urged ICAO to broaden its mandate and find solutions, on a multilateral basis, to

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147. Cheng, op. cit., note 35, at 86.

148. Wassenbergh, "The Special Air Transport Conference of ICAO - April 1977", 42 J. Air L. & Com. at 508 et seq. (1976).

149. See Feldman, "Economics and Politics are New Concerns of ICAO", Air Transport World at 20 (Nov. 1977).

150. See Aviation Week & Space Tech. at 32 (May 2, 1977).

the most pressing economic problems. In their view, the majority of ICAO's work in technical areas has been accomplished and the Organization needs therefore "a new mission".

The Special Air Transport Conference was held in Montreal from April 13 to April 26, 1977.[151] It was widely attended. Ninety-seven contracting States of ICAO were represented; two non-contracting States attended as observers together with eleven international organizations. The Conference was invited to examine some of the emerging difficulties relating to tariff enforcement; policy concerning international charter air transport; regulation of capacity in international air transport services and the machinery for the establishment of international air transport fares and rates.[152]

In view of the periodic obstacles encountered in attempting to find a unique multilateral solution to various problems, the Conference formulated only recommendations on the type of regulation most conducive to the development of an economically stable and efficient international aviation system that could satisfy the varying needs of users

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151. Special Air Transport Conference (Montreal, 13-26 April 1977) Report at 1 (hereinafter cited as SATC (1977), ICAO Doc. 9199).

152. Id. at 1, 35; SATC-WP/1.

throughout the world. Twenty recommendations were, therefore, adopted by the 1977 Conference. Recommendations 1 and 2 deal with tariff enforcement. All member States should require carriers to file rates and fares with governments and once they are filed and approved "violation of such tariffs (should be) punishable by deterrent penalties".[153] These two recommendations thus strongly advocate strict tariff enforcement by States, and by IATA's compliance system as far as IATA member carriers are concerned. Not only illegal discounting by airlines is condemned, but also by passenger and freight agents, tour organizers and freight forwarders. The two recommendations also urge ICAO to undertake studies and collect information in the field of tariff enforcement.

Discussions at the Conference on the policy concerning international charter air transport led to the adoption of Recommendation 3, recommending that studies be undertaken to review the definition of scheduled and non-scheduled international air services, and to establish policies and guidelines pertaining to non-scheduled international operations.[154] The most crucial battle, however,

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153. Recommendation 1, SATC (1977), ICAO Doc. 9199, op. cit., note 151, at 6.

154. For more details, see infra Chapter V, Section V.

occurred over recommendations on capacity. A larger bloc of developing nations supported full predetermination of capacity in bilateral agreements, while the United States supported basic Bermuda agreement principles and was joined frequently by Norway and Sweden.[155] The Conference officially recommended (in Recommendation 4) that the ICAO Council undertake studies to establish criteria for regulating capacity on scheduled and charter services as well as develop a model clause (or clauses) that could be included by countries in bilateral pacts, primarily on the basis of predetermination of capacity.[156] For the first time, one sees here a preference of a majority of ICAO member States for the predetermination method of capacity determination. Finally, Recommendations 1 to 4, dealing with tariff enforcement, international charter air transport and the regulation of capacity, were approved by the Twenty-Second ICAO Assembly in 1977.[157]

In the field of international fares and rates, the 1977 Conference adopted no less than 15 recommendations. Many of these recommendations contained words directing

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155. See SATC (1977), ICAO Doc. 9199 at 14.

156. Recommendation 4 uses the term 'prior determination'. Id. at 16; infra Chapter VI, Section III.

157. Assembly Resolution A22-23, ICAO Doc. 9215 at 88.

members to take into consideration the views and needs of carriers which are not members of IATA when making airline economic policy decisions.[158] In other actions, the Conference recommended that the Council establish means for sending ICAO representatives as observers to IATA Traffic Conferences.[159] This Recommendation would subsequently be implemented pursuant to IATA's 1978 organizational restructuring.[160] The Conference also encouraged all member States to urge their scheduled and non-scheduled carriers to meet for coordinating their tariff policies.

It has been correctly remarked, by one commentator, that the 1977 Air Transport Conference produced evidence that the traditional international regulatory systems of civil aviation were being questioned.[161] However, one can still criticize the Conference for failing to deal with the issues of the exchange of traffic rights, co-operation between airlines and monetary problems.

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158. See, e.g., Recommendations 5, 7, 8, 13 and 17.

159. Recommendation 6, SATC (1977), ICAO Doc. 9199 at 23.

160. "The State of the Air Transport Industry", IATA Annual Report at 14 (1981); see also infra Chapter VII (footnote 64).

161. Naveau, Droit du Transport Aérien International at 139 (1980).

In Recommendation 20, the 1977 Conference decided that another special air transport conference should be held in three years, prior to the next regular session of the ICAO Assembly in September 1980. The Second Air Transport Conference met in Montreal from February 12 to February 28, 1980.[162] One hundred and one contracting States of ICAO were represented; one non-contracting State and nine international organizations attended as observers.

It is evident, in the words of ICAO Council President Kotaite, that radical changes in air transport have broadened ICAO's responsibilities from solving technical problems to include actual efforts toward harmonizing aviation economic policies and improving the machinery for establishment of fares and rates.[163]

The 1980 Conference should no longer be considered, as might have been the case with its predecessor meeting of 1977, as a special occasion; rather it was a stage in a long process.[164] New developments in international civil

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162. Second Air Tranpsort Conference (Montreal, 12-28 February 1980) Report at 1 (hereinafter cited as AT Conf/2, ICAO Doc. 9297).

163. Kotaite in his opening of the Second Air Transport Conference, ICAO Draft AT/Conf/2-Min. P/1 at 1 (15/2/1980).

164. Desmas, "The Second ICAO Air Transport Conference", 13

aviation since 1977 Conference were taken into consideration; frequent fuel price increases, deterioration of the world economic situation, liberalization of non-scheduled rules, implementation by the United States of its new aviation liberal policy, reorganization of IATA and a tendency towards reinforcement of regional bodies.[165]

The Second Air Transport Conference was indeed an interesting forum for discussion of the various differences between the United States and other nations around the world over international air transport economic policies. Once again, United States efforts to win other segments of the airline community over to its way of thinking were rebuffed, in some ways even more dramatically than during earlier confrontations.[166] The majority of the delegates attending the Conference seemed to be saying that the American policies of deregulation, "open skies" and increased competition might be "all right in the U.S., but not in the rest

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ITA Bull. at 305 et seq. (Aprial 7, 1980).

165. Id.; Wessberge, "Initial Proceedings of the Second ICAO Air Transport Conference", 11 ITA Bull. at 259 (March 17, 1980).

166. "ICAO Conference Rejects U.S. on Capacity Restriction Removal", Aviation Week & Space Tech. at 30 (Feb. 25, 1980).

of the world or in most international markets".[167] In short, strong support for a multilateral approach to international air transport problems was reported in the Conference, while the "unilateral approach" of the United States continued to receive widespread condemnation.

The subjects discussed in the 1980 Conference were along the lines highlighted by the 1977 Air Transport Conference. Regulation of international air transport services was the first item on the Agenda and it was subdivided into three categories: distinction between scheduled and non-scheduled air services; regulation of capacity in international air transport services; and regional multilateral air transport agreements. Agenda item 2 dealing with international air transport fares and rates was divided into five categories: mechanisms for establishment of scheduled passenger fares; mechanisms for establishment of non-scheduled passenger tariffs; mechanisms for establishment of scheduled and non-scheduled air freight rates; co-existence and harmonization of methods by which fares and rates are established; and tariff enforcement.[168] Each of these areas was addressed in detail resulting in

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167. Woolsey, "ICAO Transport Conference Shuns U.S. Airline Policies", Air Transport World at 20 (April 1980).

168. AT Conf/2, ICAO Doc. 9297 at 1, 63; AT Conf/2-WP/1.

five recommendations adopted by the Conference on the first Agenda item,[169] and twenty-six recommendations on the second Agenda item.[170]

The various recommendations that resulted had actually little to do with competition, "open skies", or unilateral ratemaking. Multilateralism was the foundation upon which most of the recommendations were based, and "the U.S. delegation of representatives from CAB, the State Department and the Department of Transportation" had very little impact on the way things went. To the contrary, it appeared that American pressures on IATA and other parts of the international airline community have had the effect of frightening nations, particularly the small ones, into adopting a more conservative appproach than they ordinarily might have.[171] The recommendations emanating from the Conference would thus establish an international regulatory mechanism far to the right of even IATA. It is interesting

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169. Id. at 7-24. Recommendation 1 was approved by the 23rd Assembly of 1980. See ICAO, Panel of Experts on Regulation of Air Transport Services, ATRP/5-Report at 3 (Para. 8) (July 1981). Recommendations 2, 4 and 5 were also approved by the Assembly. See Resolution A23-18, Provisional Edition at 49.

170. The 23rd Assembly approved the Recommendations 6 through 11 and 13 through 31, see Resolution A23-19.

171. See Air Transport World at 20 (April 1980).

to note here that some of the delegates said their efforts were spurred by the fear that the United States might have weakened IATA to the extent that ICAO or regional bodies will have to maintain the concepts of multilateralism.[172]

In fact, the 1980 Air Transport Conference demonstrated a broad consensus of opinion that the establishment of fares should involve the participation of the entire world civil aviation community and that reference should be made to IATA wherever possible.[173] In addition, a predetermination type of capacity clause was adopted by the Conference as the only method to be used, while the concept of free determination was firmly rejected.[174] In other words, the Conference strongly objected to any unilateral action by governments in general and to the United States deregulation policy in particular.[175] Thus, the 1980 Conference preferred that the difficulties faced by the system must be discussed and resolved through common

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172. Woolsey, op. cit., note 167, at 21.

173. See infra Chapter VII, Section V.

174. The methods for regulating capacity will be examined in more detail in Chapter VI.

175. Taneja, Airlines in Transition at 74, 79 (1981); infra Chapter VII, Section V.

approaches, taking into consideration the interests of all participants.

Even if the immediate sequels of the 1977 and 1980 Air Transport Conferences are rather modest, the idea of holding such meetings should not be abandoned. ICAO provides a unique forum, where developed and developing, western and socialist nations can discuss the various economic aspects relating to international civil aviation to reconcile conflicting and political views and the differing national interests at stake. In itself, of course, this may be extremely helpful and fruitful. Moreover, one would rather see the implementation of the Conferences' Recommendations in the long run.[176]

PRELIMINARY CONCLUSION

Due to basic disagreement over the nature of "multilateralism", the 1944 Chicago Conference relegated the task of economic regulation to bilateral air transport agreements, which in fact still constitute the prime tool for the formulation of international aviation law. Differences in philosophies, national policies and attitudes

176. See Azzie, "Second Special Air Transport Conference and Bilateral Air Transport Agreements", 5 Annals of Air and Space Law at 3 et seq. (1980).

complicate at present international co-operation in air transport and seem to jeopardize the attainment of consensus on desirable economic regulation. Yet the nature of international aviation does not make it feasible for any nation completely to renounce continued co-operation with other States in ensuring the necessary conditions for the operation of international air services. It can be therefore reasonably anticipated that the pressure of actual needs and requirements in international air transport, its global dimensions as an integrated system, will force States into seeking, identifying and expanding areas of consensus, rather than deepening differences and antagonism.

The continuing "multilogue" on aviation matters on a world-wide basis must be regarded as an essential means to develop and maintain a coherent international air transportation network. ICAO, after many years of concentration on technical and legal issues, has now focused on economic problems facing international aviation and will continue to provide such a suitable forum for discussion of long-term issues. It should, however, be noted that multilateralism encompassing all the nations of the world on the economic issues of international aviation is unlikely achievable in the near future. It is therefore the writer's view that multilateralism in the form of regional air transport agreements are the only practicable alternatives, and should

constitute the first step in a process that could lead to the long awaited global multilateral air transport agreement.

In fact, the wide variety of membership and therefore the diversity of interests within ICAO rule out unanimous action, but among the smaller, more homogeneous regional organizations of ICAO such as ACAC, AFCAC, ECAC and LACAC, a degree of consensus is achievable and effective inter-regional and external policy activity is feasible. Parallel trends, of course, can be seen commercially through regional co-operation between airlines. However, regionalism in aviation can only be fully successful if the States/Parties are willing to reconcile their sharp political contradictions. It is a fact that the absence of serious political disputes, combined with close cultural relations, common bonds of history and geographical proximity, would accelerate the realization of the desired enterprisory co-operation. Economic necessity alone, as experience demonstrated, will not be sufficient to secure agreement. Perhaps in this way, the world aviation community can begin the slow process of consolidation and consensus-building which will enable it to achieve at least a semblance of the universal regime sought forty-one years ago at Chicago.

Finally, it should also be kept in mind that

regional co-operation should then not be a defensive and parochial effort, but a way to better integrate into the global air services network of the future to arrive at a truly multilateral economic regulatory system for international air transport. States should therefore direct their efforts towards this potential goal. Failure to reach this objective means that the present conflicting regulatory regime will continue to remain. It will be wise hence to bear in mind: "If to do were as easy as to know what were good to do, chapels had been churches, and poor men's cottages princes' palaces" (Portia in the Merchant of Venice). Some consolation may be derived though from Kissinger's words (the former American Secretary of State): "Order once shattered can be restored only by the experience of chaos";[177] a seed of hope and progress belonging to the very essence of frustration.

177. Kissinger, World Restored, cited in Matte Ed., op. cit., note 16, at 114.

CHAPTER V

THE EVOLUTION OF THE MARKETPLACE

SECTION I - THE DEVELOPMENT OF INTERNATIONAL NON-SCHEDULED AIR TRANSPORT SERVICES

Prior to the Second World War, non-scheduled or charter operations were infrequent and economically unimportant. The main concern of States centred on the regulation of their respective scheduled air services which (at that time) constituted the major element of international aviation. Many governments, therefore, directed their policies towards the subsidization and promotion of such services. Charter air services, due to this lack of subsidy, operated at high cost which limited their use to certain sectors and individuals who could afford that (e.g. press agencies and newspapers etc.).[1] However, in some cases the charter flights were performed by scheduled airlines as a type of special service, e.g. for the transportation of large sums

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1. The U.K. Air Ministry, "Report of the Committee to Consider the Development of Civil Aviation in the United Kingdom", London at 9, 23 (1937).

of money or gold or for rescue expeditions.[2]

During the early years after World War II, the characteristics of the international marketplace did not change much and the importance of non-scheduled services was still limited. They were usually used as single flights and single person flights for humanitarian and emergency purposes, taxi class passengers and to places where no reasonably direct scheduled service was available.[3] The international aviation community devoted its efforts to the re-establishment and development of scheduled services in order to meet the needs of official and business travel. Charter services, therefore, were ad hoc operations, non-competitive in relation to scheduled services as well as being relatively expensive.

Over the years, however, non-scheduled air services began changing this character and emerged as an increasingly significant force in the international movement of passen-

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2. Sundberg, Air Charter: A Study in Legal Development, Stockholm at 11 (1961).

3. ICAO Doc. SATC Information Paper No. 2, "Policy Concerning International Non-Scheduled Air Transport" - Background Documentation for Agenda Item 2 of the SATC, Montreal, April 1977 at 1, 4 (Nov. 1976) (hereinafter cited as ICAO Background Documentation); Gazdik, "The Distinction Between Scheduled and Charter Transportation", Air Law, Vol. 1-2 at 66-67 (1975-77).

gers. While it is difficult to put an exact date on the commencement of the change, by the early fifties this development started in Western Europe[4] (first in the United Kingdom, then in Scandinavia and later in Western Germany) where travel agents organized a series of flights for carrying inclusive tour passengers to Mediterranean destinations. Such services rapidly expanded, and growing traffic flows with increasing frequencies developed between Northern Europe and Mediterranean destinations (Spain in the first place).[5] Later on European carriers extended their activities across the North Atlantic to North America[6] (under the affinity group concept) and have spread more slowly to other parts of the world.

In fact, non-scheduled traffic has been responsible for the revolution in air travel. It has expanded air

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4. ICAO Background Documentation, id. at 1; Guldimann, "The Distinction Between Scheduled and Non-Scheduled Air Services", 4 Annals of Air and Space Law at 139 (1979). However, other writers found the emergence of charters began immediately after the end of World War II in the U.S.A. and Europe. See Marx, "Non-Scheduled Air Services: A Survey of Regulations on the North Atlantic Routes", 6 Air Law at 133, 140 (1981).

5. Scoutt & Costello, "Charters, the New Mode: Setting a New Course for International Air Transportation", 39 J. Air L. & Com. at 17 (1973).

6. Rosenfield, "U.S. Liberal Bilaterals and Charter Traffic to Latin America", 7 Air Law at 158 (1982).

service from a means of transport for the wealthy to a means of mass transportation. It has also opened up both the travel and the tourist industries and it has had considerable economic and social ramifications for both developed and developing States.

Charter traffic has been a major element in air commerce since the mid-1960's.[7] By 1971 the international air charter reached its peak when the estimated international non-scheduled passenger traffic share (which constituted the major part of all non-scheduled traffic) accounted one-third (to be exact 32.2%) of total international passenger traffic.[8] Of this non-scheduled traffic, 57% was carried by non-scheduled operators and 43% by scheduled carriers. However, by 1974 non-scheduled traffic had declined to 27.2% of all international traffic.[9] Of this

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7. Gazdik, "Co-existence of Scheduled and Charter Services in Public Air Transport", The Aeronautical Journal, Vol. 77, No. 745 at 36 (Jan. 1973); ICAO Background Documentation, op. cit., note 3, at 1.

8. ICAO Secretariat, "A Review of the Economic Situation of Air Transport, 1969-1979", ICAO Circ. 158-AT/57 at 22 (1980). As expressed in million passenger-kms, the total world performed this year was 255.0. From this total, 82.0 million passenger-kms or 32.2% were performed on non-scheduled services. As to the North Atlantic region, charter traffic (in 1971) accounted 30.8% of all North Atlantic traffic.

9. ICAO Secretariat, "Review of the Air Transport

charter traffic, 63% was carried by non-scheduled operators. Of these 63%, 43% of the operators were licensed in Europe, 18% in North America and 2% elsewhere.[10] The remaining 37% of the charter traffic was carried by the scheduled airlines. It is worth noting here that the largest single international charter market in 1974 was between the member States of the European Civil Aviation Conference (ECAC). In that year, intra-ECAC charter traffic totalled 19.7 million passengers or about 41% of all intra-ECAC air passengers (in terms of passenger-kilometers, charter traffic represented 57.5% of the total). The second largest market was the North Atlantic with 3.4 million passengers, representing 26.4% of all North Atlantic traffic.[11] The charter market has thus become a substantial part of commercial international traffic.

Although international non-scheduled passenger traffic's growing rate fluctuated considerably over the years since 1975, its percentage share of total international passenger traffic kept declining to 22.5%, 19.8% and 18%

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Situation - Past, Present and Future", ICAO Bull. at 20 (Oct. 1977).

10. ICAO Circ. 136-AT/42 at 1 (Nov. 1976).

11. ICAO Background Documentation, op. cit., note 3, at 2.

in 1978, 1979 and 1980 respectively.[12] According to statistics in 1981, 494,400 million passenger-kilometers were performed on scheduled international traffic, while 98,700 million passenger-kilometers on non-scheduled international traffic.[13] Charter air services thus represented 16.6% of all international traffic, down from 32.2% ten years ago (in 1971). This trend can be attributed to the narrowing price differential between scheduled and non-scheduled service due to the fact that many new promotional excursion fare structures were introduced on scheduled air services. In spite of these results, the largest charter market in 1981 was still amongst the twenty-two States belonging to ECAC. In the 12 months ending October 1981, intra-ECAC charter traffic accounted 27 million passengers or about 41% of all intra-European air traffic, whereas in the same year the charter share of North Atlantic air

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12. See, e.g., "Estimated International Non-Scheduled Revenue-Passenger Air Traffic, 1978-1982", ICAO Bull. at 31 (July 1983). On the North Atlantic, charter traffic dropped to 2.03 million passengers in 1980, constituting only 10.8% of the total market. However, intra-ECAC charter traffic totalled 27.3 million passengers or about 42% of all intra-ECAC passengers. See "1982 Non-Scheduled Passenger Traffic Declined Again", ICAO Bull. at 32 (July-Aug. 1982).

13. ICAO Bull. at 31 (July 1983).

traffic was only 9%.[14]

It seems recently, however, that charter operations have begun to rise again, reversing the trend of the pasc decade. By the end of 1982, e.g., the proportion of international traffic carried on non-scheduled services (including those operated by scheduled carriers) increased for the first time in eleven years to about 18.3%.[15] Of this charter traffic, 61% was carried by specialized non-scheduled operators and 39% by scheduled carriers. As to intra-ECAC traffic, charter traffic rose by about 5%

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14. Id.; IATA Annual Report of 1982 at 14, 20; World Airline Co-operation Review, (IATA Publication) at 3 (Apr.-Jun. 1983); Aviation Daily at 159 (Sept. 29, 1982).

15. Of course, it is still much lower than the level of 32% reached eleven years ago in 1971. See, in general, "Charter Traffic Had Sizable Growth Last Year", ICAO Bull. at 31 (July 1983); Aviation Week & Space Tech. at 35 (Mar. 7, 1983). By the end of 1983, total charter passenger traffic increased by almost 2%. In terms of passenger kilometers, charter traffic remained at about 18% of all international traffic. As to intra ECAC charter traffic, there were indications that this traffic rose by about 2% whereas charter traffic on the North Atlantic increased by 5.7% compared to 1981. See "International Non-Scheduled Passenger Traffic Slightly Higher in 1983", ICAO Bull. at 23 (July 1984). Finally, according to preliminary statistics recently published by ICAO, total non-scheduled passenger-Kms performed throughout the world increased by an estimated 6% in 1984. See "Performance by Charter Operators Improved in 1984", ICAO Bull. at 29 (July 1985).

compared to 1981.[16] On the North Atlantic, however, non-scheduled traffic increased by almost 25%; the last increase having occurred in 1977. This high increase in charter rate on the North Atlantic can be attributed in part to the strength of the American dollar which increased United States travel to Europe to take advantage of a cheaper European vacation.[17]

In general, the most significant factor contributing to expanding and developing the importance of international non-scheduled air services has been the change in demand within the international market.[18] In Europe and the North Atlantic (the two major markets where most of this development occurred) the pattern was the same; charter services met a demand that was not met by existing scheduled services. The increase in disposable income has led to the growth of the market for personal travel, as opposed to

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16. Intra-ECAC charter traffic totalled 3.3 million passengers or about 46% of all intra-ECAC passengers. See ICAO Bull. (July 1984) at 23; supra note 14.

17. Kozicharow, "Charter Revival Forces Fare Revisions", Aviation Week & Space Tech. at 35 (Mar. 7, 1983); supra note 13, at 30.

18. Wassenbergh, Public International Air Transportation Law in a New Era, Deventer at 51 et seq. (1976); ICAO Background Documentation, op. cit., note 4, at 1 et seq.; Scoutt & Costello, op. cit., note 5, at 15.

business travel upon which scheduled services chiefly relied. For a large proportion of such travellers, the most important consideration was now the price of air transportation.[19] The fact that the scheduled carriers maintain year-round regular services, allowing flexibility in a traveller's plans, operate during off-season periods with rather low load factors and have to shoulder high personnel costs, kept their tariffs relatively high. This situation enabled charter operators to offer air transportation at substantially lower fares[20] to the extent that the word 'charter' became synonymous with cheap fares. Furthermore, charter transportation has been instrumental in the development of international mass tourism which has assumed considerable economic and social importance for a large number of developed and developing countries.[21] Since these transformations, the leisure traveller (especially the

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19. Masefield, "The Air Charter Challenge", Flight International at 549 (Apr. 5, 1973).

20. Detière, "Competition Between Scheduled and Charter Services", ITA Bull. at 247 et seq. (Mar. 19, 1973); id.

21. International Symposium on "Air Charter Transport and Its Impact Upon Tourism", held at Taormina from 19 to 21 Nov. 1976, Milano at 111 (1977) (hereinafter cited as Symposium on Air Charter). For a summary of this Symposium. See 2 Air Law at 183 et seq. (1977).

tourist) has increasingly become the dominant user of passenger air transport, with less emphasis on such scheduled service characteristics as frequency, flexibility and on-demand availability.

There is one problem of terminology that would be clarified here; it is the use of the terms "non-scheduled" and "charter". It seems that the difference between the two terms is mainly of a political nature, since it has been contended that "non-scheduled" is a public law term, while "charter" is a private law term pertaining to the contract between an air carrier and a charterer.[22] However, it is apparent that they are not identical to each other, as non-scheduled air transport services include all services which are not scheduled in nature, including air taxi, humanitarian and emergency operations, private flights and, of course, charter services. Undoubtedly, charter services compose the main part of non-scheduled services. This is the reason why the terms "non-scheduled" and "charter" have come to be used interchangeably in colloquial language, because the policymakers are mostly concerned with flights

22. ICAO Background Documentation, op. cit., note 3, at 16; Assum, International Air Charter Transportation: Its Legal Regulations and Implications, unpublished thesis, McGill University at 3 (1975). However, since 1955, the term "supplemental" carrier was used in the U.S. See Sundberg, op. cit., note 1, at 124.

performed for compensation and, of course, the essence of charter is the payment by the charterer for the use of the aircraft or part of it.

For the purpose of this work, the terms "non-scheduled", "charter", "supplemental" and "irregular" services are used synonymously, specifically meaning international non-scheduled commercial air transport services.

SECTION II - THE REGULATORY FRAMEWORK OF INTERNATIONAL AIR CHARTER TRANSPORT

Since the mid-1960's, non-scheduled transportation grew to represent a significant proportion of total traffic. In so doing, it had substantial effects on the industry of aviation as a whole. In an environment where there was little basic change in the nature of scheduled air service regulation, air charter policy provided, from this time on, a sensitive barometer of international policy evolution.

Charter operations became not merely a measure of change to the marketplace but helped to promote that change, i.e. by virtue of their independence from scheduled operations, they introduced new components in a dynamic system, both operationally and at policy level, most importantly, although "outside the system, their presence impacted on

entry, designation, capacity and pricing".[23]

Due to the increasing importance of charters, each State felt the need to regulate and provide for them. As is well known, the provisions of Article 5 of the Chicago Convention allowed international non-scheduled air services to be operated without formal bilateral agreements.[24] In addition, due to the lack of a uniformly accepted definition of what "non-scheduled services" are, each State has been relatively free to determine the scope of the second paragraph of Article 5 and its regulations under this provision. For this reason, paragraph 2 of Article 5 has almost become inoperative[25] and hence the governments remained free to impose unilateral restrictions concerning air charters.

It is thus interesting to note that over a period of some 40 years only (since Chicago 1944) regulations have been promulgated to restrict the operations of air charters, have then been modified to attenuate the restrictions imposed, and finally tend today to give charter transporta-

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23. Hammarskjold, "Trends in International Aviation and Governmental Policies", Aeronautical Journal at 144 (May 1980).

24. For the interpretation of Article 5, see infra Section V of this Chapter.

25. Haanappel, Pricing and Capacity Determination in International Air Transport, Kluwer at 15 (1984).

tion the rights traditionally granted to scheduled services. The trends and reversals in charter policy are particularly clear when one considers international regulations in Europe and in the United States, and particularly over the North Atlantic.

Regulations in Europe

As seen above, the legal regime for charters established by the Chicago Convention has left the contracting States free to apply the conditions and limitations they deemed necessary. Apart from a few exceptions like Belgium, which totally prohibited charters, it can be said that the European attitude towards charters was liberal.

When ECAC was established in 1954, "(t)here was... general agreement that non-scheduled commercial air services should be allowed freedom of operation within Europe without prior permission from governments if such services did not compete with established scheduled services".[26] Thus, as long as charters were not competing with scheduled services, they were to be allowed without prior governmental approval. Nevertheless, the States were left free to determine which

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26. ICAO Recommendation No. 5 of the Conference on Coordination of Air Transport in Europe, ICAO Doc. 7575-CATE/1 at 11 (1954).

operations would threaten scheduled air services.

In 1956, ECAC members adopted a "Multilateral Agreement on Commercial Rights of Non-Scheduled Air Services in Europe", or the so-called "Paris Agreement".[27] The purpose of the Agreement was to harmonize the policy of the contracting Parties, insofar as charter air transport was concerned, by abolishing certain restrictions and liberating air traffic. In practice, however, the Paris Agreement permitted prior governmental approval for non-scheduled services except in certain narrowly defined circumstances.[28] It was more "a formal commitment to promote limited charter travel than an effective change in the existing regulatory system".[29]

The scope of the 1956 Paris Agreement is very limited. The criterion used to determine the freedom of

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27. For the text of the Agreement (which was signed at Paris on Apr. 30, 1956), see ICAO Doc. 7695 (1956) 310 UNTS 229; Matte, Treatise on Air-Aeronautical Law, Carswell at 683 et seq. (1981).

28. Prior approval is not required if the services: carry six or fewer passengers on an occasional basis; air humanitarian or emergency in nature; are not operated more than once a month between a pair of points; or are between regions without a "reasonably direct connection" by scheduled services (Article 2).

29. Kamp, Air Charter Regulation - A Legal, Economic and Consumer Study, New York at 49 (1976).

charter air transport is the extent to which this freedom would harm the scheduled air services. Large-scale passenger non-scheduled traffic is only liberalized "between regions which have no reasonably direct connection by scheduled air services".[30] In sum, the Agreement does not affect the vast majority of charter flights within Europe and is totally inapplicable to charter flights serving points outside Europe, since it is only a regional arrangement. Psychologically speaking, however, this Agreement proved to be significant in that it has shown that it is possible to tackle on a multilateral basis even the commercial aspects of civil aviation.[31]

One of the most important effects of the Paris Agreement has been a considerable rise in Inclusive Tour

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30. Article 2 of the 1956 Paris Agreement.

31. Johnson, "Rights in Air Space", in Vlasic and Bradley Eds., The Public International Law of Air Transport, McGill University at 71 (1974). In this regard, one should remember that in March 13, 1971, five States members of the Association of South East Asian Nations (ASEAN-Group) concluded the "Multilateral Agreement on Commercial Rights of Non-Scheduled Air Services Among the Association of South-East Asian Nations" at Manila. In brief, its terms are phrased in a similar way to the Paris Agreement; however, the clause favouring passenger transport between regions lacking reasonable access to scheduled services is not contained in this Agreement (Article 2 of the Manila Agreement).

Charter (ITC) traffic within Europe.[32] Since this type of charter was usually performed on routes which were not served by scheduled services, and by its nature did not draw passengers away from scheduled carriers, such traffic has been included within the scope of the Agreement and has, therefore, been subject to a rather liberal regime. The growing importance of ITCs on intra-European routes was difficult to ignore, and in 1961 ECAC recommended that its members "should continue to adopt a liberal attitude toward flights exclusively reserved for inclusive tours".[33] In this regard, one has to remember that although the text of the Paris Agreement contains only a modest liberalization of the types of non-scheduled traffic, subsequent ECAC recommendations and national policies proved very favourable to the large-scale development of ITCs.[34]

Inclusive Tour Charters began developing in the early 1950's first in the United Kingdom, then in the other European countries, and they became the dominant form of

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32. Driscoll, "The Role of Charter Transport in International Aviation", Air Law, Vol. 1, No. 2 at 76 (1976).

33. Recommendation No. 6 of the Fourth Session of ECAC, Doc. 8185, ECAC/4-6 (July 1961).

34. See Marx, op. cit., note 4, at 142; Haanappel, op. cit., note 25, at 127.

charter travel. The main feature of such type of charter traffic is that the charter participant must purchase a package deal, including both round trip air travel and ground arrangements, such as hotel accommodation, car rental, excursions, etc. Over the years, ECAC recommendations have to a large degree been successful in harmonizing the ITCs regulations and rules amongst the different European States. However, while this type was very successful within the Europe-Mediterranean region, its significance was limited between Europe and North America, mainly due to restrictions placed on them by States in both regions.

The major developments in non-scheduled transportation started in Europe at the end of the 1960's and beginning of the 1970's.[35] At that time, scheduled carriers were switching to wide body aircraft, and their old equipment was for sale. In addition, the income of the European population had attained an optimum since the war and holidays were being extended. To meet these changes, the United Kingdom introduced the Advance Booking Charter (ABC) and was followed by the other European countries. The main characteristics of ABCs can be summed as follows:[36]

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35. See, e.g., Scoutt & Costello, op. cit., note 5, at 17 et seq.; Marx, op. cit., note 4, at 142.

36. See, in general, Lowenfeld & Mendelsohn, "Economics,

(a) The full capacity of the aircraft is chartered by one or more charter organizers.

(b) The charterer(s) put(s) together (a) group (s) of charter participants.

(c) The charter participants must book and pay their (round trip) flights in advance of departure.

(d) A prescribed minimum duration of the journey from departure on the outward portion to arrival on the inward portion.

In general, the advance and payment periods vary between one and three months. However, such periods over the years showed a tendency to be shortened. Usually there is a system of non-refundable deposits made by charter participants. Finally, ECAC has also been successful in harmonizing its member States' regulations and rules pertaining to ABCs.

Regulations in the United States

Prior to the mid-1950's, there was no real need to develop regulations applicable to international non-scheduled operations since most passengers were travelling on business using scheduled air services. However, by 1955

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Politics and Law: Recent Development in the World of International Air Charters", 44 J. Air L. & Com. at 484 et seq. (1979); ECAC/INT.5/12 Report (1981); Matte, op. cit., note 27, at 153 (footnote 105).

the CAB expressed its desire to liberalize charter operations in its "Large Irregular Air Carrier Investigation".[37] The trend to liberalize charter rules continued during the following years, as the CAB refined its policy and its requirements. In 1959, as a consequence of a court ruling (in American Airlines v. CAB)[38] limiting the use of exemptions for supplemental carriers, the CAB decided to issue certificates of convenience and necessity instead of granting exemptions; in substance, however, the regime remained the same.

Part 207 of the CAB Economic Regulations had limited non-scheduled carriers to the transport of bona fide groups engaging the entire capacity of the aircraft; this in fact established the "Affinity" rule. This limitation, however, raised some problems in the enforcement of the rules, as clubs were formed for the simple purpose of creating a 'prior affinity' for the travellers to enable

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37. The decision of CAB after this investigation was to encourage the survival and growth of supplemental or irregular carriers. See CAB, Docket No. 5132, quoted in Goldklang, "Transatlantic Charter Policy - A Study in Airline Regulation", 28 J. Air L. & Com. at 109 et seq. (1962); see also Taneja, Airlines in Transition, Toronto at 50 (1981).

38. American Airlines, Inc. vs. CAB, 235 F. 2d 845 (D.C. Cir. 1956).

them to take advantage of the low fares offered.[39] Paradoxically, the rules governing Affinity Group Charters were largely based upon those established by IATA, the world Association representing the scheduled carriers. They were developed in the form of IATA Traffic Conference Resolution 045 (Passenger Charters)[40] in an effort to protect scheduled air services. The real significance of this Resolution lies in the fact that many of its provisions have been incorporated into the various national regulations and hence also applied to charters performed by non-IATA airlines.

IATA Resolution 045, which has been revised on several occasions, stipulates that charter contracts shall be with one charterer, who (in the case of affinity charters) may sell space on the chartered aircraft to a group which has "principal purposes, aims and objectives other than travel and sufficient affinity existing prior to the application for charter transportation to distinguish it and set it apart from the general public", subject to

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39. For more details, see Goldklang, op. cit., note 37, at 125-127; Marx, op. cit., note 4, at 135-136.

40. A Traffic Conference Meeting was convened at Bermuda in November 1948, where certain proposals relating to charters were adopted to be issued as Resolution 045 on April 7, 1949. See Sundberg, op. cit., note 2, at 102; Goldklang, op. cit., note 37, at 105 et seq.

numerous detailed conditions and restrictions.[41] In fact, Resolution 045 severely limited the scope of charter operations, mainly due to the plane-load concept and the no-resale of seats rule.[42] As the years went by, this Resolution became even more arbitrary and complex, proving the theory of one legal scholar that "law is the only profession which records its mistakes carefully, exactly as they occurred, and yet does not identify them as mistakes".[43]

The "prior affinity" rules had been enacted in the United States for the exclusive protection of scheduled services, but the development of aviation required a revision of the existing concepts. From the beginning of the 1960's, the CAB started to adopt a more liberal international policy toward charters,[44] resulting, inter alia, in a

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41. ICAO Background Documentation, op. cit., note 3, at 9-10; Haanappel, op. cit., note 25, at 128-129.

42. See Paragraphs 1, 4 and 9 of IATA Resolution No. 045.

43. Elliot Smith, "Conference on Teaching of Law in Liberal Arts Curriculum", 39 J. Am. Judicature Soc'y at 47 (Nov. 1954).

44. Keyes, "The Transatlantic Charter Policy of the United States", 39 J. Air L. & Com. at 219 et seq. (1973).

permission for "Split Charters" in 1964.[45] Authority to conduct a Split Charter involved the right for more than one chartering entity to share or split the whole capacity of a chartered aircraft, as opposed to the concept of a plane-load charter. This type of charter was made necessary as a result of the significant increases in airplanes capacity when jet aircraft were used by the chartering industry. However, it has to be remembered that these charters were still affinity groups (i.e. members of a club, society, university, etc.) but the decision "marked the beginning of heightened competition between supplemental and scheduled carriers for tourist travel over the North Atlantic".[46]

A major breakthrough in charter transportation occurred in 1966 and 1968,[47] with the CAB's authorization

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45. CAB, Transatlantic Charter Investigation, 40 CAB 233 (1964).

46. Lowenfeld & Mendelsohn, op. cit., note 36, at 481.

47. It should be noted that the U.S. courts upheld the validity of ITCs for domestic transportation in 1966 (American Airlines, Inc. v. CAB, USCA, 9 Avi. 18.230, D.C. Circ., July 19, 1966), but rejected them for foreign traffic. In disapproving ITCs for foreign transportation, the Court of Appeals found that the CAB had exceeded its authority in blurring the distinction between individually ticketed and bulk transportation (Pan American World Airways v. CAB, USCA, 2nd Circ. July 20, 1967, 10 Avi. 17.399). Finally, the Congress adopted an amendment to the FAA and authorized foreign ITCs in Sept. 1968.

of Inclusive Tour Charters (ITCs). The development of ITCs in the United States thus began much later than in Europe, and never became a significant factor on the American air travel scene. The main reason for that was the fact that the CAB put numerous restrictions on the performance of ITCs. Amongst other things, a three overnight stop requirement prevented the growth of European-type point to point ITCs. Over the years, however, the American policy towards charters was becoming more and more liberal, but the 'affinity' concept was still too harsh for the non-scheduled carriers. In an attempt to eliminate this requirement of 'prior affinity', the CAB adopted the so-called Travel Group Charters (TGCs). This new type did not require any affinity between the travellers, but the regulations still required, inter alia, an advance booking period of 90 days, a minimum group of 40 people, a minimum stay of 7 days, pro-rata pricing and bonding by the organizers, to protect the public against defaults. The TGC was accepted by the American courts,[48] but "perhaps because of its complexities...(it was) very nearly a still-birth".[49] The 'alphabet game' went on with two other experiments by the CAB, the One-Stop

48. See Saturn Airways, Inc. v. CAB, 483 F. 2d 1284 (D.C. Circ. 1973).

49. Lowenfeld & Mendelsohn, op. cit., note 36, at 482.

Inclusive Tour Charters (OTCs) and the ABCs. The OTCs were very similar to ITCs, but they only required one stop instead of the three needed for ITCs.[50] As to the ABC concept, the CAB approved this type of charter with the view of eventually replacing both Affinity Group Charters and TGCs.[51]

It seems that the Affinity Group Charters, the predominant type of charters on the North Atlantic for almost 20 years (1953 to 1972) are now far less common than in the past. It was evident that the volume of traffic moving on pro-rata affinity charter flights had made it virtually impossible to enforce the regulations in a number of States. It was also widely recognized that the affinity concept was inherently discriminatory against those who did not belong to organizations with enough members to qualify as charterworthy. For these reasons, the United States CAB withheld approval of IATA Resolution 045 in June 1972, thus making its provisions inapplicable to, inter alia, the key

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50. 40 Fed. Reg. 34, 089 (1975), former 14 C.f.R. Part 378.A. The OTC was also upheld in courts, see Trans World Airlines v. CAB, 545 F. 2d 771 (2d Circ. 1976).

51. 41 Fed. Reg. 37.763 (1976), former 14 C.F.R. Part 371. See infra for more details.

North Atlantic charter market.[52] The CAB, in its disapproval of the Resolution, found that it impeded carriers from meeting the increasing demand for low cost mass air transportation and was, therefore, inconsistent "with the development of a sound overall air transportation system".[53] At the same time, the United States, Canada and ECAC member States took measures intended eventually to phase out affinity groups and to replace them with non-affinity groups as the main form of charter on the North Atlantic. These measures then took the form of a Declaration of Agreed Principles for North Atlantic Charter Flights or the so-called "Ottawa Declaration of 1972".[54] In pursuance of this Declaration, Canada, the United States and a number of ECAC member States introduced non-affinity group charters on the North Atlantic in 1973. This new category of non-scheduled operations, termed (as was shown) ABCs by Canada and several ECAC member States and TGCs by the United States, was originally intended to replace affinity charters on the North Atlantic completely by the end of 1973.

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52. Of course, the Resolution is still valid in some areas, but no longer in key markets such as Europe and North Atlantic.

53. CAB Order 72-6-91 (Jun. 21, 1972).

54. Signed at Ottawa in October 1972 by Canada, U.S.A. and ECAC member States, 68 Dept. St. Bull. 20 (1973).

However, only Canada adhered to this date.

The phasing out of the Affinity Group Charters started earlier in Europe than in the United States. After 1973, European origin "prior affinity" charters dropped sharply in number and ECAC urged its member States to terminate all of them by the end of 1975.[55] In the United States, however, the situation was not the same. Although they actually intended to do so, the Americans could not immediately eliminate "prior affinity" groups on the North Atlantic. The reason lies in the fact that, whereas ABC proved to be successful and very popular to the general public in Europe, the American TGC never became widely accepted. The varying degree of success encountered by the two types of non-affinity charters may be partly attributed to detailed differences in regulations. Whereas the ABC cost is a fixed price set by the charter organizer, the final TGC price was to be pro-rated among the number of participants on departure. Unlike the TGC, the ABC is not subject to cancellation if there are insufficient passengers prior to departure. In other words, under the ABC rules it is the operator who bears the risk of insufficient demand

55. ECAC was further instrumental in harmonizing the ABC rules of different European countries. See ICAO Doc. 9044, ECAC/INT.S/5 (SP) (Nov. 1972); ECAC/ECO-11/7 (Apr. 1974).

and passenger cancellation, while according to TGC rules it was the passenger, who bears the risk.[56] Furthermore, the ABC retailer may withhold his commission at the time of sale, while the TGC retailer was only compensated after the flight. Due to these rules, the marketing of the American TGC was extremely restrictive and difficult. In 1976, the United States CAB, therefore, adopted the European-type ABC (for an experimental period of 5 years) which would enable the organizers to market this type at a fixed price. This type of charter was introduced by the CAB, with even more liberal rules than those applicable in Europe, to eventually replace TGC and Affinity Group Charter. Coming to a major decision in 1978, the CAB announced that it intended to do away "with the entire alphabet game of ABCs, OTCs, TGCs and even affinity charters and substitute for all these a single Public Charter".[57]

For the purpose of this work, a special emphasis is

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56. For instance, if the TGC organizer was only able to fill up 90% of the chartered aircraft or part thereof, the passengers would have to pay for the unoccupied 10% of the seats. Although the CAB relaxed its rules toward TGC in 1973 and 1974, the system remained basically the same. See CAB, "Notice of Proposed Rule Making", SPDR-35, 39 Federal Register at 10915-17 (Mar. 1974); TGC Regulations, 39 Federal Register at 29345-50 (Aug. 1974).

57. 14 C.F.R. Part 380 (1979). The Final Rule was adopted 14 Aug., effective 15 Aug. 1978.

given to the concept of "Public Charter", since it is considered the most liberal type ever introduced in the field of charters. As of January 1, 1979, "old-rule charters"[58] were revoked and Part 380 of the Federal Regulations legislated the "Public Charters". The CAB's feeling of urgency was such that an "emergency blanket waiver" was granted to "all U.S. and foreign direct and indirect air carriers authorized to operate passenger charters".[59] Member O'Melia (as sole dissenter to this waiver decision) described it as a "cavalry charge gesture";[60] it remained in effect until the formal "Public Charter" decision replaced it in broadly similar, but permanent terms.

Part 380 of the Federal Regulations defines "Public Charter" as a "one-way or round-trip charter to be performed by one or more direct air carriers, which is arranged and sponsored by a charter operator and which meets the require-

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58. It should be noted that charters conducted by educational institutions and charters for special events were retained, but subjected, to a large extent, to the new Public Charter rules. See 14 C.F.R. Part 380.17, Part 380.18.

59. The waiver (from charter restrictive rules) was granted for a temporary 90-day period beginning 19 April 1978. See CAB Order 78-4-122.

60. CAB Order 78-4-122 at 6.

ments set forth in sub-part B of this Part". The main characteristics of this new liberal charter type may be summed up as follows:

(a) There can be intermingling of passengers of different charter types.[61]

(b) There are no advance booking and payment requirements with respect to passengers participating in the charter.

(c) No requirements for ground accommodation or length of stay rules.

(d) The departing flight and returning flight of a round-trip charter need not be performed by the same direct carrier.

(e) The sale of one-way charter, (the first time that anything but round-trip sales had been permitted).

(f) Selective price discounts and a variety of other increases in flexibility.

A minimum contract size of 20 seats (between direct air carriers and charter operators) is however retained, ostensibly continuing the distinction between scheduled flights and "Public Charters". In addition, it seems that the second important feature to keep this distinction, is the use of an intermediary (the charter operator) between the

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61. Although the passengers must be exclusively charter participants, other persons (e.g. operator's parents, employers, officers, etc.) are allowed to participate, on a free or reduced basis.

air carrier and the passenger. However, it should be realized that even this difference has been watered down. Since September 1979, the CAB has allowed Public Charters to be sold directly by the air carrier to the individual passenger.[62]

In this regard, one should also mention that the grant of scheduled authority to supplemental or non-scheduled airlines is now permissible in the United States. Since September 1978, some of the large supplementals have received authority to operate international scheduled routes and are now performing scheduled services in addition to their charter services.[63] Finally, the subsequent introduction of "Part Charters"[64] authority (on 1 January 1982) has helped virtually to make redundant the distinction between scheduled and non-scheduled transport in the United States - and hence for charters between the United States and its liberal bilateral partners.

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62. In this case, however, there is still a 7 day advance ticket purchase rule. See Parts 207 and 208 of the CAB Economic Regulations.

63. Capitol International was awarded rights between Brussels-Boston/Chicago/New York; World Airways between Amsterdam-Baltimore/Chicago/Detroit/New York and Oakland. See CAB Order 78-9-2 (Sept. 1, 1978).

64. The carriage of charter passengers with scheduled traffic on one single scheduled flight.

To conclude this section, one can point out that the trend to ever more liberalization of international air charters was significant for the North American, North Atlantic and European marketplaces. However, in many other regions and countries, governments felt unable to accept and approve such developments and therefore their attitudes towards charters remained much more restrictive.

SECTION III - FROM UNILATERALISM TOWARDS BILATERALISM IN INTERNATIONAL NON-SCHEDULED AIR TRANSPORT

With international charter traffic subject to unilaterally-imposed "regulations, conditions or limitations", a wide variety of regulatory policies affecting non-scheduled air services presently exists. These regulations range from absolute restriction to a large measure of freedom. Nevertheless, as a result of restrictive interpretation of Article 5 of the Chicago Convention, most of the international charter flights are subject to prior governmental approval.

The only exception to this requirement of prior permission may be found in two regional agreements (i.e. the 1956 Paris Agreement and the 1971 Manila or ASEAN Agreements) which exchange traffic rights for non-scheduled air

services.[65] However, as was previously mentioned, those two Agreements are too limited in scope to have an important effect on international charter operations. In this context, it should perhaps be remembered that during the first half of the 1950's, very few States concluded bilateral agreements relating to non-scheduled air services and these are no longer in force now.[66] Apart from such exceptions, international air charters are still generally authorized on the basis of unilateral governmental regulations. As these unilaterally imposed charter regulations may vary from one country to another, there has always been a very difficult choice-of-law question in these matters. In other words, which country's rules should govern a particular charter flight. Is it the rule of the country where the charter flight commences (country of origin rule), or the rule of the country where the charter flight terminates (country of destination rule)?. For example, if State A has one set of regulations and State B has another, more

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65. See surpa (footnotes 27 and 31) of this Chapter.

66. See the UK-France Agreement (1950), the UK-Switzerland (1952), France and Germany (1955). However, these Agreements failed to remove the prior approval requirements for charters. See Lichtman, "Regularization of the Legal Status of International Air Charter Services", 38 J. Air L. & Com. at 450 et seq. (1972). It should also be noted that France concluded charter agreements with Spain and Italy in 1948, 1949 consecutively.

restrictive set, which rules should govern a charter flight from A to B?. The general practice has always been that the most restrictive set of rules should apply (the rules of State B). Moreover, if the charter flight also served States C and D (both of which had rules similar to State A), the restrictive rules of State B would still apply. What this has meant is that "the lowest common denominator, i.e. the most restrictive rule, has tended to dominate".[67]

In the beginning of the 1970's, however, the United States started a new policy of concluding bilateral arrangements on international air charters. These charter arrangements took the form of a temporary memorandum of understanding (as was concluded with many European countries)[68] or alternatively, a bilateral non-scheduled air services agreement (such as concluded with Yugoslavia, Canada and Jordan).[69] In all such arrangements the "country of

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67. Driscoll, op. cit., note 32, at 78.

68. The first Memorandum was concluded with Belgium in Oct. 17, 1972, and followed by Austria, France, Germany, Ireland, The Netherlands, Switzerland and the U.K. Only the Agreement with France contained no provision on the country of origin.. See Browne, "The International Angle", 77 Aeronautical Journal at 29 (1973).

69. Only the Agreement with Canada (TIAS 7824) is still in force. The Agreement with Jordan (TIAS 7954) was replaced by a liberal agreement in 1980 and the Agreement with Yugoslavia (TIAS 7819) was replaced by a

origin" rule prevails thus assuring travellers originating in the United States of the application of the liberal American charter rules and not by the often more restrictive rules of the country of destination (e.g. in the above example, the rules of State A would apply).

The United States bilateral trend on charters was the palpable result of the wording used in the 1970 Nixon Statement that:

> "The foreign landing rights for charter services should be regularized, as free as possible from substantial restrictions. To accomplish this, intergovernmental agreements covering the operation of charter services should be vigorously sought, distinct however, from agreements covering scheduled services. In general, there should be no trade-off as between scheduled service rights and charter service rights."[70]

It is interesting to note here that, not only does the United States take a strong and positive bilateral stand, but it is also "anti-multilaterally oriented". Browne, Chairman of the CAB in 1972, illustrated this point of view by reasoning that what proved impossible in 1944 at Chicago (in the infancy of international air transport), is hardly worth even initial attempts in today's complex air traffic

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(continued from previous page)
Bermuda I type agreement in 1977 (TIAS 9364).

70. U.S. Statement on International Air Transportation Policy, approved 22 June, 1970, 63 Dep't St. Bull. at 88 (July 20, 1970).

situation. He thought that, from a practical point of view none of the objectives that are being handled bilaterally (e.g. capacity, frequency, tariffs, etc.) is capable of being handled multilaterally. Thus, he pointed out that "the matters of number of carriers and access to varying markets is something too closely identified by all governments with exchangeable benefits to be derived" that they "cannot be lumped into a multilateral understanding".[71] On the contrary, ECAC used to encourage the conclusion of a multilateral agreement on North Atlantic charters. It has always objected to its member States entering into bilateral non-scheduled air service agreements with the United States. However, notwithstanding ECAC opposition, many European countries (such as Belgium, West Germany, France, the United Kingdom, The Netherlands, etc...) have concluded bilateral charter arrangements with the United States.[72]

In Bermuda II, provisions relating to charters were included for the first time into the scope of a bilateral

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71. Remarks by Browne, Chairman of CAB, before the Royal Aeronautical Society, London at 11 (Mar. 13, 1972). It can also be seen from the disagreements on charter policy between the U.S. and the UK during the Bermuda negotiations in 1976-1977, that the Americans were still hesitant to conclude a multilateral charter agreement.

72. See supra note 68.

scheduled air services agreement.[73] The close relationship between scheduled and non-scheduled air services no longer justified dealing with the two sectors in isolation. The Preamble of Bermuda II clarifies, inter alia, the importance of this relationship: "believing that both scheduled and charter air transportation are important to the consumer interest and are essential elements of a healthy international air transport system." Article 14, paragraph 2 of the Agreement further confirms the co-existence of both types:

> "The contracting Parties also recognize the substantial and growing demand from that section of the travelling public which is price rather than time sensitive, for air services at the lowest possible level of fares. The contracting Parties, therefore, taking into account the relationship of scheduled and charter air services and the need for a total air service system, shall further the maintenance and development of efficient and economic charter air services so as to meet that demand."

Article 14, paragraph 3 of Bermuda II also refers to Annex 4 which deals in detail with air charters. This Annex (in paragraph 1) incorporated into the regime of the Bermuda II Agreement -the existing United States-United Kingdom Memorandum of Understanding on Passenger Charter Air

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73. There was, however, an exceptional case (in Oct. 1955) when the bilateral agreement between France and Germany covered charters in the text (see Article II) UNTS Vol. 353 at 203 et seq.

Services on April 1977 (since expired). However, Annex 4 was amended in April 1978 by a new Charter Air Services Agreement whereby charter traffic rights and some categories of cargo charters were permitted in a more liberal way.[74] The new Charter Agreement was valid for a period of 2 years, and thereafter new negotiations were required before the "country of origin" rule would apply. In 1980, however, the two contracting Parties were unable to renew the 1978 Charter Agreement mainly due to the United Kingdom reluctance to accept the liberal American charter rules.[75] The interim system was, therefore, to continue to operate on the basis of national regulations, but with the principle of reciprocity and balance being respected as far as possible.

It seems that entering into bilateral air transport agreements covering both scheduled and non-scheduled flights has remained American policy since the conclusion of Bermuda II. Typically, the United States liberal bilaterals cover both charter and scheduled services whereby the availability of inexpensive charter air service is encouraged and

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74. Amendment Concerning Charter Services of April 25, 1978, TIAS 8965. For more details, see Khan, United Kingdom/United States Air Transport Agreement of 1977 and its Amendments: An Analysis, unpublished thesis, McGill University at 150-151 (1984).

75. Aviation Week & Space Tech. at 34 (Mar. 31, 1980).

charterworthiness is generally governed by the "country of origin" rule.[76] With such charter policy becoming increasingly liberal and the country of origin rule applicable between the United States and many other countries, it is somewhat paradoxical that the volume of United States charter air traffic has decreased considerably in the late 1970's and early 1980's. It is apparent that "the overall result of the U.S. policy has been the decrease of charter traffic".[77] Liberalization of the American aviation policies permitting low fares on scheduled flights, in large part the result of post-Bermuda II liberal bilaterals are mainly responsible for the reduced volume.

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76. An exception is the United States-Philippine of 1980 (TIAS 10443).

77. Rosenfield, op. cit., note 6, at 158; supra note 63. Of course, such result was not intended by the U.S. policy which aims at expanding both charter and scheduled traffic.

SECTION IV - THE MAIN CHARTER PROVISIONS IN THE UNITED STATES LIBERAL BILATERALS

Generalities and Analysis

The United States policy for international air travel seeks to encourage expanded traffic through market forces. One of the ways this can be achieved is through non-scheduled air services. The American Policy of 1978 aims at "liberalization of charter rules and elimination of restrictions on charter operations".[78] It goes on to explain that:

> "Restrictions which have been imposed on the volume, frequency, and regularity of charter services as well as requirements for approval of individual charter flights have restrained the growth of traffic and tourism and do not serve the interests of either party to an aviation agreement. Strong efforts will be made to obtain liberal charter provisions in bilateral agreements."[79]

In fact, there are two elements in this objective: first, to liberalise charterworthiness rules; and second, to amend bilateral terms. The two are distinct, one domestic, the other international. This is so because, in the

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78. U.S. Policy for the Conduct of International Air Transportation Negotiations, August 21, 1978, 14 Weekly Composition of Presidential Documents.

79. Id.

absence of any bilateral or multilateral regulation of charters, (as stated earlier), this form of carriage has been regulated purely in national legislation and rules which set out eligibility and operational requirements. The United States liberal bilateral air transport agreements have not sought agreement on these terms; they have merely required the bilateral partner cede its right to regulate what a charter shall be under the agreement.[80]

If there is one document that summarizes the basic terms of the United States government's international aviation policy, it is the "American Model" liberal bilateral air transport agreement.[81] This "Model" has been revised and refined as to detail from time to time reflecting current United States policy. In fact, some countries have agreed with all of the proposed provisions, while other countries have accepted some or none in their bilateral talks with the Americans. The revised provisions, in addition to reflecting the changed views covering capacity, tariffs, routes, multiple designation and fair competitive

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80. This cession is either for country of origin or double country of origin/country of designation charter operations, depending on the agreement.

81. Bogosian, "Aviation Negotiations and the U.S. Model Agreement", 46 J. Air L. & Com. at 1011 (1981). The Model is printed as an Appendix to this Article at 1021-1037.

practices, contain a provision relating to charter traffic. The purpose of this provision is to provide the greatest possible freedom for non-scheduled air services to operate in the marketplace.[82]

The "Model" charter provision specifies that the rules and regulations to govern such traffic shall be those of the party in whose territory the traffic originates. It also provides for complete freedom in third and fourth freedom charters from any point in either country to the agreement, without reference to the points of scheduled service. The criterion is whether such carrier has been designated within the terms of this agreement. Finally, traffic from the United States to a third country is authorized (without a special permit) so long as such charter stops for 2 days within the territory of the other party to the agreement. The American view is that such a stop is sufficient to break the chain, and constitute such traffic as fourth freedom traffic.[83]

It should be kept in mind, however, that actual liberal bilateral air transport agreements pertaining to charter air services often show variations from the "Model" charter provision, more often than not in the form of

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82. Annex II of the Model, id.

83. CAB Regulation ER-1220, at 5 (May 8, 1981).

restrictions. Typically, each of the actual liberal bilaterals provides at least for: (1) the right to operate third and fourth freedom combination one-way or round-trip charters, with stopovers en route at will; (2) the right to carry traffic from the designated carrier's country beyond the territory of the other party (with transit or stopover in the other party's territory);[84] and (3) country of origin charter rules to apply. In every case "most favoured nation rules" apply. Because of these rules, typical characteristics of each kind of service, which still corresponds to different market demands, are not always to be taken into account.

Provisions on Non-Scheduled Air Services in the Liberal Bilaterals

Preamble

In some liberal bilateral air transport agreements, the Preamble (which always reflects the spirit of any agreement) expresses the consensus of both parties on the co-existence of scheduled and non-scheduled air services. Both categories are "important to the consumer interest and

84. Article 4(a), U.S.-Netherlands Agreement of 1978. However, fourth freedom transit/stopover rights are not permitted.

are essential elements of a healthy international air transport system".[85] These bilaterals further recognize the close relationship between both types and the need for continued development of a total air service system "which caters to all segments of demand and provides a wide flexible range of air services".

The Preamble in some other liberal bilaterals mentions only that the agreement covers both scheduled and non-scheduled operations.[86] However, there are certain bilaterals which make no reference at all to charter traffic.[87]

Grant of Traffic Rights for Charter Air Services

In general, each of the liberal bilateral air transport agreements stipulates that:

> "Each Party grants to the other Party the right for the designated airlines of that

85. See, e.g., the Preamble of German Protocol, Jamaica Protocol and the Belgium Protocol.

86. For example, U.S.-Thailand Agreement; U.S.-Jordan Agreement; The Netherlands Protocol; and Israel Protocol.

87. U.S.-Fiji Agreement; U.S.-Belgium Agreement of 1980, U.S.-Papua New Guinea Agreement. Although charters were not mentioned in the Preamble of such Agreements, they have been included in the text itself.

> other Party to uplift and discharge international charter traffic in passengers (and their accompanying baggage)...at any point or points in the territory of the first Party for carriage between such points and any point or points in the territory of the other Party, either directly or with stopovers at points outside the territory of either Party or with carriage of stopover or transiting traffic to points beyond the territory of the first Party."[88]

This clause allows thus one-way or round-trip third and fourth freedom, either directly or with stopovers en route. It also allows designated airlines of one contracting Party to carry charter traffic originating in their home country through the territory of the other contracting Party, with stopover rights there to the territory of third countries. However, fourth freedom transit/stopover rights are not permitted. This means that the wording of this clause does not cover fourth freedom traffic charter carriage by a designated carrier from a point beyond the territory of the other Party in transit via or with a stopover in the territory of that Party to its home-country.[89] Finally, it is worth noting that any point or points in the territories of

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88. The Netherlands Protocol (Article 4 (11)); German Protocol (Article 4(a)); Israel Protocol (Article 4(a)); U.S.-Fiji Agreement (Article 13(b)).

89. See, e.g., Wassenbergh, "Innovation in International Air Transportation Regulation (The U.S.-The Netherlands Agreement of 10 March 1978)", 3 Air Law at 144 (1978).

the contracting Parties may be served; hence the absence of the need to include a specific charter route schedule.

There is no liberal agreement that allows fifth and sixth freedom charter carriage. In other words, a designated carrier may not carry charter traffic between the other Party's territory and a third country, without a stop-over of at least two consecutive nights in its home-country.[90] This seems to be a vestige of traditional protectionism and an exception to the "liberalization" concept. However, in some bilaterals a derogation from this restriction is permissible in the way that "each Party shall continue to extend favourable considerations to applications by designated airlines of the other Party to carry such traffic on the basis of comity and reciprocity".[91]

Most of the liberal bilaterals permit the carriage of cargo on non-scheduled air services. However, it is not clear whether this right is granted separately or in combination with the right to operate passenger charters. In some

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90. For example, German Protocol (Article 4(b)).

91. German Protocol; Article 4(b); The Netherlands Protocol, Article 4(b); Papua New Guinea Agreement, Article 13(c). The word "comity" can be defined as "rules of politeness, convenience and goodwill observed by States in their mutual intercourse without being legally bound by them". See Brownlie, Principles of Public International Law, Clarendon Press at 31 (1979).

agreements, separate cargo charter flights are allowed.[92] Other bilaterals seem to limit the cargo charter traffic to combined flights (i.e. mixed passenger/cargo charters).[93] The United States-Netherlands Protocol permits combined charters but will only allow all cargo charters when the whole capacity of the plane is purchased by a single charterer (as defined by the Party in whose territory the cargo is uplifted).[94] Finally, separate cargo charters or combination charters are also allowed in some liberal bilaterals. In this context, the United States-Belgium Protocol is interesting in the sense that its Preamble explicitly states that the cargo flights between the two contracting Parties should be performed in a deregulated environment and that traffic rights are granted for charter traffic "in passengers (and their accompanying baggage) or in cargo or in combination".[95] In fact, this is not surprising since the Belgian national airline (Sabena) was a pioneer in introducing combined Boeing 747 flights and still derives a large percentage of its total profits from its

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92. See U.S.-German Protocol, Article 4(a).

93. U.S.-Papua New Guinea Agreement (Article 13(b)); Israel Protocol (Article 4(a)).

94. Wassenbergh, op. cit., note 89, at 144.

95. Article 4(1) of the 1978 U.S.-Belgium Protocol.

cargo operations.[96]

Country of Origin Rule

Under this rule, eligibility for charter air services is determined exclusively by the aeronautical laws and regulations of the country where the charter transportation originates. This principle is being used by the United States as the main tool in effectuating its policy towards the liberalization of international non- scheduled operations. Charter passengers originating in the United States are thus governed by the American liberal charter rules only and not by the often more restrictive charter rules of the country of disembarkation.

All the liberal bilaterals function with the country of origin rule with respect to charterworthiness. Each charter airline (whether a national of one contracting Party or of the other) shall follow the charterworthiness rules of the country where the charter air transportation, on a one-way or round-trip basis, commences. However, a unique feature of some agreements lies in the fact that the designated airlines of one Party have the right to use

96. See Merckx, "New Trends in the International Bilateral Regulation of Air Transport", 17 European Transport Law at 144 (1982).

either Party's charter rules for traffic originating in the other Party's territory (i.e. "double country of origin" or "country of designation" rule). The 1978 United States-Belgium Protocol was the first to contain this extension:

> "In addition, airlines of one Party may also operate charters originating in the territory of the other Party in compliance with the charterworthiness rules of the first Party."[97]

Applying this principle to American carriers means that American designated carriers may apply United States charter rules (including the Public Charter) to traffic which they uplift in Belgium destined for the United States. This right, however, does not extend automatically to the Belgian carriers; i.e. Belgian designated carriers cannot perform United States Public Charters originating in Belgium. They may perform such charters when originating in the United States (the principal country of origin charterworthiness rule). The home country retains domestic control over its own designated carriers, so that "country of designation" is a more appropriate description.

When the charterworthiness rules of one Party to the bilateral apply more restrictive terms to different national airlines, the least restrictive regulations will apply to the designated airlines of the other Party (i.e.

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97. Article 2(3) of the U.S.-Belgium Protocol.

the so-called "Most Favoured Airline Clause").[98] In this regard, one has to note that in the "free-market" environment, the decision as to "more restrictive" is presumably left to the airline. Although this extra-territorial application has the potential for dispute, this has apparently not occurred to date.

The country of origin charterworthiness rule is further liberalized by the minimum procedural requirements rule contains in some liberal bilaterals. In general, such agreements stipulate that neither Party shall require a designated airline of the other Party, for charter originating in the territory of that other Party, to submit anything more than a declaration of conformity with the rules applicable to charter traffic of that other Party.[99]

Most Favoured Nation Clause

All the liberal bilateral air transport agreements contain a "Most Favoured Nation Clause" dealing with the

98. See, e.g., Annex II of the 1979 U.S.-Fiji Agreement (TIAS 9917); Article 2(4) of the U.S.-Belgium Protocol of 1978.

99. Annex II, Section 3 of the U.S.-Thailand Agreement; Annex II, Section 3 of the U.S.-The Netherlands Antilles Agreement.

rules of operation of non-scheduled air services. If the charterworthiness rules of one Party to the bilateral apply different standards to different foreign countries, that Party must "apply the most liberal regulation or rule to the designated airlines of the other Party".[100] This means that the country of origin may not apply more liberal rules to any other airline. Strictly speaking, this is a "most favoured carrier and nation" rule.[101]

It may be of interest to realize that the most favoured nation rule is a principle of international trade law which is formally laid down in Article I of the "General Agreement on Tariffs and Trade", or the so-called GATT Treaty.[102] This Treaty prescribes (in Article V, paragraph 2) equality of treatment towards goods and vessels in transit across the territory of a contracting Party. The

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100. See, e.g., Annex II, Section 2 of the U.S.-Fiji Agreement.

101. See Wassenbergh, op. cit., note 89, at 144; supra note 98.

102. GATT was as opened for signature on Oct. 30, 1947, as a provisional arrangement between 23 countries. The institution which was to replace it, the International Trade Organization (ITO) never came into being owing to insufficient ratifications of the "Havana Charter". More than 80 countries now subscribe to GATT. See, in general, GATT (TIAS 1700); Ryan, International Trade Law, Sydney at Chapter I (1975).

same provision continues to require that "no distinction shall be made which is based on the flag of vessels, the place or origin, departure, entry, exit or destination, or any circumstances relating to the ownership of goods, of vessels or of other means of transport".[103] One may indeed wonder if the same principle of "non-discrimination" would apply to international civil aviation. Finally, it should be remembered that a most favoured nation treatment can exist in the technical field relating to the importation of aircraft spares, etc., but it is almost non-existent for the commercial operations themselves.

As is evident from the above presentation of the main charter rules, the general provisions of the liberal bilaterals, to a large extent, apply equally to charter and scheduled traffic. This is, of course, in line with the American policy that liberal bilaterals cover both forms of air service. It is not clear, however, if the country of origin rules (embodied in these bilaterals) will gain widespread acceptance. These liberal rules, which in the United States are now the Public Charter rules, have actually made the distinction, which was never really clear, between the two types of air transport, practically non-existent.

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103. For the State Practice regarding this provision, see Hyder, Equality of Treatment and Trade Discrimination in International Law, The Hague at 141 (1968).

Further efforts and attempts are thus necessary to try and settle the growing difficulties in distinguishing between them. The following section therefore attempts to explore the main efforts exerted by States under the auspices of ICAO in relation to the distinction problem, and also suggests a possible solution to this uncertainty.

SECTION V - THE VANISHING DISTINCTION BETWEEN SCHEDULED AND NON-SCHEDULED AIR SERVICES

The Nature of the Problem and Its Consequences

The two terms "scheduled" and "non-scheduled" owe their importance to their adoption in the Chicago Convention of 1944. Article 6 (which governs scheduled air services) implements the principle of sovereignty in Article 1 of the Convention, and is therefore the most restrictive regulatory regime possible for such services. Article 5 of the Convention (which governs non-scheduled air services) appears to be somewhat more liberal. Consequently, there are two entirely different regulatory regimes dealing with the allocation of commercial rights for international civil aviation.

The first paragraph of Article 5 stipulates, inter alia, that "each contracting State agrees that all aircraft

of the other contracting States, being aircraft not engaged in scheduled international air services shall have the right...to make flights into or in transit non-stop across its territory and to make stops for non-traffic purposes without the necessity of obtaining prior permission". This clause thus exchanges on a multilateral basis the first and second freedoms of the air for all non-scheduled flights without the necessity of obtaining prior approval. The clear intention of this phraseology is to confer a right of operation without prior negotiations other than advanced notification necessary for ATC, customs, public health and other similar purposes.[104] To this date, this provision hardly raises a controversy and the regulations of most States therefore grant freedom of entry to such flights upon prior notification on the basis of reciprocity. Only a limited number of States, however, require prior permission, due generally to safety or security considerations.[105]

The second paragraph of Article 5 continues to

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104. See, e.g., Annex 9 to the Convention, Para. 2.3.2.1; Lissitzyn, "Freedom of the Air: Scheduled and Non-Scheduled Air Services" in McWhinney and Bradley Eds., The Freedom of the Air, Montreal at 89 et seq. (1968); Thomas, Economic Regulation of Scheduled air Transport at 178 et seq. (1951).

105. ICAO Background Documentation, op. cit., note 3, at 17.

state that:

> "Such aircraft, if engaged in the carriage of passengers, cargo, or mail for remuneration or hire on other than scheduled international air services, shall also, subject to the provision of Article 7, have the privilege of taking on or discharging passengers, cargo, or mail, subject to the right of any State where such embarkation or discharge takes place to impose such regulations, conditions or limitations as it may consider desirable."

Article 5 here exchanges the third, fourth and fifth freedoms for commercial non-scheduled flights, but subject to the important restrictions enumerated at the end of the paragraph. In fact, the main debate relating to Article 5 centres around this proviso for it posed the question of what "regulations, conditions or limitations" may or may not be imposed. Could this mean that States have the right to require prior approval? As evident from the whole text, Article 5 has been designed to avoid the requirement of prior governmental permission for all non-scheduled services.[106] Thus, the ICAO Secretariat in 1949 ruled that the member States were not entitled to require prior permission for non-scheduled flights.[107] However, this

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106. Cheng, The Law of International Air Transport at 193, 195 (1962); Wassenbergh, Post-War International Civil Aviation Policy and the Law of the Air at 109 et seq. (1962); Johnson, op. cit., note 31, at 62.

107. ICAO Doc. 6894, AT/694 (Aug. 26, 1949).

interpretation was not in line with the attitude of most States which preferred to require prior approval for such flights. In 1952, the ICAO Secretariat interpretation was therefore reversed by the ICAO Council to the effect that any requirement of prior permission should not be "exercised in such a way as to render the operation of this important form of air transport (i.e. non-scheduled air transport) impossible or non-effective".[108] The subsequent practice of most States in imposing "regulations, conditions or limitations" was to require prior permission for the performance of virtually all international non-scheduled air services. For this reason, the second paragraph of Article 5 has almost become inoperative.

Article 6 of the Convention, in contrast, denies any multilateral grant of privileges for scheduled international flights, by stipulating that "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". Although non-commercial privileges are accorded to scheduled flights by the "International Air Services Transit Agreement", commercial privileges are normally granted only

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108. ICAO Doc. 7278, D/841 at 12 (May 10, 1952); ICAO Doc. AT/WP 206 (1951).

through bilateral agreements. As a result, a worldwide system of bilateralism continued to develop[109] remaining the main instrument for regulating scheduled international air transport.

Apart from the first two freedoms granted by Article 5, one is indeed tempted to say that there is no real difference in substance between the provisions of Articles 5 and 6, the only divergence being in form and procedure. Guldimann has correctly observed that:

> "By virtue of Article 6, scheduled air services need a special authorization by any of the foreign governments involved. By virtue of Article 5, non-scheduled services may be excluded or restricted at the discretion of any of the Foreign governments involved."[110]

In other words: "without an express governmental yes, a foreign carrier cannot operate a scheduled service; without an express governmental no, a foreign carrier is entitled to operate a non-scheduled service."[111]

The only accepted conclusion, therefore, is that non-scheduled commercial flight is authorized by the Chicago

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109. This means that Chicago Convention has brought no progress to the situation that existed between the two World Wars under Paris and Havana Conventions of 1919 and 1928 respectively, as far as scheduled flight is concerned. Lissitzyn, "Bilateral Agreements on Air Transport", 30 J. Air L. & Com. at 248 (1964).

110. Guldimann, op. cit, note 4, at 14.

111. Id.

Convention, but subject to such rules and regulations as are set down by the receiving State, while scheduled commercial traffic can be provided only on the bargaining table between the States involved. The result has been that non-scheduled service is based generally on unilateral governmental regulations, while scheduled service has been regulated by bilateral agreements.

An essential prerequisite for effective regulation is a clear understanding of the nature of the activity to be regulated, but the Chicago Convention, although it distinguishes between the rights to be accorded to non-scheduled flights (Article 5) and scheduled air services (Article 6), does not define these terms. It merely refers to non-scheduled flight as a flight by an aircraft which is not engaged in scheduled international air service, but leaves scheduled service referred to in Article 6 undefined. Article 96 of the Convention, however, only defines the expression "air service" by indicating its public character as being performed for public transport, and the expression "international air service" solely in its international perspective.[112] These definitions cannot, therefore, be

112. Article 96 defines "air service" as "any scheduled air service performed by aircraft for the public transport of passengers, mail or cargo". The term "international air service" is defined as "an air service which passes through the airspace over the territory of more

used to determine the nature and the meaning of scheduled as opposed to non-scheduled operation. The distinction between the two terms is of particular importance due to the different legal treatment each type receives under the Convention and because of its role in determining the scope of bilaterals for the regulation of scheduled flights.

In searching for a definition, it was crucial to determine first what services should be regarded as scheduled, vis-a-vis those as non-scheduled.[113]

In order to satisfy the need for this distinction, the question was raised in 1947 by the First Assembly of ICAO which reached an inconclusive Resolution to the effect that "the ICAO continue studies with the object of devising for international adoption a definition which clearly distinguishes for the purposes of the Convention between scheduled and non-scheduled operations".[114] During its Second Session in 1948, the Assembly requested the ICAO Council to lay down a definition for the guidance of the States Party to the Convention, in applying Articles 5 and 6

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than one State".

113. Goedhuis, "Questions of Public International Air Law", Recueil des Cours, Vol. 81 at 256 (1952).

114. ICAO Doc. 4522, AI-EC/74, at 15.

thereof.[115]

After nearly 4 years of preparatory work and discussions, the ICAO Council adopted on the 25th of March 1952 a "Definition of a Scheduled International Air Service" on the assumption that all international air services not fitting into that Definition would be regarded as non-scheduled.[116] The ICAO Council based its definition on the following elements:

(a) The operation must consist of a series of flights. A single flight by itself can thus never constitute a scheduled international air service although it may form part of such a service.

(b) The operation must be international in character. Each flight must pass through the airspace over the territory of more than one country.

(c) The purpose of the operation must be the transportation of passengers, cargo or mail for remuneration, monetary or otherwise. Free operations for humanitarian reasons, or operations for other purposes (such as training or cropspraying) cannot be regarded as scheduled, even if they fulfill the other elements of the Definition.

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115. See "Repertory Guide to the Convention on International Civil Aviation", ICAO Doc. 8900 at 1-3 (1971).

116. See ICAO Doc. 7278-C/841 at 3 (May 10, 1952).

(d) The operation must be open to use by members of the public.

(e) The operation must be systematic in the sense that it must be operated according to a published timetable, or in a way leading to regularity or frequency.

This Definition is cumulative in its effect: if any of the above-mentioned characteristics is missing, the flight must be classified as non-scheduled.[117] It is hardly a generous Definition, but with due credit to ICAO it "reflected the actual state of the industry at that time: a limited system of international routes that, at least in intercontinental markets, was initially designed primarily for the carriage of air mail; and virtually no international charter operations".[118] Therefore, the Council's Definition has never received wide acceptance by the contracting States. Many countries have their own definition, whereby a non-scheduled service is often defined in a positive way.[119]

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117. Id., Notes on the Application of the Definition (Note 1).

118. Driscoll, op. cit., note 32, at 76.

119. Guldimann, "Scheduled and Non-Scheduled International Air Services, Confirmation or Elimination of the Distinction", ITA Bull., No. 22 at 489 (Jun. 9, 1980). The UK (CAA) defines the expression "charter flight" as a flight in respect of which the following condi-

Over the years, the Council's Definition could not keep up with the expansion and evolution of the marketplace. During the last two decades non-scheduled air transport, as has been shown,[120] has developed enormously with new types of services such as ITCs, non-affinity group charters (ABCs and TGCs) and finally Public Charters. These low cost services are performed more or less regularly in accordance with a published timetable and open to use by members of the public, and hence gradually approached the operating characteristics of a scheduled service. They came to be commonly called "schedulized" or "programmed" charter services[121]

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tions are satisfied:

> "(a) all the accommodation on the aircraft which is occupied by passengers or cargo has been sold to one or more charterers for re-sale; and
>
> (b) in the case of a flight for the carriage of passengers, the operator had made available not fewer than 10 seats to each charterer, provided that this shall not apply to service for the carriage only of ship's crew, including masters, their baggage and parts or equipment for ships."

Quoted from ICAO Background Documentation, op. cit., note 3, at 16.

120. See supra, Section II of this Chapter.

121. See Special Air Transport Conference (Montreal, 13-26 April 1977) Report, ICAO Doc. 9199 at 10 (hereinafter cited as SATC (1977), ICAO Doc. 9199); Guldimann, "Air Transport in International Law", in Wassenbergh

and could thus conceivably come under the ICAO Council's Definition of 1952. As a result, the distinction between the two types of air transport (which was thought to be basic) is not as decisive as often believed. There is no clearcut borderline, and individual States are given a very wide discretion in respect of traffic rights for non-scheduled operations, as well as with regard to the classification of "programmed" charter flights as scheduled or as non-scheduled respectively.

In fact, the public pressure for lower air fares has necessitated the nations, for political reasons, to accept the operation of such "schedulized" charters in order to enable ever more people to legally travel by air on such flights. In this context, one could perhaps say that, because States (for political reasons) had to allow a large measure of freedom to the charter carriers, they were prepared to accept uneconomic fares on the scheduled services of the national scheduled carriers. Lord Boyd Carpenter, Chairman of the British Civil Aviation Authority, once stated that "we have come out unshamedly as proponents of cheap fares...the philosophy remained that it was better to fill aircraft at low fares than fly them around half-

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& Fenema Eds., International Air Transport in the Eighties at 151 (1981).

empty at high fares".[122] Thus, it became "politically more important to enable the public to travel by air at low fares than to protect an economically viable international scheduled network".[123] However, it can be stated that the governments did everything to find ways and means to protect their scheduled carriers and at the same time to serve the interests of the travelling public. In addition to the prior permission required for the operation of charters, there are three general types of restrictions on their operations: marketing restrictions through charter definitions and rules; geographical and route restrictions; and capacity control.[124]

Marketing-type restrictions enable States to restrict the access to the market by simply barring certain types of charters such as ITCs, ABCs, etc. Geographical and route restrictions are self-explanatory.[125] Capacity-

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122. Cited in Flight International at 535 (Apr. 5, 1973).

123. Wassenbergh, op. cit., note 18, at 52.

124. For more details about these methods, see ICAO Circular 136-AT/42 at 21 et seq. (1977); Karamoko, International Non-Scheduled Passengers Air Transport: Origin, Characteristics, Development, Issues, unpublished thesis, MIT at 38-40 (Jun. 1979); Rosenfield, op. cit., note 6, at 163-164.

125. It is interesting to note here that the Israeli government has recently applied new rules forbidding a

control restrictions can vary from State to State and usually take the form of absolute quotas or some relationship to the existing capacity offered by the scheduled carriers.[126] Finally, price can also be controlled through either a price floor based on estimated costs or a fixed relationship to the existing IATA negotiated tariffs for scheduled operations.[127] In sum, all these restrictions exist in order to ensure that charter flights do not impair the viability of scheduled operations and to provide some opportunity for non-scheduled carriers to compete in the marketplace. From a regulatory point of view, however, one can still argue that the interests of the charter carriers and the scheduled carriers cannot easily be harmonized.

Due to the increasing competition of the charter

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mix of Israeli and foreign passengers flying on charter flights out of the country to destinations within a 150 N.M. radius of cities served by scheduled carriers. Some foreign charter airlines reacted to these rules by stopping services to Israel. See "Israeli Charter Rules Anger Airlines", Flight International at 93 (18 Aug. 1984).

126. It can also take the form of uplift ratios, i.e. a directional balance of the third and fourth freedoms.

127. States that have not adopted any particular price control rule, nevertheless exercise general surveillance over charter prices on an ad hoc basis.

operators, the scheduled carriers (in retaliation) began to offer services at prices and with features that matched the non-scheduled services. For instance, affinity group fares were IATA's response to affinity group charters. Group inclusive tour (GIT) fares were also its response to ITCs, while APEX fares were the answer to non-affinity group charters (ABCs and TGCs).[128] As a result, the concepts of scheduled and non-scheduled services began to merge from either side of the fictitious border line separating them, in a manner which leaves the usefulness of the distinction open to considerable doubt. Thereby, a severe competition bloomed between the two categories which led to excess capacity on certain routes, insufficient capacity on others and waste of resources. The poor financial results of most scheduled international carriers and the regulatory confusion in the field of international charters were, to a large extent, the consequences of this development.[129]

It is worth noting that an attempt was made in 1974 to integrate charter only air carriers into IATA's struc-

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128. For these special fares, see IATA Working Paper presented to the 1977 SATC, ICAO-WP/5 at 3 et seq. (1011/77); ICAO Circular 136-AT/42 at 4-5 (1977).

129. Wheatcroft, "The Size Shape of Future Air Traffic", in Wassenbergh & Fenema Eds., op. cit., note 121, at 106.

ture, whereby they would be entitled to vote on charter matters only.[130] However, these new amendments never came into force due to the lack of United States approval which argued that IATA "tried to extend its cartel to include the entire airline industry".[131] In fact, the bloodless war of competition between scheduled and non-scheduled operators is still going on. For example, an increase of almost 25% in non-scheduled traffic in 1982 (on the North Atlantic) forced scheduled carriers to revise fare levels in 1983 to win back a larger share of the diverted traffic volume.[132]

A controversial problem has always been, whether non-scheduled commercial air services divert traffic from scheduled air services, i.e. whether they impair the profitability and efficiency of scheduled air services. The

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130. Haanappel, "The International Air Transport Association (IATA) and the International Charter Airlines", 3 Annals of Air and Space Law at 151-152 (1978); Hammarskjold, op. cit., note 23, at 150.

131. CAB Docket 27756.

132. See supra, Section I of this Chapter; IATA Study on Aviation Deregulation, Geneva at 40 (Dec. 1984). It is interesting to note (as an example of competition) that the 1983 summer transatlantic promotional fares included a round-trip price of $599 between New York-London compared to $770 in 1982; New York-Rome at $749 compared to $899 in 1982; New York-Frankfurt at $699 compared to $749 in 1982. See Aviation Week & Space Tech. at 35 (Mar. 7, 1983).

scheduled carriers always argue that the charter operators should not be given the freedom to divert traffic from the regular services and that the governmental charter regulations should closely define "charterworthy" traffic and that the aeronautical authorities should strictly control the compliance with their charter regulations. They base their arguments on the fact that while the scheduled operators must maintain regular routes throughout the year to destinations which are sometimes unprofitable, the charter airlines "merely take the cream off the tourist season traffic".[133] It is submitted that this is not the case. The fact that there is only one air travel market,[134] but this overall market comprises both a business travel and a leisure travel segment. It is evident that business travellers usually fly on scheduled air services. The leisure travellers (especially the tourists), however, can use both scheduled and non-scheduled services, and will choose that type which is the most convenient to them.[135] Price considerations will of course be their main concern.

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133. See Flight International at 93 (18 Aug. 1984).

134. Statement by Hammarskjold before the Sub-Committee on Aviation of the US Senate Committee on Commerce (21 Oct. 1971); Gazdik, op. cit., note 7, at 36; "Agreeing Fares and Rates", IATA Publ. at 69 (Jun. 1974); Detière, op. cit., note 20, at 251.

135. See supra (footnotes 19 and 20) of the Chapter.

In this regard, it must be remembered that charter traffic (with its low fares) has definitely made air travel accessible to individuals who would be otherwise unable to fly by air. In the United States (the biggest air traffic market in the Western world), it seems that the problem of diversion has not been a major issue. In Saturn Airways, Inc. v. CAB, the United States Court of Appeals for the District of Columbia stated that "the consistent lamentations and predictions of doom by diversion raised by the scheduled air carriers in the past have proved, to our way of thinking, to be considerably overstated".[136] The Americans thus view the introduction of charters as being a major catalyst to the expansion of international air transport, since they "generate new traffic and help stimulate expansion in all sectors of the industry".[137] Whatever is said for or against non-scheduled air service, this form of air carriage has undoubtedly been to the benefit of the aviation consumer.

In conclusion, while no one denies the need for both scheduled and non-scheduled air services, the question is one of balancing competition between the two sectors,

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136 Saturn Airways, Inc. v. CAB, USCA, D.C. Cir., 12 Avi. 17.986 (July 11, 1973).

137. The US 1978 Policy, op. cit., note 79.

taking into consideration the needs of different components of the traffic mix, the desire to promote tourism and foreign trade, and the rights of both sectors of the industry to coexist. The difficulty lies, therefore, in the inability to match the aviation policies of different States in order to achieve the desired goals and objectives. Professor Fanara correctly observed that "the broad dimensions acquired in the last decades by charter air transport have favoured the worldwide circulation of persons. However, some difficult problems have arisen due both to the lack of coordination between scheduled and non-scheduled flights, and to the different policies followed by the various States in protecting their own domestic interests".[138] Since international air transportation, by definition, involves more than one country, it is vital to compromise the divergent and sometimes conflicting policies and interests of various countries to establish a satisfactory multilateral approach or sufficient regional agreements that provide for the needs of all participants.

138. Speech delivered to the Symposium on Air Charter, op. cit., note 21.

ICAO's Intervention in the Problem

With the development of the marketplace over the years, various types of services evolved which were neither scheduled nor non-scheduled services. It became apparent that those services, commonly referred to as "programmed" or "schedulized" charters, have the following basic characteristics in common with scheduled services:[139]

(a) they operate as a systematic series of flights between the same regions;

(b) they operate in accordance with a published timetable and at publicized tarriff; and

(c) they are open to all members of the public and are not subject to "common carrier" obligations.

These flights, however, can still be considered as non-scheduled services by virtue of the fact that they are not directly offered to the public by the air carriers, i.e. they may only be sold to charter participants through intermediaries (tour operators, charter operators, charter organizers, etc.).[140]

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139. ICAO Panel of Experts on Regulation of Air Transport Services, ICAO, ATRP/1-Report at 10 (July 1978); supra note 121.

140. It seems that there is also another significant difference between the two types which appears to lie in attainable load factors. It is estimated that scheduled services can never operate at load factors

The 1977 Air Transport Conference dealt at some length with the problem of differentiation between scheduled and non-scheduled air transport. In the course of its discussion, the Conference realized that the final objective in this field was to ensure that both categories satisfy the needs of the public in a manner that permits their efficient and economical operations.[141] To achieve this final objective, the Conference in Recommendation 3, recommended, inter alia, that studies be undertaken on characterizing non-scheduled international operations and distinguishing them from scheduled operations, and on examining the feasibility of amending Articles 5, 6 and 96(a) of the Chicago Convention and of revising the 1952 Definition of scheduled services.[142] In spite of its somewhat general language, Recommendation 3 represents a potential starting point for changes or further evolution of international

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exceeding 65 to 70%. Charters, however, can in principle operate at 100% load factor. See Haanappel, op. cit., note 25, at 124; supra note 62.

141. SATC (1977), ICAO Doc. 9199, op. cit., note 121, at 10.

142. Id. at 11-12. In this regard, Egypt submitted a Working Paper suggesting preparation of a "coordinated and integrated regulatory set-up, encouraging both scheduled and non-scheduled air transport". SATC-WP/46 at 2.

regulatory regime in several important aspects of air transport.

Pursuant to this Recommendation, a "Panel of Experts on Regulation of Air Transport Services" was established by the ICAO Council (Air Transport Committee) in 1978, to carry out amongst other things this Recommendation. It is interesting to note that this group of experts were appointed taking into account the personal merits of its members rather than their national representation to their governments. It was therefore expected, as a result of their work, that recommended solutions of practical and possible applications would be available to the contracting States.[143]

The general view of the Panel members was that the Council Definition of 1952 had become obsolete, and they therefore examined several alternative ways of establishing guidelines which would better reflect the current characteristics of scheduled and non-scheduled operations. At this stage of its work, the Panel agreed that the most useful approach would be to establish the distinguishing characteristics of scheduled and non-scheduled services separately.

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143. Gertler, "ICAO Air Transport Regulation Panel and the Development of International Air Law", 8 Annals of Air and Space Law at 68 (1983); ICAO, ATRP/1-Report at 3.

It dealt at length with listing such characteristics.[144] In sum, the following are the most significant distinguishing characteristics:[145]

Scheduled Air Services:

(a) are obliged to provide service with a high degree of regularity according to a widely distributed schedule;

(b) operate over a network of routes, normally with interline facilities and interchangeability of tickets;

(c) operate sufficient capacity so as to be able to provide on-demand service on a high proportion of occasions; and

(d) subject to the filing of tariffs and their approval by governments.

Non-Scheduled Air Services:

(a) are not obliged to operate services and can be cancelled if a satisfactory payload is not available;

(b) operate pursuant to a charter contract with one or more charterers with the intention of covering the entire capacity of the aircraft, and

(c) operate in conformity with charterworthiness rules.

Most Panel members understood that certain difficulties in the air transport regulatory field derive largely from the fact that, as conditions have developed, scheduled

144. ICAO, ATRP/1 - Report at 7-9.

145. Id.

and non-scheduled (in particular the "programmed" charter) operations, which are governed by entirely different systems, compete in the international market.[146] They therefore decided to consider the common characteristics of scheduled services and "programmed" charters in the light of the 1952 Council's Definition. The Panel concluded that such charter services have in many ways acquired the characteristics of scheduled services according to the terms of the 1952 Definition.[147] From the regulatory viewpoint, however, one can argue that the possible need for harmonization of regulatory regimes arises because of the competitive situation that may develop when:

> (a) both scheduled and "programmed" charter services operate over the same route or between the same regions;
>
> (b) both types of service compete for the same travel market; and
>
> (c) the "programmed" charters offer a significant proportion of the total aircraft capacity offered by all air services during a given period.

Realizing these facts, the Panel members agreed that they should define only one category of air service,

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146. SATC (1977), ICAO Doc. 9199, op. cit., note 121, at 10 (Para. 6); Bogolasky, "ICAO Panel of Experts on Regulation of Air Transport Services", 3 Annals of Air and Space Law at 602 (1978).

147. For these characteristics, see supra note 139.

thereby defining the other services by exclusion, to avoid the probability of confusion through overlapping or omission. In this regard, they preferred to define or characterize the scheduled air service and, as a result, directed their attention to the feasibility of amending the Council's 1952 Definition. Somewhat surprisingly, and reversing itself, the Panel members arrived at the consensus that the 1952 Definition was sufficiently flexible to permit States to classify some charter operations, particularly certain "programmed" charters as scheduled, and that this desirable flexibility "should be emphasized by the introduction of a general note and by modification to existing notes pertaining to the Definition in Doc. 7278".[148]

This conclusion arrived at by the Panel was approved by the 1980 Air Transport Conference which recommended that the 1952 Definition "be maintained without revision";[149] and with only a less significant change in the language of sub-paragraph 4 of the general note,[150] it

148. ICAO, ATRP/2-Report at 4; ATRP/3-Report at 7.

149. See Recommendation 1, AT Conf/2, ICAO Doc. 9297, at 7. The changes of "Notes", relating to the 1952 Definition were also considered and approved by the 23rd Session of the ICAO Assembly in 1980. See Resolution A23-18, ICAO Doc. 9316, at 81.

150. The Conference added these words "user with the appropriate ticket of air waybill" instead of the

adopted the modifications to the "Notes on the Application of the Definition" as proposed by the Panel. The approved "General Note" reads as follows:

> "This Definition typically encompasses a service:
>
> (i) which is part of an international network of services, operating according to a published timetable;
>
> (ii) where the on-demand passenger has a reasonable chance of securing accommodation;
>
> (iii) which normally operates irrespective of short-term fluctuations in payload;
>
> (iv) where stopover and interlining facilities are offered to the user with the appropriate ticket or air waybill, subject to the relevant international agreement, if any.
>
> Because of the operational characteristics expressed by the Definition and subject to the considerations in Note 6 below, States may, at their discretion classify as scheduled a service which operates, for example:
>
> (i) pursuant to a charter contract with one or more charterers with the intention of covering the entire capacity of the aircraft; and
>
> (ii) frequently and with regularity."[151]

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words "passenger with the appropriate ticket" proposed by the Panel. Id. at 7, 8; ATRP/3 - Report at 9.

151. Attachment to Recommendation 1, AT Conf/2, ICAO Doc. 9297, at 8.

The new Note 6 replaces the former Note 8 which explained the term "open to use by members of the public". The last sentence of old Note 8 was amended as follows:

> "A service may be regarded as open to the public, notwithstanding certain restrictions, which relate, for example, to the time of reservation, the minimum length of stay, or the obligation to deal with an intermediary. It will be incumbent on each contracting State, in respect of each service having such characteristics, to assess the scope of these restrictions and decide whether the restrictions are so substantial that the service should be considered as non-scheduled."[152]

On the other hand, Note 1 explaining the cumulative nature of the elements of the "Definition" was amended to say that if any of the characteristics (a), (b) or (c)[153] is missing, the series of flights cannot be classified as a scheduled international air service, subject to the provisions of Note 6 mentioned above. Finally, the old Notes 7, 9 and 11 were deleted.

Evaluation of ICAO's Work

(1) It seems that the differing political and economic circumstances surrounding international air transport, i.e. the diverging and conflicting national policies

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152. Id. at 11.

153. See supra (footnotes 116 and 117) of this Chapter.

with regard to the distinction between scheduled and non-scheduled operations, shaped the final course taken by the Panel of Experts. Instead of pursuing its terms of reference by revising the 1952 Council's Definition, the Panel took a quite different approach. It retained the Definition as is, but introduced several changes and additions in accompanying "Notes" to permit States to classify certain types of regular or frequent non-scheduled services as scheduled. The Panel thus refused to proceed into the core of the regulatory problem and try to reduce national divergences with respect to differentiation between the two categories, in order to provide the system with some more harmony. This was correctly labelled by one commentator as an "exercise in international frustration".[154]

(2) One can criticize the Panel's conclusion as being too flexible and leaving too much room for divergent national laws. The proposed amendments in fact give virtually absolute freedom to States to classify some non-scheduled services, particularly certain "programmed" charters as scheduled, the same freedom they have been enjoying with respect to economic regulation of international air services, as a result of the existing regulatory

154. Guldimann, op. cit., note 110, at 135.

regime of the Chicago Convention.[155] Each amendment of the 1952 Definition should rather aim at a precise and legally binding definition, which would allow the so-called "programmed" charters to fall under the definition of a scheduled air services.

(3) Since the Panel's conclusion is not binding on contracting States, it was generally well received by the 1980 Air Transport Conference and, as some statements show, was "the only approach possible" or "the best that could be achieved".[156] It is worth noting here that some participants to the Conference made proposals aiming at formulating a more definite and clearer guidance for States on how to use their discretion for a possible re-classification of certain charter services as scheduled.[157] They were however rejected by an ample majority of delegations who obviously felt that complete freedom of action, in completely divergent directions, would be more valuable than any

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155. See supra, "The Nature of the Problem", in Section V of this Chapter.

156. Statements made by the U.K. and Norway, cited in Azzie, "Second Special Air Transport Conference and Bilateral Air Transport", 5 Annals of Air and Space Law at 5 (1980).

157. At Conf/2, ICAO Doc. 9297, at 6; see, e.g., Working Paper presented by Switzerland to the Conference, AT Conf/2-WP/15, at 2.

degree of uniform limitation.

(4) In order for the proposed amendments to be functional and acceptable to States, it is crucial that they be uniformly accepted by such States; that is to say the re-classification of the same types of charter services as scheduled must be agreed upon between States, a step which is unlikely to be reached in the near future. The alternative to this step would be that States intending to implement these amendments will have to negotiate classification of certain charters by "argumentation, bargaining, and if necessary, compromises"[158] within the existing and prevailing system of bilateralism.[159] However, it has to be noted that the use of bilateral agreements to re-classify charters will have an effect upon their structure and certain amendments and adjustments therein will be necessary to cope with the new situation to insure that the smooth operation of these flights is not impaired.

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158. Azzie, op. cit., note 156, at 6.

159. Id. where the author further clarified that it would be "up to the two Parties to modify accordingly all pertinent provisions of the bilateral agreement" (e.g. designation, capacity and tariff clauses or the route schedules) "be it by explicit changs in the text or by supplementing the agreement by an exchange of notes". For more details about this alternative, see El-Hussainy, "Bilateral Air Transport Agreements and their Economic Content with Special Reference to Africa", 8 Annals of Air and Space Law at 123-125 (1980); Matte, op. cit., note 27, at 166-171.

(5) The ambiguity now surrounding international aviation will undoubtedly further progress the blurring of the two types of operation, even if opposed by States which prefer to maintain the distinction and to keep non-scheduled services within well defined regulatory limits. It is hopeful therefore that the Third Air Transport Conference (convened by the ICAO Council for October 1985)[160] will provide another opportunity to the international aviation community to explore reasonable solutions to this uncertainty.[161]

Continuation of ICAO's Work

In fact, the extreme caution of the Air Transport Regulation Panel was without doubt influenced, as has been pointed out, by the conflicting policies and positions of member States. It is however important to emphasize that already in the early stages of its work, some members of the Panel were of the opinion that work should be continued to

160. ICAO State Letter S29/1-84/31 of April 6, 1984.

161. The tentative Agenda for the Conference includes two items which could lead to discussion of the problem: item (1) Commercial rights for scheduled services, and item (2) Policy concerning international non-scheduled air transport. See Attachment to ICAO State Letter S29/1-84/31 of April 6, 1984.

establish more definite guidelines as to how governments should use their discretion with regard to the application of the 1952 Definition in the problem area of "programmed" charter flights.[162] Significantly, the 1980 Air Transport Conference agreed that the Panel, without reviewing the amended "Notes" to the Definition, might need to "supplement its work" as a consequence of its future work on regulation of non-scheduled air transport.[163] This agreement of the Conference stimulated some activity in the Panel towards further clarification for States of certain aspects or implications of a possible re-classiffcation of charter services as scheduled. The views of Panel members were canvassed on such aspects as the effects of re-classified operations on bilateral agreements and on third countries, the problem of possible disagreements between States on re-classification and the tariff regime to be applied, the concept of "substantial restrictions", etc. The ICAO Secretariat prepared a summary of these views for

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162. See ICAO-ATRP/3 - Report at 7, Para. 18 (Oct. 1979).

163. AT Conf/2, ICAO Doc. 9297, at 7, Para. 10. Also the Assembly, in its 24th session of 1983, directed the Council to continue the studies on the regulation of charters (Res. A24-11).

the last meeting of the Panel;[164] but owing to insufficient time, the Secretariat's paper could not be considered and thus this fairly extensive preparatory work potentially very useful to States was brought to an end without benefit to anybody.

During the period between 1981 and 1983, the Panel held four meetings to complete its work programme.[165] The sixth meeting of the Panel established two lists, the first consisting of those operations considered as "international non-scheduled air transport" and the second of those excluded from this concept.[166] It is interesting to note that "Public Charters" are considered non-scheduled,[167] while "Part Charters" are recognized as a form of marketing by scheduled airlines and can, according to the Panel, not

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164. It was held during the period 7-18 March 1983. ATRP/7-Report.

165. See ICAO-ATRP 4/5/6/7 - Reports.

166. No attempt, however, was made to actually define the types (e.g. Affinity, ITC, ABC, etc.) of non-scheduled operations. See ATRP/6 at 4-8 (March 1982).

167. Id. at 4. For a different opinion, see Guldimann, "Public Charters - Chicago Article 5 or Article 6", in Kean Ed., Essays in Air Law, London at 81 et seq. (1982).

be considered as non-scheduled.[168] In their seventh and last meeting (which was held in March 1983), the Panel members listed a number of devices which governmental aeronautical authorities may use in regulating non-scheduled international air services.[169] The fact, however, is that the Panel's work on regulatory devices resulted in nothing more than a factual compilation and categorization of currently known regulatory mechanisms of devices applied by States to international non-scheduled operations. The Panel members also developed a long list of almost 28 guidelines which may be used for the regulation of non-scheduled transport. These guidelines do not actually reflect any single policy orientation but rather a range of national policies and objectives.[170] It should be noted therefore that the listed criteria and the developed guidelines do not imply the Panel's approval, support or rejection thereof.[171] This reflected the view of many members that the

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168. Id. at 6-8. As such the Panel did not develop any rigid definition on views on these operations.

169. ICAO-ATRP/7 at 3-6.

170. Id. at 7-14. An important area which was not addressed in any detail by the Panel involved the question of guidelines relating to the possible reclassification of programmed charter operations as scheduled.

171. Id. at 7, Para. 17.

diversity of national policies (in the area of non-scheduled regulation) would limit their capability to develop meaningful and generally acceptable guidance material.

It is worth mentioning here that the Panel of Experts, during its sixth meeting mentioned above, also reconsidered the subject of the feasibility of amending Articles 5, 6 and 96(a) of the Chicago Convention.[172] After lengthy discussions, however, the Panel members arrived at the consensus that such amendments were "neither necessary nor appropriate" for two basic reasons.[173] One had to do with the approval by the 1980 Air Transport Conference (Recommendation I) and the 23rd Session of the Assembly (Resolution A23-18) of the amended "Notes" to the Council's Definition of 1952.[174] Since this Definition was made more flexible by the amended and added "Notes" but was otherwise retained, the traditional concepts of distinguishable scheduled and non-scheduled operations reflected in Articles 5 and 6 of the Chicago Convention respectively, did not require revision on these grounds. The other main

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172. The Panel had this problem on the agenda of its second meeting in 1979, but deferred it to some later meeting due to insufficient time. See ICAO-ATRP/2-Report at 15, Para. 42. No work, however, on the subject had been done until the sixth meeting of March 1982.

173. ICAO-ATRP/6-Report at 14, Para. 44.

174. See supra note 149.

reason was the complexity and time-consuming nature of the amendment process itself. The Panel thus decided that it had concluded its work on this subject.

Notwithstanding the deficiencies existing in Articles 5, 6 and 96(a) of the Chicago Convention, the Panel members apparently decided not to amend them after taking into account the policy and procedures relating to the amendment of the Convention. In this respect, it should always be borne in mind that Assembly Resolution A4-3, which is still in force, sets out the necessary steps regarding the Convention's amendment.[175] Of particular relevance is Resolving Clause 1 requiring that any proposed amendment be proved necessary by experience and/or demonstrably desirable or useful.[176] Thus, an amendment of the Convention may be considered "appropriate" when either or both of such specific tests is satisfied: i.e. the amendment is proved indispensable; it is demonstrably advisable or helpful. It seems that the Panel could not confirm compliance with either condition of the test. Moreover, according to Resolving Clause 7, the ICAO Council should not itself

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175. Resolution A4-3, "Policy and Programme With Respect to the Amendment of the Convention", (1950). This Resolution is still in force, see "Assembly Resolutions in Force", ICAO Doc. 9349 (as of October 1983); ICAO Doc. 9414, A24-Res. (1983).

176. Id. Resolving Clause 1.

initiate any proposal for amendment unless such change is urgent in character. Whereas, Resolving Clause 4 stipulates that Article 94 of the Chicago Convention should be maintained in its present form. This Article deals with amendment procedures and states, inter alia, that amendments must be ratified by at least two-thirds of the total number of member States.[177] The total number of contracting States being 156 by 1985, means at least 104 ratifications would be required before any amendment could enter into force.[178] Also, the time required for an amendment to the Convention, approved by the Assembly, to enter into force varies considerably. To cite but a few examples, while Article 50(a) of the Convention amended by the Assembly on 12 March 1971 to increase the Council's membership from 27 to 30 entered into force on 16 January 1973 (taking 1 year and 10 months), a similar amendment adopted on 16 October 1974 to increase the membership from 30 to 33 entered into force on

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177. Paragraph (a) of Article 94 stipulates that "any proposed amendment to this Convention must be approved by a two-thirds vote of the Assembly and shall then come into force in respect of States which have ratified such amendment when ratified by the number of contracting States specified by the Assembly. The number so specified shall not be less than two-thirds of the total number of contracting States."

178. See, ICAO Bull. (Feb. 1985); Milde, "The Chicago Convention - After Forty Years", 9 Annals of Air and Space Law at 119 (1984).

15 February 1980 (5 years and 4 months).[179] Amendment of Article 48(a) dealing with frequency of Assembly sessions required 13 years between approval and entry into force.[180]

There is no doubt that the complexity of the amendment process, besides the possible implications for other articles of the Chicago Convention[181] are bound to discourage any such initiative unless an amendment would be perceived as necessary and urgent by a broad spectrum of States Party to the Convention. In that sense, the Panel of Experts could not have probably decided otherwise than it did.

To conclude this section, it is appropriate to note that the Panel of Experts has completed its work on non-scheduled regulation in a somewhat perfunctory manner. However, the diversity of national policies and objectives made this almot inevitable. Additionally its earlier work

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179. "The Story of the International Civil Aviation Organization", Memorandum on ICAO at 12 (1981); ATRP/5-WP/7, prepared by ICAO Secretariat at 2 (2/7/81).

180. ATRP/5-WP/7, id. at 2.

181. In fact, an examination of the Convention reveals that 18 more articles of the Convention may need to be reviewed if such an amendment is introduced. Id. at 2-3.

on the possible re-classification of "programmed" charters as scheduled has not enjoyed any significant practical acceptance. Nonetheless, within the scope of work feasible on non-scheduled regulation, a number of loose ends remain.

PRELIMINARY CONCLUSION

There is no question about the public need for both scheduled and non-scheduled operations. Scheduled air services provide the aviation consumer with regular and dependable schedules, flexibility and worldwide routes. Non-scheduled services exploit the efficiency of plane-load movement to capture the price-elastic traffic and expand passenger and cargo markets. Therefore, both types of service are needed. The issues are the balance between the interests of the operators of the two services, the public and the government on the one hand, and the harmonization of divergent national policies on the other. It can, however, be argued that the uncertainty now surrounding international air transport regulatory regime encourages States to retain complete discretion of action which is clearly regarded as better than any uniformity. New principles and ideas should, therefore, be sought and explored for better identifying and understanding the nature of international air transport in order to find the appropriate solutions to the

existing ambiguity.

In the writer's opinion, it is necessary to devise a scheme of traffic regulation that creates a balanced air transportation system which serves all segments of the public. However, one should admit that this is more easily said than done, but all of the momentum of the past few years is apparently taking the industry in this direction. The following are the main tasks that have to be addressed to create such a scheme:

(a) Charter activity must be regulated but not sacrificed to protectionism. All the regulations should aim toward an ever increasing qualification of air service on demand, in terms of efficiency and security, in order to guard the rights of the growing numbers of leisure travellers. This may be done if charter air services would be regulated by multilateral regional agreements, such as in Europe (the 1956 Paris Agreement) or the ASEAN (the 1971 Manila Agreement).[182]

(b) Bringing prices in line with costs. Since charter air transport is based on the costs of planeload operations, rate control should be unnecessary. However, when scheduled carriers dump excess capacity in some markets or when scheduled services are themselves operated at

182. See supra (footnotes 27 and 31) of this Chapter.

uneconomic levels, some action by governments to preclude these destructive practices is essential.

(c) Shaping capacity to meet demand. If the non-scheduled traffic is regulated as clarified above, its capacity should automatically rise to the level of public demand. On the scheduled side, however, some external control is necessary to assure that the capacity does not exceed the level of service that is actually required. This could take the form of pooling and/or capacity agreements.[183] Today the excess capacity situation in scheduled service is one of the basic problems confronting the scheduled air transport industry. Empty seats and excessive schedules prompt scheduled carriers to attempt to fill those seats at any cost. Thus the uneconomic systems come into being, such as APEX, Part Charters, and others.

(d) Redefinition of the terms ("scheduled" and "non-scheduled") to enable the nations decide the level of scheduled and non-scheduled air services that are really necessary to serve the public interest.

It is not feasible to regulate one extreme of air transport (scheduled services) while leaving the other (non-scheduled services) under unilateral supervision or

183. See infra "Preliminary Conclusion", Chapter VI (footnote 187).

uncontrolled. States have a responsibility to design a coherent and satisfactory framework for the regulation of all international air services. Failure to meet this responsibility would mean that governments will be "faced with the possibility of rate wars, cut-throat competition between the various airlines, increasing subsidies, inter-governmental antagonism and chaotic commercial conditions at the very moment when peaceful co-operation and harmonious development are absolutely vital".[184] These words were once used by Sir William Hildred to describe the situation in which governments and their airlines found themselves in 1945. They are every bit as apposite today.

184. Hildred, Statement before the Anti-Trust Sub-Committee of the Judicial Committee of the US House of Representatives (1956).

CHAPTER VI

THE REGULATION OF CAPACITY: EVOLUTION AND PERSPECTIVES

SECTION I - THE BERMUDA CAPACITY PRINCIPLES

Capacity Determination According to Bermuda I

The distinguishing characteristic of the Bermuda I system of regulation is that, in place of any formula or other method for determining capacity, it substitutes a sweeping right for each airline to institute capacity in its own discretion subject only to ex post facto action if a government complains that the capacity being offered violates certain general principles. In other words, it places no outright restrictions on capacity and leaves its determination to the aviation industry in accordance with "deliberately vague" guidelines.

The "Final Act" of the Bermuda Civil Aviation Conference[1] defined the guidelines which were to govern the operation of air services under the Agreement. Basic-

1. For the history of Bermuda Conference and its main results, see supra, Chapter II, Section II.

ally these guidelines or principles (better known as the Bermuda I principles) were intended to regulate competition between the air transport services of the two contracting Parties.[2] Four standards are prescribed in the principles. These are in essence regarded as the most important and, when incorporated into an agreement, that agreement is classified as Bermuda-type agreement. However, due to the fact that these principles were ambiguously drafted, the writer will discuss them according to the interpretation of the original drafters of Bermuda I.

The first standard provides that air service facilities available to the travelling public must bear a close relationship to the requirements of the public for air transport.[3] This requirement is usually explained as an obligation for the airlines to operate at a "reasonable load factor", or not to operate at unnecessarily low load factors on certain routes merely for competitive advantage.[4] In modern terms it can be seen as an injunction to the Parties

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2. Gertler, "Bilateral Air Transport Agreements: Non-Bermuda Reflections", 42 J. Air L. & Com. at 803 (1976)

3. See Para. 3 of the Final Act of the Bermuda Conference, 60 STAT 1499, T.I.A.S. No. 1507 (1946).

4. Cheng, The Law of International Air Transport at 412-413 (1962).

to avoid overcapacity.[5] In this respect, one should note that it was not permitted to operate an air service with excessive capacity without economic justification.[6] Apparently, to operate at 65-70% of an aircraft capacity is considered justifiable.[7]

The second standard requires that there should be a "fair and equal opportunity" for the airlines to operate on the agreed air routes.[8] This pertains to the opportunity of the designated carriers of both contracting Parties to operate on the specified routes to which they have been designated. The opportunity shall be "fair" and "equal". However, since this guideline mentions nothing about an equality of traffic, revenue or in the number of carriers,[9] one can say that it is rather a non-

5. See Wassenbergh, Public International Air Transportation Law in a New Era at 31 (1976).

6. "The capacity to be put on any air route should be related to the traffic demands - thereby eliminating uneconomic practice", see Masefield, "Anglo-American Civil Aviation", Air Affairs at 319 (1947).

7. See British Air Transport in the Seventies (The Edwards Report) at 57 (1969).

8. Para. 4 of the Final Act.

9. McCarroll, "The Bermuda Capacity Clauses in the Jet Age", 29 J. Air L. & Com. at 118-119 (1963).

discrimination principle which calls for "equality of opportunity to compete" on the routes according to fair competitive practices.[10]

The third standard obliges the airlines of one country to take into account the interests of the airlines of the other, so as not to affect unduly each other's services.[11] This requirement is to govern the relations between air carriers competing on trunk services. The interests of the designated airlines of both contracting Parties shall therefore be considered by the designated carriers of either Party while providing operations of the trunk services on all or part of the same routes. This thereby ensures that the services of either designated airline are not unduly affected.

In fact, the above-mentioned second and third standards should be read together. While the second guideline seeks fair competition, the third one indicates a certain control of competition in the sense that no airline may strive for a monopoly or domination over the other by means of purely destructive practices. In other words:

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10. This interpretation becomes obvious in the light of Bermuda II and the liberal bilaterals where the word "operate" is replaced by the word "compete", see infra Section II.

11. Para. 5 of the Final Act.

"competition but no-cut-throat competition".[12] As to "fair and equal opportunity" clause, it seemingly means that even though one designated airline may be weaker than the other, it is still entitled to an equal right to operate like the strong carrier and is to be given every opportunity to perform its assigned role.[13] An appeal process was provided in the Bermuda I Agreement, whereby the Parties could apply to ICAO for an advisory opinion in order to determine whether certain practices were limiting fair and equal opportunity or were destructive unfair trade practices.[14] Unfortunately, this appeal process remained a dead letter and thus the opportunity was lost for developing fair competition rules, on a case by case basis, in international civil aviation.

Before examining the fourth guideline, it is worth mentioning that Baker (the Chairman of the American delegation at Bermuda), in discussing the first three standards of Bermuda I, contended that their principal thrust was to prevent "unfair trade practices" by the respective carriers.

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12. Adriani, "The Bermuda Capacity Clauses", 22 J. Air L. & Com. at 406 (1955).

13. Baker, "The Bermuda Plan as the Basis for a Multilateral Agreement", Lecture delivered to McGill University, Montreal at 2 (1948).

14. See Article 9 of Bermuda I.

Moreover, the nexus between the needs of the public and capacity was introduced as a stopgap measure to prevent either Party through subsidy, from flooding the market with excess capacity and thereby undermining the financial stability of its competition. In order to refute the argument that interpreters had given the fair and equal clause, he concluded that:

> "There was certainly no intention that free and equal opportunity to compete on a fair basis and the right to do half the business were as concepts even distantly related."[15]

The fourth standard indicates that the primary objective of the provision of capacity is to meet traffic demands between the country of nationality of the air carrier and the country of ultimate destination of the traffic, with subsidiary fifth freedom traffic capacity related to (a) traffic requirements between the country of origin and the country of destination of air traffic; (b) requirements of through airline operation; and (c) traffic requirements of the area through which the airlines pass after taking account of local and regional services.[16] This guideline is apparently one of the most important and at the same time the most controversial one. In the words of Baker, this standard was deliberately written as a

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15. Baker, op. cit., note 13, at 10.

16. Para. 6 of the Final Act.

"somewhat elastic statement".[17] A distinction is made in the guideline between "primary justification" and "secondary justification" traffic.

The primary objective is to provide adequate air transport for the traffic of the country of origin of the aircraft and the country of destination of the traffic, i.e. the third and fourth freedom traffic or primary justification traffic. The secondary traffic consists of fifth freedom traffic on the specified route.[18] The "Final Act" of the Bermuda Agreement, however, made it very clear that "the capacity for the carriage of fifth freedom should have a primary effect on third and fourth freedom traffic".[19]

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17. Baker, op. cit., note 13, at 12; Article 11 (Para. 3) of Bermuda II.

18. See Cheng, "Beyond Bermuda", in Matte Ed., International Air Transport: Law, Organization and Policies for the Future at 93 (1976). For a good clarification on the various freedoms of the air, see Haanappel, Pricing and Capacity Determination in International Air Transport at 11-13, 32-33 (1984). Also, one has to admit that the problem of sixth freedom traffic has given rise to many differing and conflicting opinions and interpretations. Occasionally this freedom has specifically been provided for in bilateral agreements, i.e. in some liberal bilaterals recently concluded by the U.S.

19. Diamond, "The Bermuda Agreement Revisited: A Look at the Past, Present and Future of Bilateral Air Transport Agreements", 4 J. Air L. & Com. at 447 (1975).

But neither this Act nor any other part of the Agreement offered a concrete answer to the quantity of capacity for fifth freedom traffic allowed in relation to the quantity of capacity for third and fourth freedom traffic. It appears therefore that it was not the intention of the founding fathers of Bermuda I to set up a fixed ratio between capacity for third and fourth freedom on the one hand and capacity for fifth freedom on the other.[20] Many countries, nevertheless, correlate the amount of fifth freedom traffic allowed to be carried to/from the point on the route in their territory, to the amount of homeland traffic to/from that point.[21] One should also note that the above-mentioned criterion of "through airline operation" refers to the need to make long-haul air services economically viable by allowing airlines to pick up extra traffic on fifth freedom segments along the route.[22] Finally, the analogy of "local and regional services" does not mean that fifth freedom traffic should be carried only when such regional services are inadequate. This interpretation would undoubtedly endanger the standard of "fair and equal opportunity" by making the operations of one airline dependent on the

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20. See Adriani, op. cit., note 12, at 408.

21. Wassenbergh, op. cit., note 5, at 42.

22. See McCaroll, op. cit., note 9, at 120.

activities of another airline.[23]

All of the above-mentioned Bermuda I capacity principles should be read together with Article 9 of the Agreement which provides the jurisdictional basis for ex post facto review of airline practices. In short, if after operating for a period it is found that one airline is offering a far greater number of seats than can be justified by the traffic offering between the two countries, "that carrier can be required to show cause why his capacity or frequency should not be reduced".[24] Future capacity problems would then be solved via consultation between the governments concerned. This applies not only to the amount of fifth freedom traffic but is also applicable to third and fourth freedom capacity.[25]

Procedurally this consultative mechanism allows the market to be tested before an attempt to limit capacity can

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23. See Wassenbergh, Post-War International Civil Aviation Policy and the Law of the Air at 57 (1962). In fact, however, this criterion of local services has lost much of its meaning nowadays.

24. Azzie, "Negotiations and Implementations of Bilateral Air Agreements", Lecture delivered to McGill University, Montreal at 26 (1967 - revised 1973).

25. Cooper, "The Bermuda Plan: World Pattern for Air Transport", in Vlasic Ed., Explorations in Aerospace Law at 391 (1968).

be instituted by the joint action of the contracting Parties. If the two countries ultimately fail to reach an accord, the dispute comes again within the scope of Article 9 of Bermuda I which provides for referral to ICAO for an advisory report. This procedure, however, was subsequently changed in the United States-Italy bilateral of 1948 which required the creation of an arbitration tribunal of three judges, one selected by each Party and the third by mutual agreement.[26] Failure to agree upon a third judge within one month would permit the President of ICAO Council to designate this third arbitrator. This arbitration clause has become the model for subsequent bilaterals replacing the Bermuda clause.

Deviations from Bermuda I Capacity Principles

Since its inception, capacity determination has been the major bone of contention between the United States and the United Kingdom. It is not only because of its intrinsic importance, but also because of the controversy which surrounded it during and after the Bermuda Conference. One of the polemical aspects of Bermuda capacity principles

26. Air Transport Agreement between the U.S.A. and the Government of Italy, T.I.A.S. No. 1902, 73 UNTS 113 (1948).

had been their vague drafting. This can be explained by the fact that they were largely the result of a compromise between two opposing philosophies, i.e. there was a strong desire for freedom of commercial activity on the American side, while the British had an equally strong desire to protect their national interests.[27]

This vague drafting in the capacity clause of the Agreement stands practically on its own without any supplemental or corrective provisions[28] and has been subject to different interpretations and methods of application. Adriani supporting this vagueness considered it a useful potential creating possibilities for protection as well as necessary amount of freedom.[29] Some attributed this vague framing of Bermuda principles to be an act of wisdom, having a sound basis of reasonableness.[30] Other opinions, however, had taken a contrary view. In this respect, Lowenfeld appears to be correct when observing that the drafters were evidently more anxious to achieve agreement in

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27. For more details, see supra, Chapter II, Section II.

28. Except, of course, for cases when Bermuda language is used, but the bilateral capacity regime includes also an additional and predominant predetermination component.

29. Adriani, op. cit., note 12, at 406.

30. Id.; Diamond, op. cit., note 19, at 449.

the period allotted for the Conference than they were to avoid all potential controversy in the future.[31]

Whatever may have been the intent, the adequacy of Bermuda clauses on capacity seems to be increasingly called into question.[32] They had been criticized for the general and contradictory way in which they were couched, making them unsatisfactory from a legal point of view and resulting in little restriction on capacity or frequency.[33] A good illustration of the vagueness of the Bermuda I capacity principles can be found in a recent arbitration between Ireland and Belgium, dealing with the Bermuda I type capacity clause in the 1955 Belgian-Irish bilateral.[34]

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31. Lowenfeld, "CAB v. KLM: Bermuda at Bay", 31 Air Law at 5 (1975).

32. Doty, "Curtis Worsen Payments Deficits", Aviation Week & Space Tech. at 25 (Oct. 30, 1972); Thornton, "Power to Spare: A Shift in the International Airline Equation", 36 J. Air L. & Com. at 37 (1970).

33. Thornton, Internatinal Airlines and Policies, A Study in Adaptation to Change at 37 (1970).

34. This is an excellent example that shows how a confidential exchange of notes impacts upon fifth freedom traffic rights, and how the pooling agreement between the designated airlines, Aer Lingus and Sabena, impacts on capacity determination on third and fourth freedom routes. See Naveau, "Away from Bermuda", 8 Air Law at 50 et seq. (1983); Merckx, "The Belgium-Ireland Air Transport Agreement Arbitration", Belgium Review of International Law at

It was generally felt, however, that Bermuda principles would develop a kind of "common law" of capacity determination in international civil aviation. Some anticipated that if a sufficient number of nations used the Bermuda guidelines in their bilaterals, a system would grow wherein there would be so much uniformity that the drafting of a multilateral agreement would be facilitated.[35] Nevertheless, these principles were never accepted by other States on a multilateral basis. Instead, they are reproduced in the vast majority of bilateral air transport agreements. But the general way in which they are drafted permits both a liberal and a more conservative interpretation. In this context, one should note that the Bermuda principles work best in conditions where the airlines of both Parties are of approximately equal commercial strengths,[36] and thereby can compete with each other. While in situations where one airline is comparatively

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668 (1985),

35. See, e.g., Wheatcroft, Air Transport Policy at 70 (1964); O'Connor, Economic Regulation of the World's Airlines at 48 et seq. (1971).

36. See Loy, "Bilateral Air Transport Agreements: Some Problems of Finding a Fair Route Exchange", in McWhinney & Bradley Eds., The Freedom of the Air at 176 (1968); Diamond, op. cit., note 19, at 463.

weaker in competitive position than the other, the Bermuda system encounters many difficulties.[37] It has been claimed that no country is willing to accept a share of the traffic on a major route which would be less than about 80% of its traffic generating capability. Each nation is likely hence to begin imposing restrictions when its share of the traffic drops below that margin.[38]

The fact is that newly emerged nations endeavour to protect their national carriers by securing them a reasonable share of the traffic on the routes which they operate. In doing so, such nations are not inclined to accept the liberal interpretation of the Bermuda principles. Seemingly, the main reason behind preferring tighter economic regulation is that the twenty per cent of air traffic available for competitive capture under a normal Bermuda would go to the stronger air carrier.[39] This is because the freedom of the air proposed by the United States under the

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37. Stoffel, "American Bilateral Air Transport Agreements on the Threshold of the Jet Transport Age", 26 J. Air L. & Com. at 129 (1959).

38. See Diamond, op. cit., note 19, at 460 et seq.; Thornton, op. cit., note 33, at 35-39.

39. King, "Civil Aviation Agreements of the People's Republic of China", in 14 Harv. Int'l L.J. at 334-335 (1973).

Bermuda regime was a special kind of freedom, which had been interpreted by the weak States as the freedom of the stronger and hence was felt the need for a protective posture. Wassenbergh put this matter into philosophical perspective when he stated: "Man is as equal as he makes himself. The problem is the regulation of inequality".[40]

The above analysis may be said to constitute the major reasons for the growing trend toward restrictionism, which in practice has meant the restrictive application of the Bermuda principles. Regarding the means of applying these restrictions, it should always be remembered that restrictions which go further than those in Bermuda clauses, are often embodied in secret letters or notes (i.e. Memoranda of Understanding) between the aeronautical authorities of the nations.[41] This same secretiveness applies to consultations between the Parties over restrictions which have been imposed.[42] Yet it is also true that many of

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40. Wassenbergh, Aspects of Air Law and Civil Air Policy in the Seventies at xii (1970).

41. For further detail on the impact of such Memoranda, see, e.g., Moursy, International Air Transport and the Chicago Convention, unpublished thesis, McGill University, Montreal at 178 et seq. (1983); Gardner, "U.K. Air Services Agreemens 1970-1980", 7 Air Law at 2 et seq. (1982).

42. See Deak, "The Balance-Sheet of Bilateralism", in

these restrictions do become generally known.[43]

The restrictions imposed by the governments may take various forms. They may allow only limited number of foreign airlines to operate into their territory, limit the granting of routes to foreign carriers, restrict the number of passengers that may be carried on routes or route segments and may restrict the charter flights operations performed by foreign airlines. Limitations on the number of frequencies, days and hours foreign airlines may operate can also be imposed. Furthermore, many governments interpret the "equal opportunity" clause of the Bermuda Agreement in such a way as to secure the right of their own airlines to a half share of the traffic on the routes exchanged. Other governments prevent foreign carriers from offering more capacity than their own carriers on the routes agreed.[44] In addition, restrictions on the operations of all cargo services or on the amount of freight to be carried are not unusual.[45] Even the type of equipment to be used can be

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McWhinney & Bradley Eds., op. cit., note 36, at 165.

43. See Doty, op. cit., note 32, at 20-21; CAB Information Statement, U.S. Dept. of State Press Release No. 236 (May 6, 1975).

44. See Wassenbergh, op. cit., note 40, at 29.

45. This comes close to the Ferreira doctrine which would

restricted.

It is also worth mentioning that often the object of restrictions is to shift the regulatory framework of the bilateral agreement from Bermuda system and closer to a "predetermination" scheme.[46] Moreover, the effect of predetermination can also be reached by means of pooling agreements between airlines, which may be required or permitted in bilateral air transport agreements.[47] Cheng has correctly made the point that "when pooling or similar arrangements exist, the effect is to reintroduce predetermination by the airlines through a back door, with the proviso that this type of predetermination is entirely voluntary".[48]

Capacity control through a system of governmental predetermination and/or through pooling between airlines severely limits free competition in international air

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serve as the basis for bilateral agreements concluded by Argentina. For more information, see De Arechaga, "South American Attitudes Towards the Regulation of International Air Transportation", in McWhinney & Bradley Eds., op. cit., note 36, at 70 et seq.

46. For full details on this method of capacity regulation, see infra Section III, "Towards Predetermination of Capacity".

47. Id.

48. Cheng, op. cit., note 4, at 443.

transport. This is why the United States has heretofore vigorously resisted such predetermintion schemes. The European States, on the contrary, began to stress "equality of opportunity" when they recognized the American's total antagonism toward predetermination, and the Europeans interpreted this equality to mean reciprocity in routes on a route-for-route basis and reciprocity in traffic centers served.[49] In this context, however, one should also note that although capacity control, tariff control and pooling have very often been combined in Europe, EEC and ECAC have been engaged in studies on the liberalization of air transport regulation.[50]

The introduction of jet aircraft tremendously increased the capacity and frequency potential of the aviation industry beyond market demand. This factor, among other things,[51] caused a new series of attacks by the protectionist nations against the Bermuda format. The early

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49. See, e.g., Jones, "The Equation of Aviation Policy", 27 J. Air L. & Com. at 234 (1960); Loy, op. cit., note 36, at 177-178; Brandel, "Recent Trends in European Air Transport Law and Policy with Reference to Routes", unpublished thesis, McGill University, Montreal (1984).

50. See supra, Chapter III, Section IV.

51. See supra, Chapter II, Section III (footnotes 52, 56).

sixties found the United States embroiled in controversies with several countries who asserted that Bermuda's ambiguous language permitted unilateral restrictions on capacity.[52]

Restrictive measures were even taken by the United States itself. In an effort to improve the economic viability of the American flag carriers whose share of international traffic had been declining over the years, the CAB enacted Part 213 of the Economic Regulations in June 1970.[53] It empowered the CAB to request any foreign carrier to file: traffic data disclosing the nature and extent of its operations; its present schedules; its proposed schedules at least 30 days in advance of inauguration; and the equipment employed or to be employed.[54]

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52. See, e.g., U.S.-Italian dispute which arose when Pan Am introduced all Cargo Jet flights and the Italian government rejected its schedules, 4 Int'l Legal Materials at 974 (1965); Bradley, "International Air Cargo Services: The Italy-U.S.A. Air Transport Agreement Arbitration", 12 McGill Law Journal at 312 (1966).

53. The new economic regulation entitled "Terms, Conditions and Limitations of Foreign Air Carrier Permits". See 14 CFR, Para. 213.1-6.

54. 14 CFR, Para. 213.2-3(b); Macdevitt, "The Triangle Claims Another Victim: A Watery Grave for the Original Bermuda Agreement Principles", 7 Den. J. Int'l L. & Pol'y at 239 et seq. (1978).

The carrier might continue to operate existing schedules or might inaugurate new services unless the Board, with or without hearing but subject to a stay or disapproval of the President,[55] notified the carrier that all or any part of the carrier's existing or proposed service was contrary to the public interest or applicable law. In addition, the Board might issue a second Order to the foreign carrier requiring it to refrain from implementing a proposed schedule or discontinue an existing schedule within 30 days. If the foreign carrier was operating pursuant to a permit granted under a bilateral agreement, the Board has also to find that the foreign government or its aeronautical authority over the objections of the United States took action impairing, limiting, terminating or denying operating rights to any American carrier designated according to the bilateral agreement.

On July 12, 1974, the CAB adopted an amendment to Part 213 which enlarged its existing powers. The new amendment covered the situation where the action or inaction of the foreign government fell short of direct restriction of rights in contravention of the bilateral air transport

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55. For an explanation of the President's role in CAB proceedings affecting international aviation, see Lowenfeld, Aviation Law, Second Edition at 533 et seq. (1981).

agreement. The Board could now take appropriate action when foreign governments had, over the objections of the American government:

> "otherwise denied or failed to prevent the denial of, in whole or in part, the fair and equal opportunity to exercise the operating rights, provided for in such air transport agreement, of any U.S. air carrier designed thereunder with respect to flight operations to, from, through, or over the territory of such foreign government."[56]

It is interesting to note that the first attack under this novel approach to Part 213 was launched against KLM with demands that the carrier reduce its available capacity by 50%.[57] According to the American view, the Dutch airline carried excessive sixth freedom traffic between the United States and The Netherlands, thus depriving American carriers of a fair and equal opportunity to compete.[58] As KLM declined to comply with the Order to file its schedules, the issue was raised to the diplomatic

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56. 14 CFR, Para. 213.3(d).

57. See Aviation Week & Space Tech. at 23 (Nov. 18, 1974).

58. For a good illustration on the sixth freedom according to both the American and the Dutch interpretations, see O'Connor, An Introduction to Airline Economics at 49-50 (1982).

level, but the dispute remained largely unresolved.[59]

Such move in the American philosophy was viewed in Europe as a test case as to how far the United States was prepared to go on the road to protectionism. With the State Department expected to make similar demands upon the Swiss, Belgian, Scandinavian and French[60] carriers, the United States was now perceived as the leading advocate of restrictionism.

In fact, the authority of the CAB to promulgate the new economic regulation was bitterly contested by numerous foreign air carriers, all of whom filed petitions for reconsideration claiming that the CAB lacked the competency to enact Part 213.[61] A careful analysis of Part 213,

59. See Lowenfeld, op. cit., note 31, at 14 et seq.; Haanappel, op. cit., note 18, at 43, 45.

60. A more interesting issue than the Dutch case is the U.S.-France Air Services Award of 1978 in which the legality of Part 213 under international law was discussed. See, for a detailed analysis, "U.S.-France Air Services Award, Case Concerning the Air Services Agreement of 27 March 1946", in 54 Int'l L. Rep. at 303 et seq. (1979).

61. These petitions, which based their arguments on sections 1102 and 801 of the Act, were filed by Irish International Airlines, British Overseas Airways Corporation, British West Indian Airways, Lufthansa, KLM, Sabena, SAS, El Al, Iberia Airlines and Varig. See Docket 12063, "Foreign Permit Investigation", 34 CAB 837.

initiated by the United States to counter the so-called coercion by other countries, revealed that the American response was inappropriate and annoying to other nations. Instead it was believed, alternative procedures would have been less abrasive, such as amending the existing bilateral agreements.[62]

Capacity Control Pursuant to Bermuda II

The capacity regulation, particularly on the North Atlantic routes, was one of the fundamental targets of the United Kingdom in seeking the Bermuda II Agreement.[63] The British comprehended that excess capacity was simply leading to loss for both customers having to pay higher fares and for the air carriers flying the empty seats. At the outset of the negotiations leading up to the conclusion of Bermuda II, the United Kingdom therefore aimed at a new compromise based upon a 50-50 sharing of air traffic between American and British carriers. Although the United Kingdom was unsuccessful in this attempt, the capacity clauses in

62. Other measures include the International Air Transportation Fair Competitive Practices Act of 1974, see infra Section II.

63. See supra, Chapter II, Section IV (footnotes 58, 60).

Bermuda II are certainly more restrictive than those found in Bermuda I.[64]

To understand the capacity determination in Bermuda II, one has to read Article 11 in conjunction with Annex 2 to the Agreement. Article 11 of Bermuda II repeats the ambiguous capacity principles of Bermuda I, subject to some changes. Such modifications take account of the changed aviation environment, in particular the increased public demand for low-cost services, and the need for efficient services (the excess capacity and energy conservation problem). Article 11 also embodies the provision of a carrier already serving a route marking time for a period to allow an inaugurating competitor airline of the other country to match its frequencies. This provision was particularly essential in relation to those routes - such as San Francisco, Seattle, Atlanta and Dallas - where a British operator would be coming on to the routes after their initial exploitation by an American carrier.[65]

The mutual commitment to fair competition is found in paragraph 1 of Article 11, which stipulates that:

> "The designated airline or airlines of one contracting Party shall have a fair and equal opportunity to compete with the

64. Id. (footnote 68).

65. See Shovelton, "Bermuda 2: A Discussion of Its Implication", Aeronautical J. at 53 (Feb. 1978).

designated airline or airlines of the other contracting Party.

It is worth recalling that in the original Bermuda I, the competition basis was "fair and equal opportunity to operate". The word "operate" has now become "compete" in Bermuda II, and also no mention of routes is made.[66] Such modification is not illustrated but direction may be to ensure that all designated carriers can compete on an equal basis, i.e. a move towards the British negotiating stance of "equal competition". There are three important requirements, however, patterned to enhance fair and equal competitive opportunity. First, there is a restraint on the capacity of an incumbent airline, when a new carrier enters a market, for a period of time not to exceed two years nor to extend beyond the time when the frequency of the inaugurating carrier matches that of the incumbent.[67] Secondly, to counter airline actions leading to excess capacity, a special mechanism for capacity review on the North Atlantic is included.[68] Thirdly, to avoid future confrontations over capacity, neither of the Parties would unilaterally restrict operations.[69]

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66. See supra note 8.

67. Article 11, Para. 2 of Bermuda II.

68. See infra (footnotes 73, 77 to 82).

69. "Except according to the terms of this Agreement or by

It is significant to note that paragraph 4 of Article 11 is now much more specific than that found in Bermuda I,[70] in that it states that capacity and frequency must be related to "all categories of public demand" (thereby including the low-cost category of transport),[71] so as to provide adequate service to the public and hence permit the "reasonable development of routes and viable airline operations". In addition, reference is made to "efficiency of operation", in that capacity should be provided at levels appropriate to accommodate the traffic at load factors consistent with tariffs (which are based on criteria enumerated in the Agreement).

In markets other than North Atlantic combination air services, the ex post facto control of capacity that mentioned in Bermuda I is retained, "except that, where frequency or capacity limitations are already provided for a route specified", no additional limitations on capacity are

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such uniform conditions as may be contemplated by the Convention". Article 11, Para. (6).

70. See supra note 3.

71. This implies, in principle, the possibility of coordinating the capacity of charter operations with that of scheduled services; in principle, therefore, it affords a basis for capacity regulation of charters. However, according to Annex 4 (Para. 2) dealing with charters, one can find that Article 11 (Para. 4) does not apply to charter operations.

permitted.[72]

Although unilateral restriction of capacity is prohibited, the Bermuda II Agreement contains complex and elaborate procedures for reviewing and controlling the capacity of North Atlantic operations. This may be explained by the fact that the new Agreement is a product of excess capacity; competition of charter and scheduled services; disorder in airline pricing; the introduction of totally new service formulae (Concorde, Laker Skytrain, etc.). Since these problems are mainly related to North Atlantic routes, a new capacity regulation system was introduced in Annex 2 to the Agreement for combination air services on the North Atlantic. The purpose of the new procedures is:

> "to provide a consultative process to deal with cases of excess provisions of capacity, while ensuring that designated airlines retain adequate scope for managerial initiative in establishing schedules and that the overall market share achieved by each designated airline will depend upon passenger choice rather than the operation of any formula or limitation mechanism."[73]

The comments of British and American officials, after the signing of Bermuda II, as to the purpose of this "consultative process" reflect a conflict of viewpoint.

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72. See Article 11, Para. 5 of Bermuda II.

73. See Annex 2, Para. 2. This may be understood as a guideline in addition to the principle of Article 11 on "fair competition".

Edmund Dell, the British Secretary of State for Trade, evaluated the process as more of a capacity limitation device in and of itself. According to him, this mechanism is "designed to reduce the waste of fuel and other resources that results from flying too many empty seats...".[74] On the other hand, the Chairman of the American delegation, Alan Boyd, found the new regulation as "no more than a consultative process".[75] Other United States negotiators viewed the clause as putting pressure on capacity rather than dictating market shares.[76]

The key provisions for controlling capacity on the North Atlantic are paragraphs (3) to (6) of Annex 2 which set forth a capacity regulation mechanism based upon timely advance filing of capacity schedules between the two Parties. In sum, it involves:

(1) at least one hundred and eighty days prior to traffic season:[77] filing of capacity schedules with the other Party. The summer season includes the period April 1

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74. See Traffic World at 91 (July 4, 1977).

75. Cited in Barnard, "U.S., UK Sign New Air Services Pact: Unlikely to Much Alter Present Imbalance", in J. Com. (N.Y.) at 1 Col. 1 (Jun. 23, 1977).

76. See Business Week at 32 (May 9, 1977).

77. Date of proposed entry into force of new tariff schedules.

through October 31. The winter traffic season begins November 1 and continues through March 31;[78]

(2) at least one hundred and fifty days prior: notification of any objections.[79] In this context, it should be noted that if one Party proposes an increase in frequency, the following requirements must be taken into account:

(a) the public requirement for adequate capacity;

(b) the need to avoid uneconomic excess capacity;

(c) the development of routes and services;

(d) the need for viable airline operations; and

(e) the capacity offered by airlines of third countries between the points in question;[80]

(3) at least one hundred and twenty days prior: justification of proposed capacity schedule, or modifications;

(4) at least ninety days prior: notification of objections against 3 (above) and, where necessary, consultations;[81]

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78. See Para. 13 of Annex 2.

79. Id. Para. 4.

80. Id.

81. See Paras. 4 and 5 of Annex 2.

(5) seventy-five days prior: in case of failure to reach agreement, a so-called "fallback" mechanism comes into force whereby each carrier in question is entitled to a maximum capacity specified in paragraph 6(a) and (b) of Annex 2, based upon the previous season's capacity and increase according to an average forecast. In addition, there is also provision for minimum baselines and minimum increase.[82] One should note, however, that this "fallback mechanism" does not apply to an airline inaugurating service on a route already served by an airline or airlines of the other Party.[83] Finally, Concorde operations between the two Parties are not subject to the provisions of this Annex.[84]

Some often overlooked restrictions on capacity in Bermuda II are the provisions dealing with carrier designation which limit the number of airlines operating on the North Atlantic.[85] This limitation has been considerably liberalized in one of the recent amendments to the Agree-

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82. Id. Para. 6.

83. Id. Para. 7.

84. This leads to the conclusion that the other parts of the Agreement do apply to Concorde services, including the other Annexes.

85. See supra, Chapter II, Section IV (footnote 69).

ment.[86] However, this amendment did not touch upon the capacity issue.

As a conclusion to this section, it may be noted that, in effect, North Atlantic operations between the United States and the United Kingdom have almost become subject to a system which stops just short of involving predetermination.[87] Even if the system is very flexible and allows the taking into account of various capacity requirements, it nevertheless departs from the liberal concept of capacity regulation under Bermuda I. The general trend in international air tranpsort towards more restrictive capacity regulation[88] and the economic problems on the North Atlantic routes were largely responsible for this shift of regulatory philosophy.

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86. Id., Section V (footnotes 107 and 108).

87. The notification and consultation requirements prior to the proposed effective date of the tariff schedules amount almost to predetermination because objections on either side lead almost automatically to the necessity of reaching an agreement involving the predetermination of capacity. It is thus a sort of "optional predetermination". See also supra note 46.

88. See infra Section III of this Chapter.

SECTION II - FREE DETERMINATION OF CAPACITY, FREQUENCY AND TYPES OF AIRCRAFT

Analysis of the New Liberal Method

The free determination of capacity method relies upon competitive pricing and scheduling responses of individual air carriers to the forces of the marketplace. In other words, no government may control capacity, frequency or such operational matters as change of gauge from a large aircraft to one or more smaller planes. This means that air carriers are completely free to set their own capacity, frequency of flights and to use aircraft without direct intervention by governments.

While abrogating their direct control, governments may indirectly influence airlines' determination of capacity through designation, pricing, charters and possible consultation. It is recognized, however, that the method may be less effective where the free play of market forces is impaired or inhibited.[89]

At the 1980 Air Transport Conference, the United States presented a Working Paper in which it explained the

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89. In respect of distribution networks, fuel availability, currency restrictions.

free determination of capacity method.[90] In sum, this method is based on the following premises:

(a) Responsibility for airline management is entirely a matter for the carriers without governmental interference, which should be the rule in a free economy.

(b) Market forces are relied upon to bring all necessary adjustments.

(c) Competition between scheduled and non-scheduled airlines should be unrestricted which excludes unilateral national regulation of either category.

(d) Demand corresponding to capacity should be a function of price, so that there can be flexibility in the provision of capacity (e.g. to solve peak and through traffic problems).

(e) Competition should provide the best service for the public (no agreements between airlines or limit on the designation of carriers).

In fact, among the many complexities in developing a totally new form of bilateral arrangement was the dimension added by including charter air services beside scheduled operations. Thus, while the basic capacity provision is so simple as to be almost non-existent,[91] the more

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90. In this paper, the U.S. explained in detail the premises, merits and shortcomings of the free determination method. See AT Conf/2-WP/7, "Regulation of Capacity" (17/12/79).

91. The liberal bilaterals in fact do not include a capacity clause but rather provisions for ensuring

general issue of competition under the bilateral air transport agreements required careful treatment. The American Policy of 1978, in this area, aimed at:

> "Expansion of scheduled services through elimination of restrictions on capacity, frequency and route operating rights.... We will seek to increase the freedom of airlines from capacity and frequency restrictions. We will also work to maintain or increase the route and operating rights of our airlines where such actions improve international route systems and offer the consumer more convenient and efficient air transportation."[92]

The capacity free determination provision is based on the language of the "fair competition" clauses which gained recognition in the liberal bilateral agreements. It is interesting to compare such clauses with the corresponding capacity provisions found in the Bermuda I Agreement. The first and main variation under liberal bilaterals is that no standards of any kind exist to limit the level of total capacity. There is, instead, an interdiction against unilateral capacity limitation of the other Party's desig-

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"fair competition". This is consistent with an uncontrolled designation scheme, the two issues being closely connected.

92. U.S. Policy for the Conduct of International Air Transportation Negotiations, August 21, 1978, 14 Weekly Composition of Presidential Documents at 2-3. The limitation to "scheduled" appears to be based on the assumption that these charter operations already had this freedom.

nated carriers. The only control conceived in the competitive regime was the air carriers' self-imposed restraints of "the pricing of competitors (to prevent them) from providing excessive capacity".[93] The clause, virtually unchanged in all of these bilaterals, stipulates:

> "Neither Party shall unilaterally limit the volume of traffic, frequency or regularity of service, or the aircraft type or types operated by the designated airlines of the other Party, except as may be required for customs, technical, operational or environmental reasons under uniform conditions consistent with Article 15 of the Convention."[94]

In addition, a first refusal requirement, an uplift ratio, no-objection fee, or any other requirement with respect to capacity (which would be inconsistent with the purposes of the bilateral) is also not permitted.[95] This additional prohibition is, in fact, of a special significance to discarding restrictive practices regarding charter operations.

The second difference deals with the nature of competition. In view of the evolving role of charter air

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93. See ICAO ATRP/2-WP/6 at 4 (20 Feb. 1979). See also Wassenbergh, "Innovation in International Air Transportation Regulation", 3 Air Law at 144-146, 151 (1978), where he added the requirement that "capacity should be related to demand". Raben, also talked of a "close relationship to the requirements of the public", see "The Real Test: Does a Liberal Bilateral Work?", ITA Bull. No. 18 at 411-12 (May 12, 1980).

94. U.S.-Barbados Agreement of 1982, Article 11.

95. Id.

services since 1977, the relevant provision has evolved in one important aspect. At first, in some of the early liberal bilaterals, a "fair opportunity" was to be allowed to each Party's designated airlines to compete.[96] Then, in later agreements, this principle became "fair and equal opportunity". In each case, however, reference was to the "international air transportation" covered by the bilateral, rather than "any route...covered by the Agreement", which appears in Bermuda I.[97] There is, of course, a crucial difference between "international air transportation" and the narrower phraseology "on the agreed air routes". "Air transportation" covered by the liberal agreement includes not only the scheduled routes (as the case is with Bermuda I) but also the liberal structure of charters, and, very importantly, scheduled sixth freedom air traffic. In this respect, one should always remember that the absence of any reference to third, fourth or fifth freedoms, part of the mosaic of "internationalisation of traffic"[98] is made possible. Conceptually, and practically this is vital in

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96. See, e.g., U.S.-Netherlands Protocol of 1978, Article 5(a).

97. See supra note 8.

98. Sion, "Multilateral Air Transport Agreements Reconsidered", Va. J. Int'l L. at 197 et seq. (1982).

eliminating problems of capacity determination on fifth and sixth freedom routes, any "freedom" distinction becoming irrelevant where no capacity control exists. The primary third and fourth freedom justification of the Bermuda I Agreement has disappeared.[99] It is worth noting, however, that an exception is found in Article 5(e) of the United States-Federal Republic of Germany Protocol which retains the original Bermuda I capacity control for fifth freedom routes covered by their bilateral Agreement of 1955, as amended by the Protocol.[100] This is not surprising since the German Protocol, in terms of traffic volume, represented for the Americans by far the largest market to be liberalized even to the more limited extent of certain restrictions. In view of its genesis, it seems extremely unlikely that the Germans would contemplate any further move towards more liberalism even if the United States itself

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99. For earlier U.S. positions, see, e.g., Basse & Mathieu, "Ten Years of Commercial Aviation", ITA Studies, 651/8-E at 45-50 (1965). Even now, though, "internationalism" did not extend to charters - most of the earlier agreements limited rights to third and fourth freedom. CF Wassenbergh, op. cit., note 93, at 144.

100. Article 5(e) provides that "Article 10 of the Agreement (of 1955) shall be deleted as far as the traffic between the territories of the two contracting Parties is concerned". See U.S.-F.R.G. Protocol of 1978, T.I.A.S. No. 9591.

still saw advantage in such a step.[101]

The reasons for the initial change in the competitive nature were explained by Farmer as follows: "The deletion of 'equal' and the deletion of applicability to a 'covered route' were necessitated by the conversion of what was a scheduled service only agreement into one covering both scheduled and non-scheduled services." In addition, charter operations (the main form of non-scheduled air services) are now authorized between all points in both contracting Parties rather than confined to routes, thus the deletion of applicability to "covered routes" only. On the other hand, since scheduled operations are inherently superior to charters in their flexibility to compete, Farmer concluded, "there is no way the governments could be responsible to provide charter-designated airlines with an equal opportunity to compete with scheduled services. Hence the deletion of 'equal'."[102] Subsequently, "equal" opportunity was reintroduced, seemingly because the Americans now realized their charter competitiveness

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101. For a good illustration on the current German position against open competition, see "Lufthansa's Ruhnau Warns Against Airline Deregulation in Europe", Air Transport World at 71 (Apr. 1983).

102. ICAO ATRP/2-WP/6 at 3 (Feb. 20, 1979). The description is by Donald Farmer, then Director of the CAB's Bureau International Aviation.

adequate. The original wording ("fair opportunity") persists however in the earlier liberal bilaterals.[103] The standard wording today reads:

> "Each Party shall allow a fair and equal opportunity for the designated airlines of both Parties to compete in the international air transportation covered by this Agreement."

It should also be noted here that several of the later bilaterals refer to the need to remove discrimination and unfair protective practices, which contracting Parties will take "all necessary steps or appropriate action" to prevent.[104] These anti-discrimination provisions are backed up by strong American domestic "implementing" legislation in the form of amended Federal Aviation Act and International Air Transportation Fair Competitive Practices Act.[105]

A third change from the "traditional" competition concept is in those mutual interests which are to be taken into consideration by the contracting Parties. Instead of

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103. See, e.g., Article 5 in both the Belgium and German Protocols.

104. The relevant clause stipulates: "Each Party shall take all appropriate action within its jurisdiction to eliminate all forms of discrimination of unfair competition practices adversely affecting the competitive position of the airlines of either Party".

105 For more details, see infra (footnote 122).

taking account of the other Party's air carriers' interests (as found in Bermuda I), the new langauge "more properly"[106] relates to the other Party's interests in its own designated carriers. The relevant provision in many bilaterals stipulates:

> "Each Party shall take into consideration the interests of the other contracting Party in its designated airlines so as not to affect unduly the opportunity for the airlines of each Party to offer the services covered by this Agreement."

A final remark to make may be more semantic than real. Air carriers' "Opportunities" to "operate" now became "...to compete". Whether this makes a substantive change is not clear. For instance, Lowenfeld has commented on the original Bermuda language by stating that "this clause does have meaning, though it is susceptible to misinterpretation. I believe, and I think the consistent American interpretation has been, that this clause calls for equality of opportunity to compete, to start the race together, if you will, but not necessarily to finish together. This clause is in essence a non-discrimination, not an affirmative action, clause".[107] Although this interpretation may be somewhat

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106. Farmer, op. cit., note 102, at 3. The change appeared in the earlier bilaterals, but later agreements omit the provision altogether, relying on the anti-discrimination clause.

107. Lowenfeld, "The Future Determines the Past: Bermuda I

controversial, it suggests that, for the Americans at least, the change is a clarification rather than an amendment. Evidently, some (or many) nations firmly believe in the need for their carriers to "finish the race" too. This may well be a symbolic bone to fight over in the future.

Change of Gauge

An examination of provisions governing capacity would not be complete without mentioning change of gauge. This concept can be defined as a change to aircraft of different capacity (i.e. size) so that "the section of the route near the terminal in the territory of the contracting Party designating the airline is flown by aircraft different in capacity from those used on the more distant section".[108] It is believed that (even in the absence of a provision on change of gauge in any bilateral) contracting Parties would scarcely, for no reason whatsoever, refuse the carrier of the other Party permission to change into a smaller aircraft on the more distant section of the route,

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in the Light of Bermuda II", 3 Air Law at 5 (1978).

108. This clause has almost appeared, with minor variation, in most post-Bermuda I bilaterals. See, e.g., the UK-Chile Agreement of 1947 (Article 1).

reckoned from the carrier's homeland.[109] One thing to be remembered here is that the more distant section must be operated as part of the same service and not as a separate service. It is also worth noting that this practice must not be confused with trans-shipment which is the "transportation by the same carrier of traffic beyond a certain point on a given route by different aircraft from those employed on the earlier stages of the same route".[110] Whereas change of gauge refers to different size of aircraft, trans-shipment is directed to a change of aircraft, not necessarily of different capacity, for technical purposes. Yet, change of gauge is one of the types of trans-shipment.

Change of gauge, however, has significant economic advantages, i.e. for the operating airlines in the costs of operation. In case of an American carrier serving a trans-atlantic route with stopover at a European gateway, the traffic volume will be lower on the outward leg of the journey. A switch to an aircraft of a smaller capacity corresponds in such case better to the actual traffic demands of that leg of the journey. Nevertheless, the application of change of gauge was relatively rare, probably

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109. Cheng, op. cit., note 4, at 435.

110. Cited in Lissitzyn, "Change of Aircraft on International Air Transport Routes", 14 J. Air L. & Com. at 57 (1947).

due to the heavy costs connected with permanent stationing of aircraft in foreign countries and the difficulties in maintaining normal utilization for such aircraft.[111]

The change of gauge clause entered the picture for the first time in Bermuda I. Annex V of this Agreement deals with that matter, whereby an airline designated under a bilateral agreement changes the type or size of aircraft en route, usually in the territory of the other contracting Party. The conditions imposed upon that change already in Bermuda I (Annex V) have been followed more or less closely in subsequent bilateral air transport agreements. These limits may be enumerated as follows:

(a) the change must be justified by reason of economy of operation;

(b) the aircraft used on the outward journey must be smaller in capacity than the one used on the near section. With regard to this requirement, it should be noted that the corresponding provision in some bilaterals is based on the distinction between the section on which less national traffic is carried by the respective airline and the other section;[112]

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111. Adriani, op. cit., note 12, at 411.

112. In this case, the smaller aircraft should operate on the former section. See, e.g., Canada-Peru bilateral of 1954 (Article VI); Canada-Mexico Agreement of 1953

(c) the capacity of the smaller aircraft must be determined with primary reference to the traffic travelling in the larger aircraft normally to be carried onward;

(d) the change must be subject to the availability of an adequate volume of through traffic; and

(e) the general Bermuda capacity guidelines must be followed, particularly paragraph 6 of the Final Act concerning the primary and secondary justification traffic.[113]

Change of gauge may be commercially significant when exercising fifth freedom traffic rights from a point in a foreign country. The Bermuda-styled bilateral between the United States and France of March 1946 contains a change of gauge provision similar to the one in Annex V of Bermuda I. This provision in the United States-France Agreement[114] led to the famous arbitral decision in 1978 (commonly known as the U.S.-France Air Services Award of 1978[115]) in which the legality of a change of gauge was in issue. Pan

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(Article VI).

113. See supra (footnotes 16 to 22).

114. Air Services Agreement between the U.S. and France, March 27, 1946, T.I.A.S. No. 1507, 2257, 2258 (Annex VI).

115. See supra note 60.

Am, the designated airline of the United States, informed the French Aeronautical Authorities of its intention to operate again its route from the West Coast of the United States via London to Paris with a change of gauge in London. Pan Am had ceased to serve this route since 1975. Although the French argued that such a change in the territory of a third State was not allowed under their bilateral with the Americans, Pan Am nevertheless inaugurated the route.[116] Shortly thereafter a Pan Am aircraft was compelled to return to London after landing at Paris Orly Airport without having disembarked any passenger or cargo.

At stake was a change of gauge outside the territory of the other contracting Party and not covered by the United States-France Agreement. As stated earlier, the provision dealing with the change of gauge in the Agreement follows the general language of Bermuda I and deals with the change of aircraft occurring in the territory of the other Party. Having regard to this provision and the United States-France bilateral as a whole, the Tribunal arrived at the conclusion (by two votes to one) that a change of gauge in the territory of a third country was permitted as long as a continuous service was maintained and that a change was not de facto a provision of separate services. According to

116. Id.

the Tribunal, this conclusion was proven by the context in which the Agreement was negotiated and the subsequent practice of the Parties was not inconsistent with it.[117] Thus, the majority opinion in Arbitral Award favoured a liberal approach to the Bermuda type Agreement.

From the French point of view, however, the Award was strongly criticized as being influenced too much by the American contemporary liberal policy. Indeed, under this regime, change of gauge is much less restricted. A case in point is the United States-Federal Republic of Germany Protocol. Change of gauge is of particular significance in this liberal bilateral because of the rather extensive rights of American carriers between the United Kingdom and Germany and the fifth freedom traffic rights of American airlines beyond Germany. The Protocol explicitly provides that change of aircraft is permitted on all flights, in the territories of contracting Parties and in other countries, provided that:

> "(a) operations beyond the point of change of aircraft shall be performed by one or two aircraft (operated to the same or different destinations under the same or different flight numbers) having total capacity not more, for outbound services, or not less, for inbound services, than that of the

117. Id. at 327 et seq. It is interesting to mention that the Award was only a Pyrrhic victory for Pan Am which, in fact, never initiated the service again.

arriving aircraft; and

(b) aircraft for such operations shall be scheduled in coincidence with the inbound or outbound aircraft, as the case may be, provided, however, that if a flight is delayed by unforeseen operational or mechanical problems, the onward flight or flights may operate without regard to the requirement of this subparagraph."[118]

In general, the change of gauge provision in other liberal agreements is somewhat less detailed and provides that "on any segment or segments of the route described, a designated airline may operate air services without any limitation as to change in number or type of aircraft operated".[119] Finally, some certain liberal bilaterals precisely limit change of aircraft to "any international segment or segments" of the routes described in the bilateral.[120]

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118. The Germany Protocol, op. cit., note 100, (Para. 4 of Article 3).

119. See, e.g., the U.S.-Jamaica Protocol of 1979, Article 3(d); the Belgium Protocol of 1978, Article 3(4).

120. See U.S.-Thailand Agreement of 1979, Annex I, Section 3; U.S.-Netherlands Antilles Agreement of 1980, Annex I, Section 3.

Fair Competition in International Civil Aviation

In a system of free determination of capacity, the prerequisite for fair competitive principles becomes more exigent. The American "open skies" policy is directed to creating a competitive regime accompanied by the least barriers and restrictions. Discriminatory and unfair competitive practices which can influence the "fair and equal opportunity to compete" may take various forms. To cite but a few important examples:[121]

- preferential utilization for the national airlines generally;
- imposition of unfair airport and user charges which can not be economically justified and discriminate in favour of the national carriers;
- preferential customs, immigration and ground services for the national airlines;
- ticket tax only applicable to foreign airlines;
- discounting or special tickets on the national carrier to the detriment of foreign airlines;
- unequal or unfair business and other charges;
- preferential treatment for the national carriers regarding the carriage of mail;
- restrictions on the carriage of outgoing cargo and mail by foreign carriers; and
- monopoly held by national carriers upon check-in and boarding facilities, ticket

121. Extracted from Legal, Economic and Socio-Political Implications of Canadian Air Transport, Centre for Research of Air and Space Law, McGill University at 596 et seq. (1980).

stocks and reservation computer systems.

To provide a means of retaliation against such discriminatory practices, the Congress of the United States passed the International Air Transportation Fair Competitive Practices Act of 1974, amending parts of the Federal Aviation Act of 1958,[122] In addition, the liberal bilateral air transport agreements contain a standard clause which guarantees each Party undiscriminating commercial freedom in the other Party's country.[123] Several of these bilaterals also oblige the contracting Parties to take all appropriate action within their jurisdiction to get rid of all forms of discriminatory practices affecting the air carriers of the other Party.[124]

The 1974 Act was aimed at removing discriminatory and unfair competitive practices and required several excecutive departments of the government to monitor foreign practices which discriminated against American carriers. Section 2(a) of the original version of the Act directed the CAB, the Departments of State, Treasury and Transportation, and other Federal Agencies to administer and take appro-

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122. International Air Transportation Fair Competitive Practices Act of 1974, Pub. L. 93-623, 88 Stat. 2102 (hereinafter cited as the 1974 Act).

123. See infra (footnote 129).

124. See supra (footnote 104).

priate action for the purpose of eliminating such discriminatory practices to which American airlines were subjected in providing foreign air transportation. In this connexion, one should note that Section 23 of the 1979 International Air Transportation Competition Act added a new subsection (b) to Section 2 of the 1974 Act which broadened the CAB existing powers. The amended section now provides that whenever the CAB (upon receipt of a complaint by an American carrier or agency or upon its own initiative) determines that a foreign government is discriminating against or unreasonably restricting an American airline, the Board may take such action as it deems in the public interest to discard these practices. Such actions taken by the Board may "include, but are not limited to, the denial, transfer, alteration, modification, amendment, cancellation, suspension, limitation, or revocation of any foreign air carrier permit or tariff pursuant to the powers of the Board under the Federal Aviation Act of 1958".[125] In addition, the new subsection (b) provides that the CAB must take appro-

125. The reference to the powers of the CAB under the Federal Aviation Act means that the Board must exercise its power in a manner consistent with any obligation assumed by the U.S. under any treaty, convention or agreement (Section 1102). Hence the Board must respect eventual consultation obligations under bilaterals and any action is also subject to Presidential review.

priate remedial action against the foreign country or air carrier within 60 days after the receipt of the complaint. This period may be extended for an additional period or periods of 30 days each up to a maximum of 180 days, if the Board concludes that the complaint could be satisfactorily resolved through negotiations with the foreign government. While considering any complaint, or in any proceedings under its own initiative, the Board must confer with the State and Transportation Departments and provide any affected air carrier or foreign airline with reasonable notice and opportunity to file written evidence and statements within a prescribed time limit.[126]

It is worth noting that Section 9 of the 1979 Act empowers the CAB with a "stick behind the door" to summarily suspend, alter or amend (in the public interest and without a hearing but subject to Presidential approval) a foreign airline's operating permit if discriminatory practices are being imposed by the government of the foreign carrier. The Board may even, to the extent necessary (without a hearing but subject to Presidential approval), restrict operations between such foreign country and the United States by any

126. Section 23 of the International Air Transportation Competition Act of 1979.

foreign airline of a third country.[127] No doubt the Board could now redress legitimate grievances of American carriers by retaliation.

As to the unfair user charges (the most common complaint in recent years), Section 3 of the 1974 Act provides that the Secretary of Transportation is responsible to survey the charges applied to or imposed upon American air carriers by foreign governments for the use of airport property or airway facilities in foreign air transportation. If such charges unreasonably transcend comparable charges for furnishing such airport or airway facilities in the United States, the Secretary of State and the CAB must promptly assume negotiations with the foreign country to eliminate such discriminations. The remedy, should negotiation fail to resolve the issue, is a countervailing charge against the foreign carrier whose government or authority is responsible for the alleged discrimination.[128]

Another remedy against unfair and discriminatory practices is a standard clause which is associated with all of the liberal bilaterals and which grants American air carriers managerial, technical and operational freedom in

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127. Id. Section 9.

128. Section 3 of the 1974 Act, op. cit., note 122.

foreign countries.[129] According to this provision, each carrier can erect its own sales offices and bring its own technical and commercial staff in the other Party's country. They can conduct their own ground handling services, or at least select between agents for such operations. Each air carrier may also engage directly in sales, except for special arrangements on charters. Facilitation is to be extended to financial transfers (i.e. revenue surplus, matters of taxation and exchange operations).

It is evident that the intention behind this clause is to equip the liberal bilaterals with two standards of international economic law, namely, the "standard of equitable treatment" which serves to avoid arbitrary discrimination between foreign nationals in relations in which it is difficult to apply objective standards,[130] and the "national standard" which provides equality of treatment between foreigners so privileged and the nationals of the State granting this type of equality.[131]

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129. See supra, Section II (footnote 94); supra note 123.

130. See Schwarzenberger & Brown, A Manual of International Law, Rothman & Co., South Hackensack, New York at 88 (1976).

131. Dold, "The Competitive Regime in International Air Transportation", 5 Air Law at 144 (1980).

SECTION III - ICAO'S WORK ON THE REGULATION OF CAPACITY

The Nature of the Problem

This is probably the field which is the most controversial and in which obviously antagonistic positions are taken in theory and practice. In other words, its control conditions both the financial balance of the airlines and the interworkings of international competition.[132]

In creating an air transport industry, States are caught between two poles:[133]

(a) the promotion of economy by expanding the network of international air services for the benefit of the public; and

(b) the protection of their flag carriers so that they will get a fair opportunity to compete for business.

It is difficult to achieve these two targets with the same course of action. Practically speaking, however, all nations have emphasized the second notion.

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132. See "The Capacity Concept as Implemented in Practice in International Air Transport", Study presented by the ITA to the 1977 SATC at 1 (1977).

133. See, e.g., Loy, op. cit., note 36, at 175; Wassenbergh, op. cit., note 40, at 17.

In fact, there is no problem when there is only one airline operating on domestic routes. But when the protected air carrier starts operating abroad, difficulties arise in implementing such a policy because in international air transport a State does not have the complete control that it enjoys in relation to domestic operations. To foster and promote its objectives, it has, within the framework of the treaties which it makes, to negotiate appropriate terms. The premises on which the nation negotiates reflect its conception of the role of air transport. One can thus have diametrically opposed policies on capacity regulation.

From the regulatory viewpoint, it can be said that bilateral air transport agreements frequently contain stipulations referring to free and equal opportunity for designated carriers of both Parties or ensuring an equal sharing of the market. Other bilaterals provide for a predetermination of capacity by aeronautical authorities, which is to be adjusted according to traffic needs. Still another type of bilateral stipulates that the air transport services made available should bear a close relationship to the requirements of the public for such transport. In this latter type, a provision for an after-the-fact review of capacity is usually included. Generally, bilateral agreements do not refer directly to 5th freedom traffic to be carried by the

designated carriers of third Party States.[134] In recent years, provisions on "fair competition" were also introduced in some bilaterals.

States are in different situations when negotiating capacity with regard to geographic position.[135] Also, some nations (like the United States) generate a lot more traffic than others. The advantage of this for such states is that they can demand a large portion of the traffic, as the Americans do over the North Atlantic and Japan over the Pacific.[136] Other States with a favourable geographic position (e.g. Belgium) can use it for connecting traffic from different parts of the world, i.e. the sixth freedom traffic. It has been argued that countries which generate a small amount of traffic ought to be liberal in granting traffic rights since they have nothing to confer in return

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134. For a good illustration on the various types of capacity clauses in bilaterals, see "Regulation of Capacity in International Air Transport Services", Information Paper prepared by the ICAO Secretariat to the 1977 SATC at 5 et seq.; "Handbook on Capacity Clauses in Bilateral Air Transport Agreements", ICAO Circular 72-AT/9.

135. Stoffel, op. cit., note 37, at 125; Working Paper presented by the World Tourism Organization to the 1977 SATC, WP/22.

136. See Aviation Week & Space Tech. at 24 (Aug. 23, 1976).

and nothing to lose.[137]

Whatever their position is, or whether of the Bermuda type or not, bilateral agreements always reflect (for different reasons) the desire of the contracting Parties to safeguard "equal opportunity" for their national airlines. Against a background of increased competition, this rather vague and theoretical objective has nowadays become the subject of bitter dispute: the concept of approximate exchange tends to become one of strict application.[138]

The defenders of rigorous economic planning are increasing in numbers. Thus, the big bilateral disputes over the scheduled services have always concerned either the general principles of aeronautical policy (principle of liberalism and a posteriori or ex post facto review of the operating results, or alternatively, planning and predetermination of operating conditions), or the interlocking mechanisms of traffic rights (status of fifth freedom, and recently even sixth freedom, as compared with direct-exchange priority traffic of the third and fourth freedom type). In this respect, however, it has always to be remembered that the decisions that are made on capacity in

137. Wassenbergh, op. cit., note 40, at 22.

138. Supra note 132 at 2.

respect of non-scheduled services are usually conceded through administrative permits on a short-term basis (temporary) or are unilateral actions taken by national air transport authorities.[139]

During the past four decades, the air transport industry has been faced with cyclical supply/demand imbalances, often related to the introduction of new aircraft types. The problem of adapting to technological change is not unique to civil aviation and like other industries significant adjustments have been made over the years to meet dynamic growth and changing market characteristics. However, the last fifteen years have seen an exceptional build-up of capacity distorting the supply/demand balance beyond the industry's capabilities for adjustment. The interrelated causes of this situation may be summed up as follows:[140]

(a) changing government political philosophies;

(b) increase in market participants, i.e. the growth in the number of airlines (both scheduled and non-scheduled);

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139. See "Policy Concerning International Non-Scheduled Air Tranpsort", Working Paper submitted by IATA to the 1977 SATC-WP/5 at 5 (Para. 23).

140. See, e.g., Hill, "Comments, Bermuda II: The British Revolution of 1976", 44 J. Air L. & Com at 113-115 (1978); Taneja, Airlines in Transition at 53 et seq. (1981).

(c) influence and requirements of aircraft manufactures;

(d) the unfair advantage taken by some air carriers in "accessing" fifth and sixth freedom traffic;

(e) the "limitless growth" syndroms of the sixties; and

(f) fuel and economic crisis of the seventies confounding traditional growth projections.

The direct effect has, therefore, been that on many international routes capacity provided did not relate to demand, resulting in an unfair advantage for one partner to a bilateral agreement.

It is impossible to examine the question of capacity without briefly addressing the interrelationships of tariffs and demand on the one hand, and utilization on the other. A perusal of the States' practices in this field demonstrates that the establishment of capacity has been mainly based on the fulfilment of passenger demand. Only recently have all-cargo services begun to develop.[141] High load factors at low unit costs and low prices to the user can be achieved by careful control on supply and utilization of aircraft capacity. Low prices, however, create strong demand pressures for additional capacity. Additions

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141. See Ndum, Economic and Legal Developments on Carriage of Goods, unpublished thesis, McGill University, Montreal (1982).

to capacity to meet these demands can result in lower load factors and higher unit costs with uneconomic results for airlines. These considerations therefore necessitate the need for levels of fares and rates which take into account demand and capacity factors, and vice-versa.

Recent experience has shown that in certain markets existing regulatory provisions have not been sufficient to prevent the problem of excess capacity the provision of which has resulted in inefficient use of resources and higher costs. On the North Atlantic, for example, scheduled air services have in the second half of the 1970's operated on the average with an inordinately high number of seats unfilled. While such load factors may not have posed too serious a problem in the early sixties when carriers enjoyed the dramatic productivity gains and cost reductions which accompanied the advent of the jets,[142] they were by the mid-seventies of major concern because of the insufficient revenue and continually increasing costs in most essential sectors (such as fuel, capital, personnel and user charges). It is true that several airlines have taken steps to attempt to ensure a closer relationship between capacity and demand to the extent legally and commercially feasible. Thus, they have engaged in revenue and equipment pooling, capacity

142. McCarroll, op. cit., note 9, at 120.

limitation agreements and have also deferred aircraft purchases.[143] However, action by carriers through such means has been insufficient to meet the situation.

The general excess capacity problem is further compounded by the addition of non-scheduled capacity and the injection into the marketplace of new aircraft types which carriers are compelled to purchase in order to hold their position in a losing market. Additionally, it is worthy of note that the present overcapacity problems are being complicated by the exercise of new or heretofore unused traffic rights. This has led one commentator to feel that "the sickness of overcapacity is still with us and we still seem unable to cope intelligently with the problem".[144]

The tendency towards a more rigid configuration of capacity control links, in general, to the problem of overcapacity and the financial vitality of individual air carriers and the industry. Sufficient convincing arguments

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143. For the various types of co-operation between airlines, see, e.g., Verploeg, The Road Towards a European Common Air Market, unpublished thesis, McGill University at 94-132 (1963); Intravia, American Aviation Policy: Capacity, Competition and Regulation, unpublished thesis, McGill University, Montreal (1977).

144. Alitalia Chairman Nordio's Speech to Columbia University in New York in Feb. 1983, see Aviation Daily at 111 (21 Feb. 1983).

have been advanced to explain the merits of capacity control. For example, given the fixed nature of tariffs, capacity is the only effective tool used to compete in the market. The problem, nevertheless, remains one of defining excess capacity. While it is difficult to give an exact delineation, Friedman has found that "the best way of describing overcapacity is to do so in terms of excess frequencies provided over and above what is necessary to meet public demand and to maintain profitable operation".[145] Even Wassenbergh gives the twofold meaning of excess capacity: capacity which is not used economically, or capacity which may be eliminated without affecting the airline's traffic growth or position on the market.[146] In this regard, the load factor provided the best objective criterion in practical terms, taking into account the tariff levels on the route in question and the aircraft type used. To better comprehend this sequel, one should note that at one extreme it is evident that in scheduled operations it is not possible to achieve 100% load factor due to the uncertainty in demand and the existence of seasonality, directionality, given size of aircraft and the need to

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145. Quoted by Naveau, "A New Verdict Involving a Bilateral Agreement: Arbitration on the Belgium/Ireland Capacity Clause", 39 ITA at 980 (Nov. 1981).

146. Wassenbergh, op. cit., note 5.

reposition empty aircraft. At the other extreme, capacity would be excessive if an airline experiences an average load factor too low to provide an adequate return on investment at the existing fare level. The optimal load factor, and therefore the measure of excess capacity, would lie between these two limits.

Although the solution for the excess capacity knot is unclear, it is generally agreed that the question must be dealt with on a bilateral basis.[147] This is understandable from the fact that the damage resulting to a carrier through unilateral reductions in capacity virtually rule this out as a feasible method if competitors do not match such reductions.[148] This consequence is emphasized by the phenomenon that profit or loss for the purpose of capacity regulation is determined at the margin. The load factor needed to cover the marginal costs of operating a single flight can be very low, much lower than if fully allocated costs have to be covered. Far from improving its financial situation by cutting out a flight or series of flights, an individual carrier may well find itself in a

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147. See, e.g., Lyon, "Principles, Policies and Practices in International Air Transport", in Matte Ed., op. cit., note 18, at 38; supra note 134, at 14.

148. Working Paper submitted by the UK to the 1977 SATC at 2,7; id.

worse position where the cutback costs more in lost revenues than in direct operational savings.

In the public interest, however, it is necessary to ensure the most efficient use of resources and the consequent minimization of prices. The resources to be utilized efficiently include not only equipment and fuel but also resources in capital often in short supply, particularly in developing nations. It is therefore imperative that, in the affected areas, air carriers be given the tools necessary to resolve the problem. In this connexion, direct government action would have a tendency to be too rigid to react promptly to shifting market preferences and would not properly reward efficient and energetic carriers. But when capacity offered is far greater than demand, States should consider ways and means of permitting airlines to enter into capacity agreements with other carriers where the situation so demands.[149]

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149. See supra, Chapter V, "Preliminary Conclusion" (some recommendations submitted by the writer (Criterion "c"); infra "Preliminary Conclusion of this Chapter.

ICAO's Mediation in the Problem

There are three main reasons which justify a world-wide regulation of capacity:[150] the difficulty experienced by States in achieving an exact equilibrium in their bilateral exchange, the opposition of - at times - radically different doctrines regarding aeronautical policy and, above all, the increasing growth of charter operations which are generally outside any regulation of the overall capacity system applied.

At the time of the 1977 Special Air Transport Conference, the developments relating to capacity in international air services seemed to represent for the majority of participating States an important and pressing problem. The inclination of the Conference was hence that the regime for regulating international air transport capacity which had developed over the past thirty years had not promoted the contemplated objectives for which it had been designed. This delinquency was attributed to the fact that on many routes capacity was not closely related to demand; "fair and equal opportunity" for the airlines of the Parties to an agreement was often felt not to exist; and finally the

150. Special Air Transport Conference (Montreal, 13-26 April 1977) Report at 13-14 (hereinafter cited as SATC (1977), ICAO Doc. 9199).

carrier of one State appeared to frequently ignore the interests of the carrier of the other.[151]

As to the overcapacity problem, some delegations at the Conference suggested that this question might be short-term phenomenon resulting from the too rapid introduction of wide-body aircraft combined with worldwide inflation and economic recession. The majority however were of the opinion that, while these were contributing elements, the fundamental reason for the excessive offer of capacity was the "absence of an effective regulatory system" and that the problem was therefore long-term.[152] These and other shortcomings were charged to the "liberal attitudes to capacity regulation", referring, even if not always expressly, to the capacity control system established by the Bermuda I Agreement of 1946.

The 1977 Conference not only agreed that there was a need to re-evaluate the principles on which regulation of scheduled operations "had in varying degrees based since 1946", but decided also to extend such a re-evaluation to non-scheduled services which were even less subject to "consistent application of any internationally accepted rules". The "general view" was that these two air transport

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151. Id. at 13 (Para. 3).

152. Id. Para. 4.

categories should be "regulated harmoniously" without necessarily bringing non-scheduled operations within the bilateral framework. As a consequence, the Conference recommended (in Recommendation 4) to the ICAO Council to undertake studies aimed at, inter alia, "establishing criteria and using these to formulate alternative methods for regulating capacity on scheduled and non-scheduled international air transport services"; and "developing a model clause (or clauses) or guidelines for regulating capacity on the basis of prior determination for consideration, along with other clauses or guidelines, by contracting States".[153]

The Panel of Experts on Regulation of Air Transport Services, mentioned previously,[154] was therefore asked by the ICAO Air Transport Committee to base its terms of reference relating to capacity regulation on Recommendation 4. Early in its work, the Panel was faced with some initial difficulties that were caused by the terminology used by the 1977 Conference. ICAO studies were supposed to deal with "criteria", "alternative methods" and "guidelines" for

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153. Recommendation 4, id. at 16. Also included in this Recommendation was an enumeration of circumstances of factors the studies should take into account, and a recommendation of what States should or should not do pending the conclusion of the studies. Id. at 16-17.

154. See supra, Chapter V (footnote 143).

regulating capacity. Also, even if not specifically mentioned in Recommendation 4, there was certainly the question of "objectives" in the management of capacity. The Panel members were thus confronted with the task of developing their own interpretation of the terms and concepts to guide them in their subsequent work.[155] Consequently, they attempted to enumerate a number of objectives which, in their opinion, fell into two broad groups: those that were common to all options, and those that varied according to national point of view.[156] The "common" objectives included the avoidance of excess capacity with the consequent waste of resources, prevention of capacity "dumping", protection of the environment, harmonization of regulation of scheduled and non-scheduled operations in the same market with the possibility of a reasonable economic return to the carriers, provision of good service to the consumer and assurance of fair and equal opportunity to compete. Listed among the variable objectives were the improvement of a State's balance of international payments, protection of

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155. Gertler, "Law of Bilateral Air Transport Agreements: ICAO Air Transport Regulation Panel and the Regulation of Capacity", 9 Annals of Air and Space Law at 47 (1984).

156. ICAO ATRP/1-Report at 12 (Para. 14). This approach, including specification of common and variable objectives, was later adopted by the 1980 Conference.

interests of the national carrier and sharing of traffic to be carried.

The Panel members then agreed on a set of criteria to be used as a basis for the formulation of methods for regulating capacity. These criteria were approved by the 1980 Air Transport Conference;[157] all of them expressed the necessity for respecting "such and such" an objective and can be classified as follows:

(1) Objectives relating to the management of scheduled air transport:

- associating capacity closely with demand, with the desirable flexibility,
- providing capacity governed mainly by traffic demand between the territories of contracting Parties,
- ensuring equality and mutual benefit for the carriers of both countries concerned;

(2) A general objective:

- encouraging the development and expansion of air transport on a sound economic basis and in the public interest;[158]

(3) Objectives to ensure coherence and conservation:

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157. Second Air Transport Conference (Montreal, 12-28 Feb. 1980) Report at 14 (Para. 15) (hereinafter cited as AT Conf/2, ICAO Doc. 9297); ICAO ATRP/3-Report at 17.

158. It was noted by the Panel and then the 1980 Conference that the "public interest" is composed of three principal interest factors: (a) the airline industry; (b) users of air transport; (c) other national interests. See ICAO ATRP/3-Report at 17 (Para. 23); AT Conf/29ICAO Doc. 9297 at 14.

- allowance for airport and airway capacity,
- efficiently using resources, particularly fuel,
- protecting the environment;

(4) An objective to ensure coexistence:

- harmonizing capacity on non-scheduled flight and on scheduled services with total demand.

In the case of the methods of capacity regulation, the 1980 Conference has noted, after the Panel, that there are three fundamental modes for regulating capacity, with intermediate variants:

- the predetermination method,
- the Bermuda I type method,
- the free determination method.

Each seeks to prescribe, as has been shown, separate and distinguishable approaches to setting out the possible and desirable role of capacity within the international air transport system. Each represents efforts by nations to seek effective participation in the operation of international air transport services. States are increasingly recognizing that the primary objective of effective capacity arrangements is to endeavour to avoid, as far as possible, the deployment of excess capacity and also ensure that consumers benefit through lower prices from higher capacity utilization.[159] Although several delegates at the

159. Working Paper presented by Australia to the 1980 Conference, AT Conf/2-WP/16 at 3; Gertler, op. cit., note 155, at 43.

Conference questioned the value of "free determination" policy, on the grounds that it was a non-method, the Conference decided to take it into account with the other two, since some States have been supporting this approach.

It was generally believed, however, that free determination of capacity and freedom to set fares could result in "capacity dumping" and uneconomic fares, and a small airline could be destroyed before the situation could be remedied.[160] This is because in a system of free determination of capacity there is no direct control by governments and the airlines are hence entirely free to fix their own capacity by not only taking into account competition on the routes in question but also their real profitability and management at its most efficient.[161] One could indeed argue that this system would create overcapacity, whereas each method of capacity regulation strives to specifically avoid this problem. Additionally, with this method charter operators are faced with unlimited competition from scheduled airlines offering lower marginal prices and airlines will operate where the demand is the

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160. AT Conf/2, ICAO Doc. 9297, op. cit., note 157, at 22.

161. See AT Conf/2-WP/7, op. cit., note 90, at 2.

greatest.[162]

Although the United States, together with a number of other nations, firmly attempted at the 1980 Conference to promote the free determination method, doubts were raised by many delegates regarding the disadvantages of this method. The majority of states now feels that since the marketplace is not perfect, a certain amount of regulation is needed to protect public interest and achieve international cooperation. In addition, given the heterogeneity of markets and the divergence of national policies, the free market-oriented philosophy for capacity regulation is not feasible. This viewpoint was certianly favoured by most developing States since it was impractical for their carriers to acquire the latest and most cost effective equipment, a fact that would place them at an operating-cost disadvantage. A large majority of delegates therefore rejected the free determination method and the Conference concluded that "it would be premature to make any such recommendation to the Council".[163]

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162. See AT Conf/2-WP/16, op. cit., note 159, at 4-5; Gertler, op. cit., note 155, at 56.

163. AT Conf/2, ICAO Doc. 9297, op. cit., note 157, at 22. See also, "ICAO Conference Rejects U.S. on Capacity Restriction Removal", Aviation Week & Space Tech. at 30 (Feb. 25, 1980).

In connexion with the regulation of capacity, it is worth mentioning that the 1980 Conference also considered the future effect of fuel availability and the allocation upon capacity. To this end, it recommended that all contracting States should ensure the adequate supply of fuel for approved operations on a fair and non-discriminatory basis, at prices current in their respective national markets.[164]

Tendency Towards Predetermination of Capacity

A key principle for many States in seeking to adopt more effective approaches to capacity arrangements rests on the recognition that nations have sovereign rights to retain and promote the economically viable and efficient participation of their national carriers in the provision of international air transport services. To achieve this aim, States will undoubtedly be encouraged to adopt that approach to capacity management best suited to their individual requirements.

In this sense, the majority of the international aviation community feels that the existing system of regula-

164. Id. at 23-24; AT Conf/2-WP/27 presented by New Zealand.

ting capacity does not meet the primary objective of permitting the international carrirs of all nations to operate under conditions of fair and equal opportunity. Given the unsatisfactory operating economics of the industry and the fact that the regulation of capacity involves many factors that extend beyond the economics of airlines operations, the attitude to capacity regulation has been changing from one of ex post facto review to one of predetermination.

The predetermination system consists of prior governmental approval or determination of capacity before air services may commence. Sometimes this determination is confined to total capacity only. More often it links with scheduling flights, frequency of operations and/or types of aircraft to be used.[165] Predetermination clauses can take various forms. The total route capacity and the way it has to be shared between the designated carriers can be determined in the bilateral air transport agreement.[166] Also, the bilateral agreement can contain the Bermuda I capacity principles, but makes them subject to a priori

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165. For a good illustration on this method, see supra note 134, at 6-7; Jack, "Bilateral Agreements", 69 J. of the Royal Aeronautical Soc'y at 476 (1965).

166. See, e.g., Articles 8 and 9 of the bilateral agreement between Belgium and U.S.S.R. in regard air services, Pretoria, June 11, 1958.

rather than ex post facto governmental review;[167] or, the agreement contains an agreed sharing formula (e.g. 50/50 division of route capacity) subject to prior governmental approval. In the last two cases, predetermination can also be obtained by laying an obligation on the carriers to conclude a capacity agreement which has to be approved by both governments.[168] Often, capacity clauses working with a system of equal sharing or reciprocity of traffic, base themselves exclusively or primarily on inter-partes traffic, i.e. third and fourth freedom traffic between the contracting Parties.

The consequences of predetermination scheme may also be accomplished by modes of commercial revenue pooling agreements[169] between air carriers, which sometimes are

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167. See, e.g., Australian Standard Draft (1975) Agreement (Article 8) in 2 Review of Australia's International Civil Policy at 310-11 (1978).

168. Haanappel, "Bilateral Air Transport Agreements: 1913-1980", 5 Int'l Trade L.J. at 254 (1980).

169. A commercial pool agreement can be defined as a contract sui generis between two or more airlines for the operation of one or more air routes where the revenues derived from the services are put together and then split according to a predetermined formula. What kind of formula is to be used is well exemplified in Sharif's Report, "The Mathematics of Pool Agreements", in Vlasic & Bradley Ed., The Public International Law of Air Transport at 88 et seq. (1976).

required or allowed in bilaterals. Such arrangements, which always provide for a sharing of revenues, may cover such matters as the division of capacity, frequencies, traffic and costs. Commercial pools, whether compulsory or authorized under bilateral agreements or even without authorization in the bilateral agreement, are allowed by almost all nations of the world except the United States. The Americans are of the opinion that commercial pooling hampers the competitive environment and generally impairs the benefits that competition can bring.[170] In this regard, it should be noted that United States carriers will only be allowed to enter pools when the national interest so dictates.

In sum, the purpose of such pooling arrangements is that the airlines want to secure a way to exercise business that is to their advantage in the sense of more performance. It could also be that they desire to be sure that they get as big a share and as much benefit from the market as the other airlines. Some States therefore regard pooling as a purely airline activity, but the fact remains

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170. As an emergency measure in times of fuel shortage, the CAB has in the past often approved capacity reduction agreements between airlines. These agreements, however, did not provide for the sharing of revenues. For more details, see Intravia, op. cit., note 143, at 53 et seq.

that many recognize it as a method of capacity control which may be employed in accordance with the terms of a deterministic bilateral agreement.

During the last two decades, as has been pointed out, a noticable shift away from the Bermuda principles towards such a more stringent control of capacity, has taken place in international aviation relations. In 1965, only a relatively small number of the approximately six hundred bilaterals filed with the ICAO, required prior determination of capacity.[171] In contrast, roughly sixty per cent of States which provided information on this topic, for the purposes of the 1977 Special Air Transport Conference, favoured predetermination of capacity.[172] This trend was, therefore, highlighted at the 1977 Conference and again at the 1980 Conference it was given extensive encouragement, with its principles, based on wide experience, being codified.

The 1980 Conference, after having approved the objectives and criteria for the regulation of capa-

171. ICAO Handbook on Capacity Clauses, op. cit., note 134, at 27.

172. See ICAO Secretariat Information Paper, op. cit., note 134, at 7, 38.

city,[173] turned next to the development of a model clause(s) or guidelines for regulating capacity on the basis of prior determination. The Conference noted that the Panel of Experts analyzed the relationship between the regulatory criteria and methods to arrive at guidelines for drafting model capacity clauses for the various methods of regulation (beginning with predetermination). In this connexion, the Panel's analysis of the regulatory criteria resulted in sixteen guidelines[174] to be applicable for the predetermination method. It was concluded by the Panel, however, that any such clause could not directly reflect all of these guidelines and should express only the basic features of the predetermination method but be capable of adaptation.[175] Having taken into account this conclusion, the 1980 Conference approved, with some minor changes, the predetermination model clause (drafted by the Panel) and recommended that this clause together with the criteria and guidelines "be transmitted to contracting States for their considera-

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173. See supra (footnotes 156, 157).

174. These guidelines bring in details on the spirit in which the method of capacity should be conceived, and with all the aspects of the question being tackled in turn. For these guidelines, see AT Conf/2, ICAO Doc. 9297, op. cit., note 157, at 16-19.

175. ICAO ATRP/3-Report at 25 (Para. 37).

tion".[176]

The predetermination model clause adopted consists of the following main elements:[177]

(1) The aeronautical authorities of the two contracting Parties agree upon, or approve the total capacity provided on the agreed services before the commencement of the operations and thereafter, on the basis of forecast requirements.

(2) The primary objective of agreed services will be to provide, at reasonable load factors, sufficient capacity to meet traffic needs between the territories of the two Parties.

(3) The two Parties shall grant the designated airlines fair and equal opportunity of operating the agreed services between their territories so as to achieve "equality and mutual benefit", in principle by equal sharing of the total capacity between the two Parties.

(4) Each Party shall take into account the interests of the other, so as not to affect unduly the

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176. Recommendation 2, AT Conf/2, ICAO Doc. 9297 at 21. The predetermination model clause was also approved by the 23rd Assembly of 1980. See Resolution A23-18 at 49.

177. See AT Conf/2, ICAO Doc. 9297, op. cit., note 157, at 20-21.

services provided.

(5) In case of failure by contracting Parties to agree on capacity, the designated airlines shall not exceed the total capacity (including seasonal variations) previously agreed to be provided.

As is evident from its wording, paragraph 2 of the model clause emphasizes the third and fourth freedom traffic (inter-partes traffic) without making any specific reference whatsoever to capacity to meet fifth freedom traffic requirements. It was pointed out, however, that the use of the term "primary" objective presupposed the existence of a "secondary" objective and a point was made at the Conference[178] that this covered fifth freedom traffic without stating it explicitly in the clause itself. Thus, the text of the predetermination model clause was intentionally left only with an implied recognition of other than third and fourth freedom traffic and without enunciation of any principles to govern the supplementary capacity.

The formula used in paragraph 3 of the model clause is interesting in several respects. The "fair and equal opportunity" requirements brings to mind the typical Bermuda I language ("fair and equal opportunity" ... to operate on any route...) but should be probably interpreted as

178. Id. at 20 (Para. 21).

primarily applicable to the initial determination of capacity.[179] With regard to the actual results of operation, these should bring about "equality and mutual benefit", in principle by equal sharing of capacity. In this perception, the predetermination clause manifests here the objective of Recommendation 4 (paragraph 2) of the 1977 Conference that there be effective provision for equality and mutual benefits for the designated airlines of both Parties concerned. The wording of the model clause is directed to "equality and mutual benefit" but not to "equal and mutual benefit". Apparently, "equality" has to be therefore understood as "equality of opportunity" or "equality of sharing" in capacity and in that sense it is a clearer declaration but not basically inconsistent to the Bermudian "fair and equal opportunity". Also, it is important to remember that paragraph 3 applies only to agreed services operated between the two Parties whereas the formula under paragraph 1 of the clause applies to the "total capacity to be provided on the agreed services". Capacity on the fifth freedom sectors on the agreed services is thus subject to predeterminaiton by both Parties but not

179. Principles proposed by a number of delegations at the 1977 Conference refer to the initial predetermination of the level of capacity on the basis of fair and equal opportunity.

to the "fair and equal opportunity" principle. This may be true with respect to the needs of "equality" but less so when only "fairness" is required.

Practically speaking, the predetermination method of capacity conforms to the wishes of most nations, particularly the third world countries with relatively small or weak airlines. In bilateral negotiations between States with designated airlines of grossly unequal strength predetermination of capacity would be the first thing to look at. This method serves to protect the weaker carrier of one State from excessive competition from the stronger carrier of the other, and it ensures that the weaker side will have and retain a certain share of the air transport market. It is no exaggeration to envisage that the only rational way to achieve low fares is through increased productivity which is accomplished within the predetermination scheme.[180]

In fact, this method has always existed, in one configuration or another, on a large scale, even under the Bermuda capacity principles.[181] One can, however, note that the language of the predetermination model clause is

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180. See, e.g., AT Conf/2-WP/16, op. cit., note 159, at 4-5.

181. See supra, Section I of this Chapter.

far too general. "Fair and equal opportunity" is no longer interpreted as a prerequisite to operate according to fair competitive practices but as an excuse for a 50/50 division of the traffic. Additionally, the clause puts too much stress on third and fourth freedom capacity without indicating of any principles to govern fifth freedom capacity. Although not explicitly mentioned, the clause can also be applied to non-scheduled air services.

As to the model clauses for the Bermuda I type and free determination methods (developed by the Panel of Experts), the 1980 Conference observed that these two clauses had not been analyzed in relation to the approved objectives and criteria, and therefore it sent them back to the Panel drafting board for further analysis.[182]

The assessment of the Panel's work on capacity matters leads inevitably to the question whether the expectations of the 1977 Special Air Transport Conference were satisfactorily met. The answer would probably be in the

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182. See Recommendation 3, AT Conf/2, ICAO Doc. 9297, at 21. Pursuant to this Recommendation, the fourth meeting of the Panel (held in Montreal from 8-19 December 1980) considered criteria and guidelines for the Bermuda I type and the free determination methods. It did not, however, develop new model clauses for these two methods of capacity regulation. With this action the Panel was under the assumption that it had completed those studies on capacity. See ICAO ATRP/4-Report.

negative if the wish of the Conference is recalled: "to re-evaluate" the principles of regulation of capacity traditionally applied since 1946, or to establish a harmonious regulation of both scheduled and non-scheduled international operations within the same general policy context.[183] ICAO's 24th Assembly (held in Montreal from September 20 - October 10, 1983) seems to confirm this answer by proclaiming that it would be for the Council to decide if any more work is necessary in this area,[184] a sign of dissatisfaction, at least indirectly, with the final results.

It is hoped, therefore, that the Third Air Transport Conference to be held in October 1985 would offer an appropriate forum for the contracting Parties to fill in the gaps left on the regulation of capacity. The Provisional Agenda for the Conference includes, inter alia, two items which could lead to discussion of some aspects of capacity control or management: item (1) - Commercial rights for scheduled services, and item (2) - Policy concerning international non-scheduled air transport.[185]

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183. See supra, Section III of this Chapter.

184. Assembly Resolution A24-11, ICAO Doc. 9414, A24-RES.

185. Attachment to ICAO State Letter SC3/1-85/8 of 18 March 1985.

PRELIMINARY CONCLUSION

The international air transport industry has developed since 1946 in a way that can hardly have been foreseen by the negotiators in Bermuda. Their Agreement was designed to deal with the immediate post-war situation and yet, because it was the result of a carefully wrought compromise and was based on the flexible application of general principles rather than on precise details, the type of capacity regulation that it established served the industry well for something like three decades. However, in view of the changes that have occurred, it is not surprising that a majority of States now no longer find this approach satisfactory.

The whole picture has altered radically. For instance, proliferation in the number of international airlines, increasing irrationality in North Atlantic routes, increasing fuel costs, the rising charter regimes and political skepticism, all contribute to growing uncertainties about the viability in the long-run of a system based upon shares of national traffic, free competition and self-regulation of capacity. In short, nationalized international air transport, in the sense of "pre-established" capacity and non-competitive route shares represents a major alternative to the regime of competition epitomized by Bermuda I

type bilaterals.

The main reason behind moving towards a stricter form of capacity control has been commonly attributed to the problem of overcapacity. This issue - as connected with an unsatisfactory yield situation - has in fact become a serious question for international civil aviation in particular traffic regions. A certain amount of governmental regulation of capacity is necessary to resolve the problem and to avoid recurrences. Such necessity is based on the fact that oversupplied routes still exist[186] and that the free play of market forces cannot be expected to re-establish a reasonable balance between supply and demand or to prevent undesirable oscillations and serious losses. This is mainly due to the close correlation between the frequency share and the market share of individual airlines in a given market.

In this respect, the writer recommends that the most effective way to reduce excess capacity is by the device of reciprocal intercarrier capacity reduction agreements subject to regulatory approval.[187] Capacity agreements should be in the hands of carriers as a prime function of responsible management, but subject to governmental

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186. See supra note 144.

187. See supra note 149.

approval in order to better ensure that the public's need for adequate service is met and that the released scheduled or programmed charter capacity is not dumped on other markets.

It is no secret that a regulatory system for controlling capacity cannot be effective unless it encompasses the capacity offered in both the scheduled and the non-scheduled market. As stated earlier, there should be some administration of charter operations to keep a balance between the two categories of air services.[188] The necessity for such interrelated controls is highlighted by the fact that the market being a whole and all of its sectors being interdependent, capacity regulation must be thus subject to a systems approach that takes into account the co-existence of scheduled and non-scheduled traffic. To achieve this end, States should coordinate their policies and regulations with regard to capacity control under the auspices of ICAO. While it is premature to draft a multilateral set of binding rules with a global scope of application, it should at least be possible and useful to establish a set of recommendations in respect of capacity determination in certain traffic regions. ICAO should

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188. See supra, Chapter V, "Preliminary Conclusion" (Criterion "A" recommended by the writer).

therefore be encouraged to convene regional conferences with a view to establish a multilateral framework for coordinating national and bilateral capacity regulations. As a minimum, periodical regional talks on capacity and related problems might become a necessary part of multilateral machinery. Also, such regional meetings must take into account that the minimum of capacity control has to be compatible with a sound and economical operation of international air transportation. One final thing should always be borne in mind: "The history of the era of competition in aviation could serve as a guide for future policymakers; but, the history of the future in air transport should be written now".

CHAPTER VII

THE DETERMINATION OF PRICING IN INTERNATIONAL AIR TRANSPORT

SECTION I -- THE WORLDWIDE STRUCTURE OF RATEMAKING

General View

The possibility of establishing fares and rates[1] by inter-governmental agreement was, inter alia, extensively discussed at Chicago in 1944, but no generally acceptable formula was found. As a practical measure, the Internation-

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1. It may appear appropriate to erect a simple distinction between the terms "fares", "rates", "tariffs" and "ratemaking". The word "fares" links with the prices to be paid for the air transportation of passengers and their baggage, whereas the term "rates" relates to the prices to be paid for the air transportation of cargo. In practice, however, these two terms are often used interchangeably. On the other hand, the term "tariffs" includes both the terms "fares" and "rates". Finally, the term "ratemaking" means the method of determining fares and rates for air transportation. See Haanappel, Ratemaking in International Air Transport at 1 (1978). In this respect, one should also note that the liberal bilaterals, unlike earlier agreements, contain definitions of the terms used in connection with "ratemaking", frequently use the words "price" and "pricing" instead of "tariff" and "ratemaking".

al Air Transport Association (IATA) was created the following year under government auspices - an association of scheduled air carriers to deal, among others, with pricing of international air services subject to governmental approval of any pricing agreement.

IATA was founded as an unincorporated association at the International Air Transport Operators' Conference held at Havana, Cuba, April 16-19, 1945.[2] The Association was subsequently incorporated by a special Act of the Canadian Parliament on 18 Decemer 1945,[3] and since then it has been a substantial force in the regulation of international aviation.

Some years ago, Albert Plesman, a well known pioneer of civil aviation, observed that "the air ocean

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2. IATA is a revitalized version of an old or pre-war IATA that was created in 1919 by six European airlines and which by 1939 its membership had increased to twenty-nine. The pre-war IATA, however, was mainly a European trade association and not, at least formally, involving in international retemaking. For more details, see Hildred, "International Air Transport Association", 1 Air Affairs at 278-79 (1946); "IATA: The First Three Decades", 9 IATA Bull. at 11 (July 1949); 2 IATA Bull. (Dec. 1945).

3. See Yearbook of Air and Space Law, McGill University at 250 (1967); 9-10 Geo. VL, C. 51, as amended by 23 Eliz. II, C. III (1974). This means the Articles of Association which are governed by the Act, and which established the general rules under which the Association functions, cannot be changed without the express approval of the Canadian Parliament.

unites all peoples".[4] But in doing so, air transport itself has generated the need for a unique type of fare and rate pattern. To achieve this end, the IATA ratemaking machinery has endeavoured to enable its members to agree on a worldwide network of tariffs. Such coordinated ratemaking by the airlines was necessitated, first of all, by the fact that "most international air routes are connected and therefore, with a few exceptions, most international fares are a segment of other fares, or bear a relationship to other fares on parallel, overlapping, or matching routes".[5] Secondly, coordination was desirable since most governments opposed a free market pricing mechanism for international civil aviation. Finally, the Americans supported coordination by the air carriers themselves and were opposed to a system where fares would be determined on an intergovernmental basis through some sort of international air authority.[6]

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4. Cited in IATA Agreeing Fares and Rates, Second Edition at 1 (Jun. 1974).

5. Chuang, The International Air Transport Association: A Case Study of a Quasi-Governmental Organization, Sijthoff, Leiden at 71 (1972).

6. See, e.g., Warner, "The Chicago Air Conference, Accomplishment and Unfinished Business", 23 Foreign Affairs at 406 (1945); Proceedings of the International Civil Aviation Conference at 60 et seq.

IATA thus would permit private decisionmakers, the world's airlines, to accommodate competing national interests with respect to the level of tariffs and with a general recognition of the need for stability in international air transport. With air carriers, and not governments, as face-to-face participants, it would be "easier to pursue a climate of negotiation, hard bargaining and compromise without the additional inhibiting effects of direct confrontations involving national sovereignty and honor".[7] Furthermore, there was implied recognition by the States themselves that fares and rates had to be negotiated in the first instance by the airlines, mainly for the following reasons:[8]

(1) The airlines have the financial responsibility for conducting their operations. This means that in order to provide a continuing and efficient service the air

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(1948). In fact, the system which the U.S. had in mind at Chicago followed the example of the already existing Shipping Conferences, groups of liners operating on routes with basic agreements to charge uniform rates. See The Liner Conference System, UNCTAD Report, U.N. Doc. TD/B/C. 4/62/Rev. 1 (1970).

7. See "New CAB Authority over International Air Fares", 5 N.Y.U.J. Int'l L. & Pol. at 288 (1972).

8. See IATA's Working Paper submitted to the 1980 Conference, AT Conf/2-WP/13 at 3 (11/1/80) (hereinafter cited as IATA's WP/13).

carriers must maintain an economically viable operation,, whether they are privately owned or financed, are of mixed ownership, private and government, or wholly government owned.

(2) Only the airlines have the intimate knowledge concerning their operational capabilities, costs and through their own and industry consumer research, their market requirements. In most cases also the carriers were required to operate economically and to be financially self-sufficient.

(3) Separately negotiated bilateral tariff agreements would produce only an incoherent structure with traffic diversion and unacceptable standards of service to the general pbulic. Multilateral tariff negotiations on the part of the carrier operators were thus seen to be a means to:

(a) facilitate interlining and multi stop-operations;

(b) avoid subsidy wars between national flag carriers;

(c) ward off head-to-head government conflict; and

(d) avoid an incoherent structure of fares and rates.

Ultimately, of course, the IATA activities would be kept in constant check by governments, since none of the IATA's fare Resolutions could become effective without the approval of

the States concerned.[9]

The Bermuda I Agreement of 1946 confirmed that scheduled international fares were to be first agreed by the airlines (through the IATA pricing machinery) and then submitted for approval of both governments.[10] With the exception of recent American liberal bilaterals,[11] the great majority of the some 2000 bilaterals (concluded throughout the world after Bermuda I) follow the Bermudan example and delegate, either explicitly or implicitly, international ratemaking to IATA, again subject to approval by the concerned governments.[12] In this respect, one should remember that bilateral agreements of States whose national carriers are not IATA members, usually do not refer to the IATA ratemaking machinery. Instead they generally provide that fares and rates shall be determined by the

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9. For a good review on the evolution of the international legal process for the regulation of air fares, see "the Ins and Outs of IATA: Improving the Role of the United States in the Regulation of International Air Fares", 81 Yale L.J. at 1105-27 (1972).

10. Se infra Section II of this Chapter.

11. An important exception, as will be seen in Section III (footnote 113) below, is the German Protocol.

12. See "International Air Transport Association", in 5 Encyclopedia of Public International Law, North-Holland at 50 (1983).

designated carriers of the two concerned Parties, subject to governmental approval. Those non-IATA airlines, however, are still indirectly bound, to a considerable extent, by the existing IATA tariffs due to the dominance in international markets of IATA members.[13]

In this vogue, the international ratemaking system has emanated, whereby tariffs for scheduled air transport are set up through IATA, under government authority - given by the pricing provisions in bilateral agreements - and under government control - retained in those bilaterals. One can therefore observe that this ratemaking system is a worldwide one, and can as such be regarded as a "multilateral" regime. Paradoxically, it derives its authority from a bilateral regime, the existing network of bilateral air transport agreements. However, this ratemaking system does not encompass tariffs of non-scheduled internatinal operations which are ordinarily determined by the individual charter operators on the basis of the law of supply and demand with a limited degree of governmental intervention, i.e. by the free forces of the marketplace.[14]

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13. Taneja, Airlines in Transition at 86 (1981).

14. It has to be remembered here that IATA in 1974 decided to let charter airlines become members, whereby they would be entitled to vote on charter matters only. This amendment, however, never came into force due to the lack of necessary governmental approval. See

The machinery used by the member airlines to reach agreements on scheduled international air fares and rates and relevant conditions is provided by the IATA Traffic Conferences. While they form an integral part of the structure of the Association, the Traffic Conferences represent in some respect self-contained entities which operate in accordance with special rules and regulations. They derive their legal existence from Article VIII(5) of the "Articles of Association" and are governed by the "Provisions for the Conduct of the IATA Traffic Conferences", as amended in 1978.[15] Conference costs are also met from separate budgets voted by the Conferences themselves.

The Traffic Conferences thus function (more or less) independently from the rest of IATA, but membership, voting, or non-voting in a Conference is contemporaneous with membership in IATA.[16] Since 1978 (when the reorien-

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Brancker, IATA and What it Does at 13 (1977). Moreover, one should note that the regulation of charter tariffs has recently been incorporated into a few liberal bilaterals.

15. See infra (IATA's 1978 Restructuring).

16. "IATA Traffic Conferences Provisions", Section 2 (Paras. 1-3) T.C. Amendments No. 44-45; see also Haanappel, Pricing and Capacity Determination in International Air Transport at 94-101 (1984).

tation of IATA's activities took place), such Traffic Conferences have consisted of six different Conferences. Four are "Procedures Conferences": Passenger Services Conference, Passenger Agency Conference, Cargo Services Conference and Cargo Agency Conference.[17] The remaining two are concerned with tariff coordination: Passenger Tariff Coordinating Conferences and Cargo Tariff Coordinating Conferences.[18] In this connexion, one should also note that, for administrative purposes, the world is geographically divided into three areas that collectively cover all regions of the world.[19] These three are supplemented by joint conferences to deal with matters that affect more than one Conference area and a so-called "composite meeting"

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17. These Conferences take action of such matters as passenger and baggage handling documentation, reservations, ticketing, technical specifications restricted articles, etc... For the purpose of this work, however, an emphasis is only given on the Tariff Conferences activities.

18. For tariff coordination purposes, such Passenger and Cargo Conferences are divided into fourteen Tariff Coordinating Conferences covering both passenger and cargo matters. See "Provisions for the Conduct of the IATA Traffic Conferences", Article I(1)(2) (1978).

19. These areas are commonly known as TC1, TC2 and TC3. In this classification, TC1 is concerned with North and South America, TC2 with Europe, Africa and the Middle East and TC3 with Asia and Australia. See id. Article 1(3).

that concerns with issues on a worldwide basis. In addition, there are numerous geographical sub-areas created in each Conference. However, the Conferences themselves, and the sub-areas are subject to increase, decrease and change in boundary by the IATA Executive Committee at any time.[20] Finally, it is worth observing that fare and rate agreements between IATA airlines are, at the present time, often reached within small sub-areas of Traffic Conferences rather than in a whole Traffic Conference area.[21]

As to IATA Tariff Coordinating Conferences, their activities consist essentially of negotiation by the airlines of passenger fare and cargo rate levels and conditions as well as levels of agency commissions, with the aim of developing and adopting binding agreements (issued in the form of Resolutions) for submission to governments for approval. Each of these Tariff Conferences has responsibility for tariff matters affecting a particular geographic area. However, matters involving an area larger than one specific Conference are considered, as has been shown, at composite meetings of all Conferences involved.

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20. Id. Article XV.

21. See Reports and Proceedings of IATA Annual General Meetings.

For the purpose of this work, it is appropriate to briefly discuss the main procedures for setting up scheduled international tariffs.[22] The first step in the process is to agree on a comprehensive pattern of specified fares based on the use of the basic currencies (U.S. dollar and pound sterling). The next pace is to compute, using the agreed construction rules, all other normal fares to meet the particular needs of individual carriers.[23] This procedure is a reasonable one given the almost half-million fares in use. It should be noted, however, that a number of factors have to be taken into account before establishing the basic normal fares. These include, inter alia, distance, specific needs of States with respect to promotion of tourism, specified requirements of the airlines primarily interested in the routes in question, availability and nature of competition (non-IATA carriers, charter operators, etc.), price elasticity of demand, anticipated demand patterns in related city-pairs and, of course, costs. Added

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22. For the detailed procedures, see "Manual on the Establishment of International Air Carrier Tariffs", ICAO Doc. 9364 at 30-34 (1983) (hereinafter cited as ICAO Manual on Tariffs).

23. It has to be remembered that passenger fares fall into two categories: normal fares and special fares. Special fares are lower in price than normal fares and therefore the passenger must satisfy certain eligibility requirements to get these lower fares.

to this general list of factors are the route-linking strategies of individual carriers, a factor that affects not only traffic but also costs.[24]

In fact, the process of hammering out an agreement to change tariffs has been confined to the Tariff Conferences, where the individual interests of the carriers, and indirectly of their governments, can be safeguarded without recourse to open economic warfare.[25] In this respect, IATA members would respectfully submit that where governments find it necessary to provide instructions to their airlines before or during a Conference (and particularly if they should make public statements of policy positions for Conference guidance) they should endeavour to take into consideration, to the extent possible, the positions of

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24. As to the transportation of air goods, two different rate systems can be adopted: the flat rate and the differential rate system. A flat rate system implies a standard rate per kilometer flown for a certain quantity of goods, regardless of the distance over which the goods travel and of the type of goods. A differential rate system implies a varying rate per kilometer, depending on the type of goods, distance and the market in question. There are also general cargo rates, class rates and specific commodity rates. For further detail, see, e.g., Haanappel, op. cit., note 16, at 103-104; Rosenfield, Regulation of International Commercial Aviation in Booklet No. 14 (Nov. 1984).

25. See IATA's Working Paper submitted to the 1977 Conference, SATC-WP/7 at 5, Para. 15 (10/1/77).

other governments, and to express their views in such a manner as to permit compromises to be made in order to reach agreement.

In principle, each Conference meeting aims to reach a consensus on both general levels of tariffs and specific tariff proposals on a full Conference basis, in which case the agreements reached would be binding on all Conference members, whether or not represented at the meeting.[26] In practice, however, most full area Conference meetings at some stage refer some or all of the activities to such-area meetings with the objective of reaching agreement on a sub-area basis, either to be incorporated in a full area agreement or failing this to stand as a formal sub-area agreement.[27]

From the regulatory viewpoint, all the Resolutions of IATA Conferences require the approval, express or implied, of all interested governments before they can take effect. If a government disapproves a Resolution, the

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26. ICAO Manual on Tariffs, op. cit., note 22, at 29-30.

27. See supra note 21. In some cases, however, the agreements achieved may be with restricted Traffic Conference member participation under the limited agreement procedure.

Resolution will not come into force.[28] Many governments find it necessary or expedient to place reservations on their approval of a particular Resolution; such Resolution will only take effect subject to such reservations. It is always recognized that governments can and do give specific directions to their carriers. The obligation of such carriers to comply with such directions overrides their obligation to comply with IATA Resolutions[29] conflicting with such directions.

Indeed, IATA has no status to formulate or implement binding policies for the conduct of air transport services. It merely provides the suitable place in which IATA members can meet to discuss conflicting views and interests and hopefully resolve them through the medium of inter-carrier agreements which are expressed in the form of Traffic Conference Resolutions. In other words, such "multilateral tariff coordination" provides an apolitical forum in which the hundreds of thousands of fares and rates required to form the world air transport network can be

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28. For the impact of governments on IATA's activities, see Hammarskjold, "Trends in International Aviation and Governmental Policies", in Aeronautical J. at 153-54 (May 1980); Haanappel, op. cit., note 16, at 109-112.

29. See Sion, "Multilateral Air Transport Agreements Reconsidered", Va. J. Int'l L. at 182 (1982).

coordinated. This undoubtedly provides substantial economic benefits through minimizing organizational and administrative costs which would otherwise be incurred in the development, negotiation and filing of tariffs on each individual route.

For almost thirty years, IATA's traditional voting rule in the Traffic Conferences was "one of unanimity". Binding Resolutions could only be adopted by the "unanimous affirmative vote of all voting member airlines present and voting",[30] each voting member having one equal vote. The benefit of this rule was that a majority of small IATA carriers could not outvote a minority of large IATA airlines, and also, of course, that no single airline would be bound by a Resolution against its will. The disadvantage of the unanimity rule was that a Traffic Conference agreement could be blocked by an airline having, for example, no direct interest in a particular fare or rate. It is often argued, therefore, that decision-making by unanimity can only produce the "lowest common denominator" of the different positions of the participants in the decision-making process.[31]

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30. See supra note 25, at 6, Para. 26.

31. Klem & Leister, "The Struggle for a Competitive Market Structure in International Aviation", 11 Law & Pol'y Int'l Bus. at 565 (1979).

IATA members, however, were remarkably cautious in modifying the unanimity rule. Seemingly, they could not replace the unanimity principle on matters of vital commercial significance with a simple or qualified majority principle. But because of new competitive pressure during the 1970's (particularly on the North Atlantic) from charter operators, several IATA members sought a modification of the unanimity rule so as to allow affected scheduled airlines to respond with lower fares, without the threat of a veto by less competitive - minded members. In 1975, this unanimity rule was thus relaxed to provide for (a) limited agreements in which fewer than all members of a Conference could participate and which would bind only those participating members; and (b) the creation of sub-areas within the three existing Conference areas whereby those carriers operating under third, fourth, or fifth freedom traffic rights would exercise primary voting rights, and those carriers with an indirect interest would suffer some restriction of their veto rights.[32] These changes, together with further innovations, were then formalized (as will be seen below) during IATA's 1978 reorganization of Traffic Conference

32. For a review of the 1975 amendment to the unanimity rule, see Aubry, "IATA and the Changing Industry Environment", 1 Annals of Air and Space Law at 263 et seq. (1976); "IATA Limited Agreement Concept", 32 Interavia at 105 (1977).

procedures.[33]

As evident from the preceding brief survey, IATA Traffic Conferences are the most widely recognized forum for the negotiation of international air tariffs. It should, however, be emphasized that these Conferences are not the only multilateral machinery in which international air fares and rates are negotiated. There are at least a dozen other regional multilateral mechanisms involved in coordinating tariffs amongst their member airlines.[34] While varying roles are played by each of these mechanisms, virtually all

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33. See supra note 15.

34. For the descriptions of these regional bodies, see ICAO FRP/2-Report at 10-12 (Nov.-Dec. 1977); ICAO Manual on Tariffs, op. cit., note 22, at 4, 34-39. In this respect, it may appear appropriate to also mention the 1967 "International Agreement on the Procedure for the Establishment of Tariffs for Scheduled Air Services", concluded between the 15 countries in Western Europe. This Agreement is largely based on the existing ratemaking system, i.e. the use of IATA pricing machinery subject to governmental approval. If the Parties already have a bilateral agreement including a tariff clause, then the 1967 Agreement will replace such bilateral. Although the 1967 Agreement was reached within the framework of ECAC, its scope is open for accessions by any member State of the UN or any of its specialized agencies. For the text of the Agreement, see Bradley & Haanappel Eds., Government Regulation of Air Transport at 134 (1982). It is significant, however, to note that the ECAC has been considering the possibility of a new modified agreement to replace the original, but so far no progress has been achieved. For the wording of the new agreement, see ECAC, Doc. INFA Report (30/5/80), Appendix IX; supra, Chapter III, Section IV (footnote 189).

have an interrelationship with IATA's Conference machinery. They coordinate their tariff activities, to a greater or lesser extent, with those of IATA, and in some cases they hold regional meetings prior to IATA Tariff Conferences in order that their member airlines may reach joint positions for development in the IATA forum. Nevertheless, a critical distinguishing feature of the IATA machinery is that it is the sole multilateral coordinating mechanism with worldwide applicability. It is, therefore, to the advantage of any State that its national carriers should be represented in the negotiation of international air tariffs through a machinery which is capable of melding regional requirements into a worldwide air transportation system.

Show Cause Order

During the period between 1946 to 1978, the United States CAB had continuously approved, although sometimes grudgingly, the IATA agreements relating to international air fares and rates.[35] This approval was explicitly

35. In the United States, the CAB had (until January 1, 1985) the responsibility of reviewing and approving IATA developed fares. Since then, this authority went to the DOT (instead of DOJ) when President Reagan signed a Compromise Bill amending the original Deregulation Act of 1978. See Flight International at 1025 (Oct. 20, 1984). For the reports of the House

required in order to relieve IATA's rate-fixing activities from the operation of the American antitrust laws.[36] Historically, the first approval was obtained on February 19, 1946 for a period of one year. It was then renewed in 1947, 1948, 1952 and, from 1955 through 1978, the approval became permanent.

A large portion of the credit was given to IATA for the progress made by international air transport. The CAB

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and Senate discussion, see Congressional Record-House on CAB Sunset Act (Sept. 19, 1984).

36. One has to remember that IATA's ratemaking resembles price fixing, which is illegal under the antitrust laws of the U.S. See, e.g., United States v. Socony-Vacuum Oil Co. 310 U.S. 150 (1940); Sherman Antitrust Act, an Act to protect trade and commerce against unlawful restraints and monopolies, Act of July 2, 1890, 26 Stat, 209, as amended; the Clayton Act which was enacted in 1914 to strengthen the Sherman Act. In order to shield IATA from claims of illegal price-fixing, Congress established a two-step procedure for the conferral of antitrust immunity on IATA tariffs. Under Section 412 of the Federal Aviation Act of 1958, all IATA tariff agreemetns were required to be filed with the CAB. The CAB would then approve such agreemetns unless they were "adverse to the public interest". Under Section 414 of the same Act, such approval would guarantee antitrust immunity. Moreover, the immunity-conferral procedure was later amended in 1979 to provide for discretionary (instead of mandatory) filing of rate-fixing agreements. For a good brief review on the CAB's authority to exempt the airlines from antitrust regulations, see Pentis, "Public Interest Under the Federal Aviation Act of 1958 and the Airline Deregulation Act of 1978", Northrop University Law Journal at 83 (1983); Haanappel, op. cit., note 16, at 83-86.

cited IATA's contribution to the establishment of worldwide integrated tariffs, its uniform procedures and documentation, and its elimination of restrictions in international travel. It is not surprisingly therefore that IATA, despite some drawbacks, was accented in Presidential Policy Statements as the most practical system available.[37]

Indeed, a healthy industry system, combined with a government approval process, constituted the most practicable overall machinery for the establishment of international tariffs. If there is one lesson beyond dispute which can be drawn from the past 40 years of development, it is that "a great deal of quasi-governmental negotiation can be effectively made in such a forum (IATA ratemaking machinery) which could not be resolved by governments directly".[38] Surprisingly, however, this highly publicized system began to be criticized and was accused by the United States of being a "closed shop" which excluded all competition between airlines.[39]

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37. See, e.g., the 1963 Statement on U.S. International Air Transport Policy, 30 J. Air L. & Com. at 76 (1964).

38. Hammarskjold, op. cit., note 28, at 154.

39. See Report of the Subcommittee on Investigations and Oversight of the Committee on Public Works and Transportation, U.S. House of Representatives, at 5 (1983) (hereinafter cited as the Levitas Sub-

During the second half of the seventies, the American government, committed to the principle of free trade in international aviation, exhibited growing concern about IATA Traffic Conferences and threatened to apply anti-trust regulations to international air transport affecting the United States. The first real attempt to make major structural changes in international air policy came with Carter Administration's "open skies" policy. In the process of deregulating domestic air transportation, it was decided to also deregulate international air transportation.[40] In June 1978, the CAB - never a supporter of the IATA - determined therefore to take its new, procompetitive philosophy to its logical conclusion, which meant attacking what it viewed as "thinly-veiled" price fixing.

In its "Show Cause Order", the CAB directed IATA and other interested persons to "show cause" why it should not make final its tentative finding and conclusion that the tariffs negotiated through the IATA Traffic Conference machinery were no longer in the public interest and thus

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committee).

40. Id.; supra, Chapter II, Section V; Chapter III, Section III.

should no longer be approved.[41] In other words, the CAB questioned whether United States airlines should continue to receive antitrust immunity allowing them participation in IATA Tariff Conference fare-setting. It also questioned whether foreign airlines flying to the United States should be immune from antitrust prosecution if they conferred to set tariffs on American-bound routes. Finally, IATA and other interested parties were required to "show cause" why the CAB should not finalize its tentative findings.

The CAB's unilateral proposal to withdraw its approval of the IATA's pricing activities caused serious concern in the international aviation community. Approximately ninety States, through their Foreign Ministers or Civil Aviation Authorities, made formal submissions on the issue to the American government; the overwhelming majority of them opposed to the CAB position. Also, forty-five or so of international airlines protested to the CAB in support of IATA, together with several regional organizations and other different agencies.[42] In fact, the CAB's action raised

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41. CAB Order 78-6-78, June 12, 1978; Magdelenat, "The Story of the Life and Death of the CAB Show Cause Order", 5 Air Law at 83 (1980).

42. Significantly, even the U.S. State Department and DOT are in the record as being opposed to the CAB investigation. See, in general, Bornemann, "Air Transport Organization and Policy", ITA Bull. at 57-58 (Feb. 23,

momentous matters of international comity, posed serious potential for disruption of a relatively smoothly working integrated international aviation system and even suggested, according to some commentators, "the strong possibility of even greater government intervention in the formulation of tariffs, a course which would contradict U.S. policy to restrict government regulation".[43] It is apparent, therefore, that the CAB was ignoring basic differences between domestic and international air services and was attempting to force the American antitrust free competition policy on the rest of the world.

There is a further aspect which seemingly has not been well addressed in any of the above submissions, but which nevertheless is increasingly important in the international environment. As fundamental conflicts have arisen between national regulatory policies over the past seven years, there is a well recognized trend towards forms of

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1981); Gidwitz, The Politics of International Air Transport at 98-99 (1980); Griffiths, "IATA Hits U.S. Threat to Ratemaking", Aviation Week & Space Tech. at 27 (Jan. 8, 1979). One should also note that the world aviation community, through the Second Air Transport Conference, firmly supported the continuation of IATA multilateral system, see infra Section V.

43. Taneja, U.S. International Aviation Policy at 94 (1980). See also supra, Chapter IV (footnote 170).

protectionism. This is a matter of concern to many governments and threatens the viability of a multilateral worldwide air services network. It is interesting, however, to note that this problem was recently considered by an influential United States Congressional Subcommittee (the Levitas Subcommittee).[44] The Subcommittee's Report directly attacked the impact which the CAB's Show Cause Order had had on the American international relations, stating that:

> "The IATA has been a multilateral forum for establishing airline fare structures for many years. Although it has limitations, it still has the strengths of airline involvement in a multilateral forum to develop fare schedules subject to approval by the governments involved. The CAB Show Cause Order and the 'open skies' policies have seriously undermined IATA and possibly caused the airlines and foreign governments to pursue nationalistic policies with respect to the United States - such as escalation of unfair discriminatory practices."[45]

In other words, one can say that the Subcommittee clearly describes an important distinguishing feature of international aviation, as opposed to domestic trade forms; it emphasizes that co-operative activities between national flag carriers can play a vital role in limiting friction between governments. In addition, this highlights the need

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44. See the Levitas Subcommittee, op. cit., note 39.

45. Id. at 16.

for caution in comparing various domestic deregulation experiments with the international system.[46] Co-operation between airlines, as "flag carriers", provides valuable practical and quasi-diplomatic benefits; also, there is little prospect that governments will collectively relax bilateral controls on routes, market entry and capacity/frequency. In these circumstances, decontrol of pricing would not necessarily produce lower fares and would almost certainly invite inter-governmental conflict - to the consumer's disadvantage.

From the American government's point of view, however, the basic issue was one of competition rather than regulation as the best method for allocation of scarce resources. The United States substantiated its claim by showing that liberalization of non-scheduled rules has

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46. It is significant to note that the U.S. is not the only nation involved in this process. The Australian Trade Practices Commission (TPC), on July 31, 1984, issued a "Draft Determination" notifying its intention to liberalize pricing in overseas air services, a consequence of which would be the prohibition of any form of industry tariff enforcement. This "Draft" was finally issued on October 31, 1984. However, the TPC on 14 March 1985 granted IATA an interim authorization (antitrust immunity) for all IATA activities in Australia. This immunity will last until the TP Tribunal gives a final judgment on the IATA's appeal against the TPC's October 1984 decision. For further detail, see IATA Regulatory Affairs Review, Vol. 13, No. 3 at 248 (Jun.-Sept. 1984); id. Vol. 14, No. 2 at 107 et seq. (Feb.-Mar. 1985).

resulted in lower fares for a greater portion of the travelling pubic, and has led to more responsive competitive filings by the scheduled carriers.[47] No one denies that charters have provided a competitive spur to the scheduled carriers. The introduction and expansion of non-scheduled operations exhibit what intelligent and enlightened regulation can do to make the marketplace more competitive. It should always be remembered, however, that the Americans and some other nations did this within the existing regulatory framework, illustrating that the regime is flexible and can accept constructive changes. Now the United States felt compelled to entirely dismantle the regime, an action which would not only disrupt a regime built over thirty years, but which would not guarantee that international fare decisions would be made solely on the basis of economic considerations. On the contrary, it is more likely that these decisions would be dictated by political or bureaucratic considerations.[48] In any event, it is ironical that the United States, by giving the charter operators scheduled

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47. See supra, Chapter V, Section IV (Generalities and Analysis).

48. See, e.g., Hammarskjold, "One World for Fragmentation - The Tool of Evolution in International Air Transport", Annals of Air and Space Law at 82-83 (1984).

authority, may have killed a real competitive spur to the scheduled airlines.[49]

The Americans considered the IATA pricing machinery to be adverse to the public interest, since it violates the American antitrust laws. In the United States, the Sherman Antitrust Act of 1890 states that every contract or combination in restraint of trade among the States or with foreign nations is illegal, i.e. the Act prevents the creation of cartels or monopolies.[50] The appropriateness of the Sherman Act is, however, not clear. It assumes, for example, that if there were no private agreements, a competitive market would exist. But it is proven that in international air transportation, a purely competitive market cannot exist,[51] even in the absence of a private agreement (e.g. IATA). And since the IATA coordinated tariffs are ultimately submitted to the affected nations for their review and approval before they become effective, it is obviously debatable whether they are cartel agreements

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49. See supra, Chapter V (footnote 63).

50. See supra note 36.

51. This is mainly because the regime of international air transportation is firmly founded on State sovereignty with route entry, supply and tariffs being dictated through thousands of bilateral and multilateral agreements. See supra, the whole Chapter I.

and not in the public interest.[52]

The fact of life in international air transport is that the regime of competition is pregnant with various kinds of obstacles and risks. It is hard to believe that a reasonably competitive pricing system would exist in the absence of IATA worldwide pricing agreements. After all, every State has a legitimate right to regulate any segment of commercial aviation operations serving its territory and to protect traffic volume and market share for its "flag carriers". Since most nations could still act unilaterally against any particular fare, demolishing the IATA ratemaking system would not automatically produce price competition. Instead, it is believed that the lack of an integrated system is likely to result in higher costs to the consumers and financial instability to the airline.[53] Eser, Director General of IATA, stressed these facts when he has recently observed that "States will not allow foreign economic considerations and interests to control such an

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52. In addition, "IATA does not allocate markets or determine the extent of participation in them by its members", O'Connor, An Introduction on to Airline Economics at 110 (1982).

53. See, e.g., Lazar, Deregulation of the Canadian Airline Industry: A Charade at 26 (1984); Meyer; Oster; Maorgan; Berman & Strassman, Airline Deregulation at 3 (1981).

industry".[54] In other words, dismantling IATA in no way guarantees the existence of free market forces.

Notwithstanding the validity of the above well established facts, the "sunsetted" CAB was never convinced to bring the "ill-conceived" Show Cause proceeding to its end. Instead, the Board found that IATA pricing machinery substantially reduced competition in the provision of international air transportation services to and from the United States.[55] Nevertheless, it discovered (after intensive pressure from the Departments of State and Transportation) that continued approval of the multilateral machinery was required because of considerations of international comity and foreign policy. A grant of antitrust immunity was hence given to IATA in April 1980 for a period of two years, subject to a number of conditions, the most significant one being that United States Airlines would during this period not be allowed to participate in IATA's North Atlantic Tariff Coordinating Conferences. This Order, however, was not made final until May 1981, and even then the effectiveness of the Order was stayed until September 1981. It should also be noted that the effectiveness of the May 1981

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54. Remarks by Eser to European Parliament Committee on Transport Public Hearing on Civil Aviation at 7 (21-22 Feb. 1985).

55. See CAB Order 80-4-113, April 15, 1980.

Order was stayed twice more temporarily in September 1981 and January 1982, until its effectiveness was stayed indefinitely until further order of the Board in March 1982. The March 1982 Order might have shelved the proceeding indefinitely to make place for the first United States-ECAC Memorandum of Understanding which, as will be seen later, specifically envisaged the use of (IATA) multilateral tariff coordination on the North Atlantic.[56] Therefore, as a consequence of this Memorandum, approval of IATA Traffic Conferences was renewed twice until May 6, 1985.

It is apparent, however, that international pressure put on the American government began to take its toll. In a recent action, the United States DOT issued an Order on May 6, 1985, granting further approval and immunity from the antitrust laws to the IATA ratemaking machinery.[57] Although no term had been set upon that approval or immunity, IATA is required to resubmit its agreement governing the operation of its Traffic Conferences five years from the date of the Order's issuance. In fact, such Order constitutes the DOT's final decision in the Show Cause

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56. See infra Section IV. In fact, the negotiation of this Memorandum has made an automatic withdrawal of approval from the IATA Traffic Conferences inappropriate.

57. DOT Order 85-5-32, May 6, 1985.

proceeding and, with its issuance, the proceeding has come to a close. But, to reaffirm its reliance on free market forces, the DOT reserves the right to review its approval and immunity at any time as required in the public interest. This commitment is explicitly highlighted in the following statement made by the DOT:

> "We will continue to preclude IATA from expanding its role in international air transportation in a manner adverse to competition or the public interest, by, for example, undertaking tariff enforcement activities."[58]

With this new Order in mind, it may seem appropriate now to recognize that the CAB essentially gave very little thought to its Show Cause action and even less thought to the consequences of such a proposal. According to one Board member, for example, the action to launch such an extensive examination resulted from a "single, brief, closed-door session on a Friday afternoon".[59] It would almost appear, therefore, that the Board singlehandedly desired to institute a change in the whole system, just for the sake of a change. Instead, an open dialogue, a respect for the sovereignty's principle, an opportunity to exchange views and consideration of international comity are more

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58. Id. at 4.

59. Cited in Taneja, op. cit., note 43, at 99 (footnote "d").

likely to result in an acceptable and more efficient framework for multilateral negotiations. Indeed, any viable alternative to the existing, and most definitely to the restructured, IATA is likely to prove far more detrimental to the public interest.

IATA's 1978 Restructuring

Since the development of the IATA Traffic Conferences in the 1940's, the dynamic changes impacting on international air transport have not occurred in vacuum. The Conference machinery has been regularly updated in order to adapt to the evolving needs of governments, airlines and the marketplace.

The most far-reaching modifications to the Conferences and their procedures, however, occurred in mid-1978.[60] But preparations for this reform were under consideration for some time. In November 1977, the IATA Executive Committee appointed a five member Task Force consisting of the chief executives of five airlines (Air

60. In fact, these changes had their roots in concerns raised within the membership as far back as 1975. During its Thirty-First Annual General Meeting, therefore, IATA introduced some modifications to its Conferences. See Aubry, op. cit., note 32, at 264-65.

Canada, Air India, Alitalia, British Airways and TWA) to examine in detail the Traffic Conference activities in the light of the present and anticipated future environment. This examination took into account the most recent policy expressions of governments, together with the need for greater flexibility, for carrier innovation and differences in route development.

The Task Force Report was completed in April 1978 and its recommendations were accepted unanimously by the Executive Committee in May 1978. These recommendations were the subject of intensive discussion at a Special General Meeting held on June 30-July 1, 1978, in Montreal. The meeting accepted, in principle, all of the Executive Committee recommendations.[61] The necessary amendments to the Traffic Conference Provisions, taking into account comments made by members at the Special General Meeting, were adopted by the Executive Committee in mid-September 1978. The revised Provisions were then submitted to interested governments and they took effect on 1 October 1979.

Thus, prior to the initiation of the CAB Show Cause

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61. See IATA Recommendations of the Executive Committee on Traffic Conference Procedures and Objectives, Revised 13 June 1978; Doty, "IATA Members Approve Restructuring", Aviation Week & Space Tech. at 35 (Nov. 27, 1978).

Order proceedings, IATA had recognized the need for modernization. But while it is true that the reorganization was an almost immediate response to the Order, there were some other significant motives. Firstly, the tariff negotiations had become more complex as more governments, airlines and routes became involved; secondly, the operations of non-scheduled air carriers had made an increasing impact on the scheduled airline industry; thirdly, some airlines and governments were leaning towards market forces for regulating tariffs in certain major markets; and finally, the whole system came under ICAO scrutiny.

The main characteristics of IATA's reorientation may be summed up as follows:

(1) The activities of IATA have been regrouped into two categories:

(a) trade association activities with mandatory membership; and

(b) tariff coordination activities with respect to passengers, cargo, or both matters with optional membership.

(2) While the existing three individual Tariff Conferences and the four joint Traffic Conferences are retained; the existing sub-area provisions were redefined to ensure that negotiations would be more responsive to regional market requirements.

(3) The provisions with respect to limited agree-

ments were made permanent.[62]

(4) The Traffic Coferences recognized the prime interest of third and fourth freedom carriers in establishing the fare levels for traffic carried at the lowest fares, without veto from other members interested, for example, in increasing fares to reflect additional costs associated with prorating.[63]

(5) Members were allowed to introduce, on third and fourth freedom routes, innovative fares responsive to changes in the market, without rescinding the existing fare agreements.

(6) Carriers were allowed to compete more freely by eliminating conditions relating to in-flight service in the following manner:

(a) conditions of service pertaining to meals, bar service, sales on board and in-flight entertainment could no longer be the subject of agreements;

(b) conditions of service could be reviewed with respect to givaways; and

(c) all Resolutions would be reviewed to eliminate any unnecessary regulation.

(7) The ICAO Secretariat are invited to the

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62. See supra note 32.

63. It is important to note that this change responded directly to SATC/1 - Recommendation 17. For ICAO Work, see infra Section V.

Traffic Conferences with observer status, while other Parties are permitted to present their position to the Conferences, initially in writing and, if necessary, supplemented by oral presentation.[64]

(8) The IATA compliance program was redefined to place more emphasis on preventive as opposed to punitive aspects.

(9) The Executive Committee modified the terms of reference of the Traffic Committee and the Industry Policy Committee.

According to Hammarskjold, IATA's former Director General, this reform was essential and not cosmetic in appearance, because "it has meant compromises between proponents of conservative regulation and the advocates of liberal competition. It has moved the machinery firmly in the direction of modernization, thereby allowing greater innovations and flexibility for individual participants". He also added that by multilateral consensus "liberalization" has been generalized throughout the world network in one full swoop.[65] Moreover, the member airlines of IATA

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64. In fact, the amendment was a direct response to the concern expressed by the ICAO-FRP, that the machinery did not take sufficient account of the interests of air transport users and also to SATC/1 - Recommendations 6 and 7.

65. Hammarskjold, op. cit., note 28, at 153-54.

have believed that this reorganization "has - through increased flexibility, openness and scope for innovation - ensured that their task of multilateral tariff coordination can maintain and expand upon the public service benefits it provides to the international aviation community."[66] Even the United States DOT has found that the modifications are significant, since they "have reduced their (IATA's Traffic Conferences) adverse impact on competition".[67] It is, therefore, undebatable that the 1978 modifications provide the needed flexibility to make the tariff coordinating process more responsive to the changing market and regulatory conditions. In short, the IATA machinery has the capability to evolve as the environment, within which it functions, changes.

The worldwide community has generally given its approval to the new IATA machinery as evidenced at the 1980 Air Transport Conference. The increased "flexibility" and "innovation" in tariff coordination would, to a considerable extent, solve the problem inherent in seeking multilateral consensus on tariffs. In addition, the regrouping of Traffic Conferences into many sub-areas permits increased emphasis on the market knowledge and tariff requirements of

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66. See IATA's WP/13, op. cit., note 8, at 10.

67. DOT Order 85-5-32, op. cit., note 57, at 4.

airlines with major commercial interests in those areas.

Contrary to the beliefs voiced by various airline officials and commentators, the writer is of the opinion that "limited agreements" and "innovative tariffs" do not constitute a shift towards regionalism, as opposed to multilateralism in international air transport.[68] Rather, this is a drift towards what may be termed "decentralization" of the IATA machinery which allows local difficulties to be solved by local decisions, without the unanimous vote of every one. Thus, while de facto the unanimity rule is still in effect, market practices dictate different consequences. With regard to "innovative tariffs", it is evident that this progress provides the capability for carriers to deal with rapidly changing conditions, government policies and consumer requirements. In this regard, it is generally believed that the filed fares are not always what the market needs.[69] The need, therefore, to fill seats (during the recession) led IATA

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68. See, e.g., Wassenbergh, "Reflections on the Sixth Freedom Question", in Wassenbergh & Fenema Eds., International Air Transport in the Eighties at 193-94 (1981); Feldman, "Regionalism Could Cloud IATA's New Beginnings", Air Transport World at 61 (Jan. 1980); Haanappel, op. cit., note 16, at 115.

69. See Wheatcroft, "Revenue Erosion - The International Background", IATA Review at 14 (Jan.-Mar. 1984).

members to offer discounts to such an extent that the Association had to find an immediate response so that Conference tariffs did not appear ludicrous. Such innovations do not undermine IATA's multilateralism; in fact, they enhance it.

Despite the continuous endorsement of IATA's new rate-setting machinery, some other general criticisms are still heard.[70] Given the diverse objectives, trends and philosophies of various nations, the IATA negotiated solutions may not have been ideal, but the Association has been successful in reconciling such dissimilarities. This is prima facie evidence that it is the best arrangement available, regardless of some major problems.

As a conclusion to this section, it should be recognized that IATA's multilateral process, despite its imperfections, represents the optimal method of negotiating international tariffs. The system offers definite benefits to consumers, carriers, governments and the international community at large. For the users, the system provides the formation and maintenance of a worldwide process; an interline network that permits travel between any points in the world on a single ticket, paid for in their national

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70. See, e.g., O'Connor, op. cit., note 52, at 110-12; Sion, op. cit., note 29, at 187, when he predicted that the Association would soon cease to exist.

currency; and providing a focal point for organizing world-wide tariff concepts. For the airlines, the system offers a democratic, non-discriminatory forum for participation in tariff negotiation, interline and prorate arrangements, and the creation of standardized procedures - all necessary elements in the long-term planning. For the governments, the system allows different nations to reconcile their conflicting national interests and objectives in an apolitical forum. Finally, the system is unique in assisting conditions of fair competition, the maintenance of a world-wide regime in which transnational interests can be best served under an otherwise unconnected bilateral network.

SECTION II - THE BERMUDA PRICING STANDARDS

The Bermuda I Ratemaking System

The Bermuda I Agreement was the first bilateral in which an undertaking was made with respect to tariffs.[71] In particular, a ratemaking system is contained in Annex II to the Agreement.

Paragraph (a) of Annex II establishes the principle

71. Cooper, "The Bermuda Plan: World Pattern for Air Transport", in Vlasic Ed., Explorations in Aerospace Law at 387 (1968).

that "rates to be charged by the air carriers of either contracting Party between points (in their respective territories) shall be subject to the approval of the contracting Parties within their respective constitutional powers and obligations". This principle, universally adopted, prescribes the process under which all scheduled tariffs must be approved by both third and fourth freedom governments before entry into force. Positive assent is, thus, required from each of the terminal Parties.[72] In fact, this practice has been followed, without variation, for all scheduled fares since the beginning of modern international air transport. For the vast majority of nations, this regime still applies. Only third and fourth freedom is governed within these terms, but there is inevitably also a practical link with intermediate fifth freedom prices.

The assignment to set tariffs is delegated by Bermuda I to the IATA ratemaking machinery.[73] The approval of this machinery by the United States, however, did not mean an automatic approval of actual IATA fares and

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72. Assent by non-disapproval has been a common practice, but this constitutes no waiver of the power to disapprove.

73. It may be an irony of history that today, the UK perceives that its own best interests could be served by the "open skies" philosophy espoused by the Americans at Chicago.

rates. As can be seen, for instance, at the end of paragraph (b) of Annex II, "any rate agreements concluded through this machinery...and involving United States air carriers will be subject to approval by the Board". Thus, all IATA agreed rates and fares had to be submitted to the CAB for individual approval. Such agreed tariffs are, of course, currently submitted to the United States DOT for the same purpose.

Any new rate which may be proposed by air carriers shall be filed with the aeronautical authorities of both contracting Parties within a specified period of time (i.e. thirty days) before the proposed date of introduction.[74] This period may be reduced, in particular cases, if the governments concerned agree. On the other hand, if both aeronautical authorities approve the proposed fares within the thirty days, the tariffs will become effective on the suggested date of introduction.

The two Parties to Bermuda I foresaw certain cases where there is no IATA negotiated solution, or when a rate agreement does not get the approval of either Party, or, finally, when either Party withdraws or fails to renew its approval to such rates,[75] and therefore paragraphs (e)

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74. Bermuda I, Annex II (Para. c).

75. Id. Para. (d).

and (f) of Annex II specify the procedures to be followed in such cases. In short, these methods distinguish between two periods, the first period before the American aeronautical authorities have been given the power to regulate international air tariffs and the second after such power has been granted.[76]

In the case where the two contracting Parties cannot agree within a reasonable time upon a proposed rate, the matter in dispute will be referred to the ICAO (formerly PICAO) for an advisory report.[77] Each contracting Party agrees to use its best efforts under the powers available to it to put into effect the opinion expressed in such report. Although nothing is said in Bermuda I as to the enforcement of such report, the advisory opinion of ICAO, in fact, determines the question in case of disagreement between the two Parties.[78]

Finally, paragraph (h) of Annex II gives some guidelines for the level at which tariffs should be set. Generally, what should be taken into consideration in such

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76. For more details, see id. Para. (e) and (f); Cooper, op. cit., note 71, at 387-88.

77. Bermuda I, Annex II (Para. g).

78. See, e.g., Matte, Treatise on Air-Aeronautical Law at 234 (1981).

process is that tariffs "shall be fixed at reasonable levels, due regard being paid to all relevant factors, such as cost of operation, reasonable profit and the rates charged by any other air carriers".[79] These guidelines have to be read in conjunction with paragraph 1 of the "Final Act" to the Bermuda Conference. The first sentence of this paragraph stipulates:

> "That the two governments desire to foster and encourage the widest possible distribution of the benefits of air travel for the general good of mankind at the cheapest rates consistent with economic principles."

In fact, the guidelines mentioned in paragraph (h) are vague. It is, however, evident that they do not allow IATA member carriers or any other airlines to fix tariffs at the highest level that the traffic will bear. Tariffs should rather cover the costs of operation, and permit a certain margin for reasonable profits. In this regard, it should also be remarked that these guidelines contain no reference to the interests of air transport users, or to the development of civil air transport, as do the respective clauses in Bermuda II.

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79. Bermuda I, Annex II, (Para. h).

The Bermuda II Ratemaking System

The tariff provisions of Bermuda II attempt to respond to both the American complaint that fares and rates set by IATA were unresponsive to market forces and the British complaint regarding the CAB tariff review practices. As is the case under Bermuda I, Article 12 of Bermuda II contains the system of governmental approval of tariffs and the possibility of using the IATA ratemaking machinery for setting the air fares and rates. Unlike its predecessor, however, the new tariff procedures of Bermuda II have been considerably streamlined and brought into line with post-Bermuda I practices.[80]

Article 12 of Bermuda II makes a distinction between tariffs set by IATA and those fixed by the air carriers. In both cases, however, governmental approval is required.[81] In the event of a governmental dispute over the tariffs and failure of consultation thereon, contracting Parties may take action "to continue in force the existing tariffs beyond the date on which they would otherwise have

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80. Haanappel, "Bermuda 2: A First Impression", Annals of Air and Space Law at 144 (1977); supra, Chapter II, Section III.

81. Bermuda II, Article 12 (Paras. 3 and 4).

expired".[82] In fact, this factor was amiss in the Bermuda I Agreement.[83]

The substantial philosophical variation in the tariff provisions of Bermuda II from the original Bermuda Agreement is further clarified in the policy declaration itself:

> "The tariffs charged by the designated airlines of one contracting Party for public transport to or from the territory of the other contracting Party shall be established at the lowest level consistent with a high standard of safety and adequate return to efficient airlines operating on the agreed routes."[84]

Moreover, each tariff shall, to the extent feasible, be based on the costs providing such service "assuming reasonable load factors".[85] It is of interest, therefore, to note that for the first time in a major American bilateral agreement, the tariff policy declaration concentrates on the lowest level of tariffs with sufficient return to efficient

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82. Id. Article 12 (Para. 7).

83. Shovelton, "Bermuda 2: A Discussion of Its Implications", Aeronautical J. at 53 (Feb. 1978).

84. Bermuda II, Article 12 (Para. 2).

85. Id. The reference to reasonable load factors for the computation of operating costs corresponded to the methods and standards of the U.S. CAB. It had the effect of establishing a relation between the level of fares and the effectiveness of operation of a given airline. See Section 1002(e) of the 1958 Federal Aviation Act.

operations, whereas the existing United States "standard article" language was:

> "all rates to be charged by an airline of one contracting Party for carriage to or from the territory of the other contracting Party shall be established at reasonable levels, due regard being paid to all relevant factors, such as costs of operation, reasonable profit, and all rates charged by any other airlines, as well as the characteristics of each service."[86]

It should also be noted that Bermuda II, in contrast to its predecessor, has a reference to new economic considerations, such as: prevention of unjust discrimination and undue preferences, or advantages in construing a fare or rate including competition for scheduled or charter air services, and finally the encouragement given to individual air carriers to initiate innovative, cost-based tariffs.

Article 12 of Bermuda II further states that the two governments should furnish appropriate guidance to their airlines in advance of or during IATA Traffic Conferences. A Tariff Working Group, comprised of governments tariff experts, is set up to review standards for tariffs and to

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86. Boyd Statement, Hearing Concerning U.S. International Aviation Negotiations Before the Subcommittee on Aviation of the House Committee, 1st Sess. NO. 4 at 59 (1977).

make recommendations on pricing.[87] Based on the results of this Working Group, the governments revise tariffs and agreements reached under the authority of IATA.

In the years after Bermuda II, low-fare agreements between the United States and the United Kingdom have been concluded. In the 1980 amendment to Bermuda II, as was previously mentioned, no specific results on tariff matters were achieved. The two Parties, however, agreed to pursue their liberal tariff policy.[88] In this regard, it is worth noting that the introduction of new-low fare services between the two countries, during the 1984-1985 winter season, could have caused an international conflict on the viability of Bermuda II.[89] This problem, however, was solved after personal intervention by President

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87. Bermuda II, Article 12 (Para. 9(a)-(b)); Annex 3(4)-(5).

88. See supra, Chapter II, Section V; Wessberge, "Sequel to Bermuda II: New Negotiations Between the U.S. and the U.K.", 9 ITA Bull. at 361 (Apr. 21, 1980).

89. On Oct. 18, 1984, the British Government disapproved low fares for the winter season filed by 13 of the airlines that fly between the U.S. and Britain. The disapproval came as a British protest against Bermuda II and the applicability of American antitrust laws in international air commerce. See supra, Chapter II, Section IV (footnote 90).

Reagan.[90]

SECTION III - RECENT TRENDS IN INTERNATIONAL AIR TRANSPORT RATEMAKING

Generalities

In a regime where the "customer" and "competition" became superior components of the air transport policy of a major and most powerful participant such as the United States, inevitably the focus becomes lower prices. The object of such a competitive framework has been to make possible new price control methods which either accentuate unilateral control or, theoretically, allow the withdrawal of government supervision altogether. As to the new pricing provisions described below, one has to stress that their object is to proscribe governmental approval and disapproval powers only.

The United States policy for international aviation

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90. See "President Halts Grand Jury Antitrust Inquiry", Aviation Week & Space Tech. at 36 (Nov. 26, 1984). The British CAA reapproved the low fares after the U.S. Justice Department gave, upon Reagan's orders, its assurance that it would not prosecute British airlines under U.S. antitrust laws. Id. at 30 (Jan. 7, 1985); "U.S.-U.K. Accord on Fares", Flight International at 5 (Jan. 12, 1985).

is designed to "provide the greatest possible benefit to travellers and shippers".[91] A major delineation in this scheme has been to "create new and greater opportunities for innovative and competitive pricing".[92] To achieve this end, the 1978 American Policy aims to develop "new bilateral procedures" to encourage a more competitive regime for fixing scheduled air tariffs. Also, the charter prices must continue to be competitive. Therefore, fares, rates and prices "should be determined by individual airlines based primarily on competitive considerations in the marketplace". The accent is hence on bilateral pricing and no reference is made to the desirability of harmonization - or to any benefit of multilateralism..

The new pricing system has led, as will be seen below, to radically different bilateral tariff provisions. These provisions, however, must be read in the context overall of a different regulatory and operating environment. In other words, they should be examined in comparison to that established under the Bermuda I principles which, in fact, governed most of the American bilateral relations.[93]

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91. U.S. Policy for the Conduct of International Air Transportation Negotiations, Aug. 21, 1978, 14 Weekly Composition of Presidential Documents.

92. Id. "Introduction".

93. For the comparison, see supra, Section II.

Without this new environment, insistence on low tariffs could, it was argued, only result in greater, not less governmental intervention.

The methods for creating those innovative prices are addressed only indirectly, if at all. Until the signing of the Unites States-Netherlands Protocol in March 1978, all scheduled pricing had been subject to the approval of both the origin and destination countries. This Protocol introduced what is called "country of origin" pricing control for scheduled services. Subsequent liberal bilaterals presented a "double (or mutual) disapproval system; more recently, further changes, using these fundamental configurations, were generated. It should be noted that, except for changes in specifics, the terms of these liberal agreements are basically consistent. This is probably indispensable if the Americans desired to create a homogeneous network of liberalization. Finally, to consider the modern provisions in their context, one has to remember that these clauses commonly apply both to international scheduled and charter air services.

The New Pricing Clauses

Definition

Most of the United States liberal bilaterals define the term "price" as "the fare, rate or price and its conditions or terms of its availability charged or to be charged by an airline for the public transport of passengers, baggage and cargo (excluding mail)".[94] Some agreements add to this definition the following words: "...(by an airline) and or its agents...."[95]

The definition in the Agreements with Belgium, Jordan and Thailand is somewhat broader and contains the charges and conditions for services ancillary to carriage of traffic offered by carriers and "amounts charged by airlines to air transportation intermediaries". It is significant to note that the reference to "air transportation intermediaries" makes it clear that, for charter operations, the definition of price only included the wholesale price charged by the air carrier to the charterer

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94. See, e.g., German Protocol, Article 6(2); Belgium Protocol, Article 6(1).

95. See, e.g., U.S.-Fiji Agreement, Article 1(G); Jamaica Protocol, Article 6(ii).

(intermediary), but not the retail price charged by the charterer to the public.

Country of Origin Pricing System

Under this form of pricing, the regulatory authority of the country where the traffic and service originate has sole power to approve or disapprove all tariffs filed[96] by national and foreign carriers. In other words, the country of origin has exclusive control over the fares for those persons purchasing one-way or round-trip tickets for travel commencing in that nation, and tariffs can only be disapproved by the aeronautical authorities of the country where the traffic begins.

There was a prior example for this basis. Country of origin pricing was, in effect, a mutual practice governing international non-scheduled air services.[97] Being point-to-point, usually round-trip operations, the

96. As to tariff filing requirements, all the liberal bilaterals state, inter alia, that: "Each Party may require notification to or filing with its aeronautical authorities of prices...." Thus, filing requirements in the liberal system have become permissive (see the word "may") rather than compulsory as is the case under Bermuda I. See also supra note 74.

97. See supra, Chapter V, Section IV.

country of (transient) destination ordinarily had no major interest in the price levels applied - at least until traffic increased to a degree which menaced its scheduled flag carrier's fourth freedom traffic. Even then, the interest in encouraging inward tourism was often a dominating element.

The pertinent bilaterals have no definition as such of a country of origin pricing system, the purpose being declared rather in the use of the clause. This is because the term itself rarely appears. Instead, the practice is conferred as a derogation from a general practice and not as a commencement point:

> "Neither contracting Party shall prevent the institution or continuation of any fare or rate or any wholesale or retail price which is proposed or offered by a designated airline of the other contracting Party, except where the first point on the itinerary (as evidenced by the document authorizing transportation by air) is in the territory of the first contracting Party, unless otherwise agreed by the contracting Parties...."[98]

As evident from this clause, each contracting government's disapproval powers are confined to tariffs offered or proposed by the other Party's air carriers when the passenger's (etc.) itinerary starts in its territory. The limitations on such disapproval powers thus refer only to

98. German Protocol, Article 6(d); Netherlands Protocol, Article 6(d).

prices of the other Party's airlines - a combined result of the derogation method of expressing the control and of each country's retention of sovereignty over its designated airlines. Meanwhile, the powers extend (as already noted) to round-trip traffic originating in the home country. Finally, it should not be forgotten that the clause applies equally to scheduled and non-scheduled tariffs.

"Double" or "Mutual" Disapproval Pricing System

Where a double disapproval agreement is in effect, no tariff may be disapproved or prevented from going into effect without the prior accord of both of the contracting Parties. A question may be immediately raised whether de facto this system of pricing retains any form of governmental intervention in international air tariffs. It appears that since its introduction in 1978 (i.e. in the United States-Israel Protocol) mutual agreement has never been reached to disapprove a tariff. The grounds for governmental intervention, as will be discussed later, are very narrow[99] and mutual intergovernmental agreement is indeed hard to achieve. One may therefore argue that this new form of control is in practice very close to "market control" -

99. See infra "Criteria for Intervention" in this Section.

if in fact market controls exist in international air transport.

Practically speaking, the mutual disapproval rule may mean "total freedom for airlines to set their prices on the basis of the forces of the marketplace".[100] This system is apparently in favour of the American balance of payments, and promotes tourism and business travel as airlines can charge prices of their choice, even in foreign originating markets.

Similar to country of origin clause, the dual disapproval provision is inscribed in the frame of prohibition of disapproval rather than a demand to approve. Therefore, while each contracting Party may require all fares and rates to be filed by the other Party's designated carriers...

> "Neither Party shall take unilateral action to prevent the inauguration or continuation of fares, rates or prices or the rules governing their availability that are contained in tariffs filed with it by the designated airlines of either Party for scheduled or charter air transportation between the territories of the two Parties."[101]

This means, for all third and fourth freedom air services, unilateral disapproval of tariffs filed by either Party's

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100. Haanappel, op. cit., note 16, at 149.

101. See, e.g., US-Israel Protocol, Article 6(a), (d).

carriers is not permissible.[102]

It should also be noted that certain criteria must be utilized before even a mutual determination to disapprove may be taken. As will be shown below, these criteria are highly subjective.[103] Consequently, utilization of the control depends primarily on the philosophies of the contracting Parties. The more "liberal element" predominates in this system of pricing.[104]

In case the aeronautical authorities of one contracting Party are dissatisfied with a price or proposal, they may so notify the aeronautical authorities of the other Party and request consultations. Until there is agreement to disapprove, however, the price may go into or remain in effect. In fact, any filed price may enter into effect with the minimum of formality. This, of course, deviates from the more firm needs of the double approval system where one Party may veto a proposal. If consultations are then held

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102 As will be seen in the "Matching" and "Price leadership" subsections below, the (sovereign) right of disapproval is in some cases waived also for services by third country airlines as well as for services of the two Parties' carriers beyond the other Party's territory.

103. See supra note 99.

104. Harbison, Liberal Bilateral Agreements of the United States, unpublished thesis, McGill University at 82-84 (Nov. 1982).

between the Parties, the price may not go into effect until agreement is achieved.

It seems that both the double disapproval and country of origin systems can engender legal problems under national legislation insofar as waiver of sovereign powers is necessary.[105] It should, however, be remembered that whereas under the double disapproval system tariffs must be disapproved by both contracting Parties, the country of origin disapproval rule allows unilateral governmental disapproval. Thus, for those who desire to keep some form of governmental tariff disapproval power, the country of origin system seems, to some extent, more realistic than the double disapproval system.

Matching and Price Leadership

Under both the country of origin and mutual disapproval regimes, several further competitive elements may be built in; these are directed both at increasing competition in the bilateral markets and expanding the

105. In fact, the total withdrawal (albeit by mutual consent) of unilateral power to suspend a price created problems even for the US. See Hearings on S. 3363 Before the Subcommittee on Aviation of the Senate Committee on Commerce, Science and Transportation, 95th Cong., 2nd Session, at 124-147 (1978).

longer term thrust of the bilaterals into a system which will permit a form of multilateralism in pricing through aggregation of bilateral agreements. To this end, various combinations of matching and price leadership provisions exist, depending on the particular agreement.

(i) Matching

Matching, or "meeting", prices implies for example that no tariff filed by any airline, including a third country airline, may be unilaterally rejected by either of the two Parties where it is set at similar prices to others offered in the market, or under "substantially similar terms and conditions"[106] permitted for other airlines. Although there has been no clear explanation of what is meant by "substantially similar",[107] several liberal bilaterals provide that conditions concerning routings, connections and aircraft type shall be regarded as substan-

106. US-Germany Protocol, Article 6(e).

107. It should be noted that the US "Model Double Disapproval Clause" only provides for "identical or similar", but this wording is not in practice generally used. For the Model Clasue, see ICAO AT Conf/2-WP/11.

tially similar.[108]

These provisions usually relate to "direct, intra-line or interline routings". Bearing in mind that matching is a less radical version of price leadership, as will be seen below, some agreements with this provision also allow that "sympathetic considerations" of non-matching fares, rates and prices proposed by designated airlines (i.e. designated by either bilateral Party) should be given where such fares, rates or prices are necessary to obtain "effective and non-discriminatory market access".

In fact, there are two main categories of route to which such matching provisions can apply. Primarily, they relate to third and fourth freedom routes between the two contracting Parties for operations by the airlines of third countries. This is generally accompanied by a requirement for reciprocity, i.e. before the airlines of such third countries may be granted matching rights they must also offer them to the respective airlines of the two bilateral partners.[109] Hence even in the "model" bilateral agreement with Thailand, which has no such reciprocity requirement built into it, the accompanying Memorandum of

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108. US-Belgium Protocol, Article (6); US-Jamaica Protocol, Article 6(5).

109. See, e.g., US-Israel Protocol, Article 6(e).

Understanding contains this limitation. It is hard to believe that a government would be prepared to give such unfettered access to its market for a third country airline without requiring a quid pro quo such as reciprocity.

In addition, provision may also exist for matching by airlines of either of the two Parties in fifth freedom markets to or beyond the other Party's territory. Thus, the United States-Germany "Pricing Article", concluded:

> "This paragraph shall apply as well to fares, rates, prices, and conditions filed by designated airlines of one contracting Party for its operations between the territory of the other contracting Party and any point in a third country."[110]

Here, again, the third country involved is likely to require a quid pro quo.

(ii) Price Leadership

The principle of price leadership is entirely new to aviation; its practical impact is much broader than matching. No definition exists of the term, nor does it appear in the liberal agreements; like most other pricing elements, it arises by mutual exclusion of sovereign disapproval rights.

From the regulatory viewpoint, the provisions

110. US-Germany Protocol, Article 6(e).

granted for price leadership are similar to those for price matching; in this case the ability is granted, not only to offer the same tariffs as primary (i.e. third and fourth freedom) carriers but actually to undercut them. Leadership thus differs from matching in that tariffs may actually be undercut or "led": (a) by the airlines of third countries in markets between the contracting Parties; and (b) by the airlines of the two Parties on respective fifth freedom routes, i.e. involving a third country.[111]

Indeed, this revolutionary new concept is an enormous departure from traditional pricing policies and few countries have knowingly undertaken to permit price leadership. The concept is, therefore, easily overlooked in those cases where it applies:

> "Neither Party shall take unilateral action to prevent the inauguration or continuation of a price charged or proposed to be charged by:
>
> (a) an airline of either Party or by an airline of a third country for international air transportation between the territories of the Parties, or
>
> (b) an airline of one Party for international air transportation between the territory of the other Party and a third country, including in both cases transportation on an interline

111. In such cases, the only governmental intervention permissible is subject to the criteria set out in the pricing article. See supra note 103.

or intraline basis."[112]

In this regard, it is significant to note that the model country of origin clause is similarly worded, but with the necessary retention of powers over third freedom prices.

General Pricing Clause

One of the most crucial innovations in the liberal bilaterals is that they no longer refer to the IATA Tariff Coordinating machinery. Instead, the pricing clauses are generally prefaced by an agreement that both Parties shall encourage individual airlines to develop and implement, e.g., innovative or competitive fares, rates and prices. These levels should then be based on "commercial considerations" or in some bilaterals, "primarily on commercial considerations".

This, however, does not mean that these agreements prohibit the use by designated airlines of the IATA rate-making machinery. An examination of all liberal bilaterals reveals that none of them contains an actual preclusion against the use of such a machinery. The German Protocol is unique in its direct reference to continued use of IATA Conference machinery in drawing up tariff proposals for

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112. See 1980 Model Clause, op. cit., note 107; US-Thailand Agreement, Article 12(3).

submission to the Parties for approval.[113] One can, therefore, conclude that the use of the IATA pricing machinery, for all other liberal bilaterals, seems to be implicitly allowed and this opinion is specifically confirmed by provisions under the United States-ECAC Memoranda of Understanding on North Atlantic air tariffs.[114]

Criteria for Intervention in Airline Pricing

There are normally three criteria upon which governmental intervention in the price levels is agreed in liberal markets as exceptions to the non-intervention provisions. These are limited to the following:

(a) prevention of predatory or discriminatory prices or practices;

(b) protection of consumers from prices which are unduly high or restrictive due to the abuse of a dominant position;[115] and

(c) protection of airlines from prices which are artificially low because of direct or indirect subsidy or support.

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113. US-Germany Protocol, Article 6(e); see also the US-Singapore Agreement, Article 10(c).

114. See infra Section IV.

115. Some agreements, however, use the word "monopoly power", see, e.g., German Protocol, Article 6(a); Netherlands Protocol, Article 6(i).

Each of these three criteria contains elements whose specific meaning has never been bilaterally agreed. Interpretation is therefore highly subjective, even after more than seven years of their operation.

If there is agreement between the Parties that any one of these criteria can be applied to a filed fare, rate or price than e.g. "best efforts" are to be undertaken to prevent the coming into force of such levels. In all cases, procedures and timetables are provided for consultation in the case of one contracting Party expressing dissatisfaction with the filed tariff.[116] In this respect, one has always to remember that the liberal scheme explicitly excludes arbitration in pricing disputes in any way which could lead to external judgements on price levels.

The Standard Foreign Fare Level (SFFL)

The SFFL was introduced by the International Air Transportation Competition Act of 1979 as a direct counterpart to the domestic United States "Standard Industry Fare Level" (SIFL).[117] In short, within the zone of 5% above

116. See, e.g., US-Thailand Agreement, Article 12(3).

117. CF. The Standard Industry (i.e. domestic Fare Level SIFL) of Section 1002(d)(4), (6), (7). The SFFL was based upon fares in effect on Oct. 1, 1979, except for

the SFFL and 50% below, airlines are free to adjust fares. It should, however, be noted that the SFFL must be periodically adjusted: in the case of fuel cost changes every 60 days, and for other cost changes, at least semi-annually.[118]

The SFFL affects liberal bilaterals in two ways. Firstly, under country of origin scheduled pricing regime, there may be no disapproval by the United States of any fare of American-origin which falls within the SFFL band. Secondly, it limits the ability of the United States to control prices offered by American carriers in limited designation "transitional markets". Hence, while the United States may seek to compel a single designation American carrier to offer more competitive fares, this power is limited by the automatic approval zones of the SFFL.[119] Also, it should be noted that in mutual disapproval markets, the SFFL has no application, as any right to take unilateral action is waived.

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markets with as much as 25% of total traffic carried by U.S. carriers in foreign air transportation.

118. See International Air Transportation Competition Act, Section 24 (Section 1002(j), (7), (8), (9) of the Federal Aviation Act of 1958).

119. In other words, under US law, the CAB was obliged to approve them.

Price Flexibility Within a Band

As evident from the above-mentioned pricing methods, individual markets have developed their own variety of different forms reflecting special needs and concerns. None of these, alone, offers the scope for general adoption. In band pricing (i.e. zone of reasonableness system), however, a more generally acceptable formula may have been discovered.

As a combination of different pricing schemes, band pricing does not preclude the use of any other variation in bilateral terms - whether in matching/leadership or capacity, designation and routing controls. In other words, rather than existing as an independent style, it can occur in any bilateral form.

The United States-Philippine Agreement contains an interesting compromise on full pricing flexibility which also employs the SFFL. It provides that, within an agreed price band, a mutual disapproval pricing regime will apply. Below the lower limit, country of origin rules come into effect.[120] Thus, the Agreement precludes the Parties from unilateral price intervention "if the price is equal to

120. See Article 12 of the US-Philippine Agreement.

or greater than 80% of the appropriate index fare leval as defined in Annex II".[121] This means: there is a mutual disapproval rule upwards from the index fare and downwards to 80% of the index fare. At the same time, for fares dropping below 80% of the index fare there is a country of origin disapproval rule.[122]

With respect to the United States-Barbados Agreement, the passenger reference fare is again determined by reference to the SFFL. The band covers prices between 115% and 40% of the "base normal economy fare".[123] Thus, within the band a mutual pricing disapproval rule applies. Outside the band, however, a dual approval rule applies.

It is worth noting that the first formal adoption of a band concept was in the United States-China Agreement of September 1980, representing therefore a compromise between conservative and liberal philosophies. However, the main difference in principle was that, in the Chinese Agree-

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121. Id. (Para. 2). Annex II stated that the level would be the U.S. SFFL as of Oct. 1, 1980, subject to future cost-based adjustment at least four times yearly.

122. Id. (Para. b); Wessberge, "Prospects for International Air Transport Under Open Competition", 43 ITA Bull. at 1083 (Dec. 15, 1980).

123. United States-Barbados Agreement, Article 12(5)(a), (i).

ment, the index fare is to be established by agreement between the two Parties, rather than being based on the SFFL.[124]

It is highly probable that the United States will continue following these lines in future negotiations, with the main variant likely to be the choice of index point. As it stands, the SFFL is not a totally satisfactory reference as only American carrier costs are used in the continuous updating process; neither is it appropriate that the costing methodology used should be entirely unilaterally determined.

Finally, if the price band concept proves in fact to be more widely acceptable, there may well be value in bilateral or multilateral formulation of guidelines for establishment of the fare index, which would remove these drawbacks and permit coordination between routes. Therefore, the fare band system, as will be seen in the following section, would subsequently also be used in the multilateral US-ECAC North Atlantic tariff agreement.

To conclude this section, it is significant to keep in mind that the United States believes "that modern air transportation has proved itself to be quite adaptable to

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124. For full details, see Harbison, op. cit., note 104, at 192 et seq.

regulation by the marketplace, and that (the Americans) as regulators should rely increasingly on competition to promote the public interest".[125] In fact, the next few years will show whether there has been a similar "modernization" of the attitudes of nations towards retaining sovereign control over commercial aviation in their airspace. Preliminary signs, however, are not convincing. Price control has long been regarded as a clear exercise of sovereignty and will not be lightly surrendered unless some durable national benefit ensues.

SECTION IV - THE UNITED STATES - ECAC MEMORANDA OF UNDERSTANDING ON NORTH ATLANTIC PRICING

In the early 1980's, the severe financial bloodbaths and instability in pricing on the North Atlantic, the continuing threat of the CAB's finalization of the IATA Show Cause Order, and the proliferation of United States liberal bilaterals had made many air carriers and governments on both sides of the ocean (but particularly in Europe) seriously concerned. In mid-1981, talks started between American and European aviation authorities (under the

125. CAB IATA Show Cause Order, op. cit., note 41, 25840, 25842.

auspices of ECAC)[126] which would eventually lead to the first United States-ECAC Memorandum of Understanding on North Atlantic air fares. This Memorandum was in force between August 1982 and February 1983. It was then superseded by subsequent memoranda, the second being in force between February and November 1983 and the third between November 1983 and November 1984. The fourth Memorandum which is now in force expires on April 30, 1987,[127] unless the Parties have agreed in writing by October 31, 1986; to continue it after the expiration date.[128]

The transatlantic fare agreement was widely welcomed. It was described as a "unique development in the history of international aviation".[129] The United States

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126. See Wessbergh "Multilateral Arrangement on Fares between the U.S. and a Group of ECAC Countries", ITA Bull. at 1 (May 19, 1982); Heilbronn, Regulating the Setting of Scheduled International Air Fares, unpublished thesis, Australia at 150 (1983).

127. See "U.S., ECAC Sign Atlantic Fare Pact", Aviation Week & Space Tech. at 33 (Oct. 22, 1984); "U.S.-European Carriers Extend Agreement on North Atlantic Fares", id. at 31 (April 31, 1985).

128. Articles 8 and 9 of the Memorandum. At present, 16 ECAC States are Party to the new agreement: Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, UK and Yugoslavia.

129. ECAC Press Release, No. 54E at 2 (May 5, 1982),

sees the compromise as confirming the development of its fares policy, which is one of the keys to deregulation. In this regard, McKinnon (Chairman of the "sunsetted" CAB) greeted the agreement as a "milestone in international aviation relations and has the potential for significant consumer benefits. For the first time, air fares to a vast region of the world will reflect the forces of a marketplace significantly unfettered by government".[130] On the other hand, the European countries consider that this multilateral approach reflects a measure of solidarity which is the goal of ECAC as an institution and which was achieved despite the conflicting interests of the member States. Even IATA hailed the pact as a "most significant breakthrough...that should help restore a badly needed measure of stability to North Atlantic market".[131]

The four Memoranda only apply to scheduled North Atlantic passenger fares and conditions relating thereto (except agency commission rates). It is possible that a future agreement may also apply to North Atlantic cargo

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quoting Erik Willoch, ECAC President.

130. Cited in Feldman, "US Not Enthusiastic About ECAC Agreement", Air Transport World at 29 (Oct. 1982).

131. Speech delivered by Hammarskjold to the Triennial Meeting of ECAC in Strasbourgh on June 8, 1982.

rates, but it is unlikely to encompass North Atlantic passenger charter fares. This is mainly because the United States has always refused to include charter operations under the umbrella of the Memoranda, so that "these 'independents' can continue, as they have in the past, to operate with a minimum of government oversight and regulation".[132]

The essence of the Memoranda is to create zones of pricing flexibility (zones of reasonableness) within which governments agree not to interfere with tariff determination. This means that Parties to the agreement will automatically approve fares filed by the carrier of anothre Party which are within the specified pricing zones.[133] Outside the zones, applicable bilateral terms are in force, i.e. double/dual approval (Bermuda I type agreements), double/dual disapproval or country of origin disapproval (liberal agreements). Finally, the pricing zones function on routes between the United States and the ECAC member State Parties,

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132. Speech delivered by Trent, U.S. Ambassador to ECAC, to the Aviation Club on October 18, 1983.

133. See Articles 2(3) and 3(1) of the current Memorandum. See also, Haanappel, "Deregulation of Air Transport in North America and Western Europe", in Storm van's Gravesande & Veen Vonk Eds., Air Worthy, Liber Amicorum Diederiks-Verschoor at 103 (1985).

but are not applicable amongst ECAC States.[134]

These principles lead one to say that the ECAC-United States compromise is a multilateral pact on principles and a bilateral agreement on the specifics. In other words, whereas the general principles are agreed upon multilateraly, exact "reference fare levels" and the breadth of the "zones of reasonableness" for different classes of service are determined between the United States and each individual participating ECAC member State separately. There is, however, one major reservation in the scheme which is designed to ensure that the agreement does not affect "matching" provisions[135] in force under existing bilaterals or arrangements:

> "Nothing in this Understanding shall be deemed to affect in any way the treatment by Parties, under existing bilateral agreements or arrangements, of fares intended to match fares in effect between the territories of the Parties."[136]

As far as pricing procedures are concerned, the most significant achievement of the agreement is the

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134. Id. Article 1(c) and (d). In this regard, it is important to note that ECAC is currently considering the possibility of drafting a new agreement on fares that would replace the 1967 ECAC Agreement that governs current European airline fare policy. See Aviation Week & Space Tech. at 36 (Jun. 24, 1985).

135. See supra, Section III.

136. Article 2(4) of the current Memorandum.

inclusion of the provision that:

> "...no Party shall make participation in multilateral carrier tariff coordination a condition for approval of any fare, nor shall any Party prevent or require participation by any carrier in such multilateral tariff coordination."[137]

As evident from its wording, this provision neither requires nor forbids airline participation in multilateral tariff coordination. It nevertheless binds both the United States and ECAC member State Parties to ensure that no legislative or administrative moves would be made by any of them to prevent, or in any way limit, multilateral tariff coordination by airlines. Although IATA ratemaking machinery is not specifically mentioned, the generic term "multilateral carrier tariff coordination" makes it clear that this machinery is, of course, included.[138] In addition, the wide generic scope of this term made it feasible for IATA to take the initiative to adopt an Addendum to its Provisions for the conduct of Traffic Conferences,[139] whereby

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137. Id. Article 2(1).

138. In this respect, Trent (US Ambassador to ECAC) has made the point when he explicitly mentioned: "While it is obvious that tariff coordination is accomplished primarily within the IATA framework, it is not the intention of this (US-ECAC) agreement to canonize IATA". Cited in Ott, "US Moving to Broaden Tariff Antitrust Immunity", Aviation Week & Space Tech. at 34 (Oct. 24, 1983).

139. The Addendum was also approved by the CAB: Orders

special conferences of IATA and non-IATA scheduled airlines on North Atlantic passenger fares may be held.[140]

The United States-ECAC agreement also establishes respectively a Tariff Working Group and a Working Group on matching/combination of fares.[141] The Tariff Working Group is composed of representatives from the United States and not more than two from each other Party, and shall meet at the initiative of any Party. Its powers are related to mutual examination and consideration of the fares in question. The other Working Group is composed of representatives of the Parties, and of such other governments as the Parties may agree. Its main task is to examine the question of matching/combination of fares within the context of the agreement and, if appropriate, propose revision to the agreement.

The other major achievement of the arrangement is that there was a multilateral agreement on a definition of five tariff levels which attempted to encompass virtually all of the different fare types being offered by the

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(continued from previous page)
82-9-108, Sept. 24, 1982 and 82-10-103, Oct. 26, 1982 (Docket 40960).

140. By end of January 1983, three of such special meetings were successfully convened. See Aviation Daily at 140 (Jan. 26, 1983).

141. See Articles 6 and 7 of the current Memorandum.

airlines of the contracting Parties. A-1 indicates first class; A-2 business class; B economy class; C-1 discount fares and C-2 deep discount fares. In this regard, economy, first class, and business class fares are defined in the text of the agreement.[142] Discount and deep discount fares are defined with much detail in Annex I to the agreement. However, the more controversial issues (such as the reference levels and maximum and minimum zone limits) are described in Annex II to the agreement. Finally, if any new ECAC member State joins, this shall be subject to acceptance, by all Parties to the agreement, of the reference levels and pricing zones applicable to the new routes covered by the agreement.[143]

The United States-ECAC agreement is unprecedented in international civil aviation. It presents a degree of pricing flexibility within a reasonably stable and predictable framework, thus permitting the airlines to get on with the business of providing air services in a commercial environment which remains highly competitive but not suicidal. In other words, it offers the possibility of a challenging new order in pricing regulation. For this reason, its functioning will be closely watched by govern-

142. Id. Article 1(I) and (II).

143. Id. Article 9(4).

ments and air carriers throughout the world, as an apparent compromise between the American model competitive system and the Europe's traditional regulatory style. One thing, however, should always be remembered that the significant facts about this agreement are its multilateral form - a necessity in pricing which requires a coordinated approach - and its affirmation of the multilateral airline tariff negotiating process. McMahon, a former President of ECAC, stressed this point when he has recently observed that the agreement "demonstrates that frank exchange of views and ideas can lead to better understanding and that confrontation can be replaced by co-operation".[144]

SECTION V - ICAO RENEWED INTEREST IN PRICING

Generalities

The questions and prospects of creating a regime of unified and centralized control of tariffs in international air transport were, inter alia, explored by the Chicago Conference of 1944. The original intention was to give ICAO substantial responsibility to police a global airline tariff

144. Speech delivered by McMahon to the International Aviation Club in Washington on April 16, 1985.

system.[145] It was therefore suggested, in a modified form for the Chicago Convention, that PICAO (later ICAO) would have the power to "review and recommend changes" in passenger and freight tariffs established by airline organizations.[146] However, since these provisions (like all other provisions dealing with problems of economic control) created acute disagreement, the Conference decided to omit them from the final draft.

It was not until 1974, that ICAO began to take a new interest in studying economic aspects, including tariffs, of world air transport.[147] The interest culminated in a number of the resolutions being taken at the Twenty-First ICAO Assembly, held in Montreal from September 24 to October 15, 1974. These initiated institutional developments and certain studies which have made a crucial doctrinal contribution during the last decade. In this respect, one should note that ICAO's Air Transport Committee

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145. See Pillai, The Air Net: The Case Against the World Aviation Cartel, Grossman Publishers, New York at 122 (1969).

146. See Proceedings of the Conference, op. cit., note 6, at 385.

147. See supra, Chapter IV, Section III (footnote 144). In fact, third world nations were largely responsible for ICAO taking up this commitment. Id. (footnotes 142 and 143).

is, of course, of much longer standing and published interesting studies well before 1974.[148] It is evident, however, that ICAO until 1974 was mainly preoccupied with technical and safety issues and devoted far less effort to economic ones.

The present functions of ICAO concerning the establishment of fares and rates stem from Assembly Resolution A21-26, which was adopted in 1974 in response to growing concern of nations regarding the impact of levels and structures of tariffs on travel, tourism and national economies. The Resolution directed the ICAO Secretariat to issue annual surveys of international air transport fares and rates, and to undertake a programme of studies concerning regional differences in tariffs and costs. It also directed the Council to establish the Fares and Rates Panel. This Panel has, in fact, met on a number of occasions, and in 1977 and 1980 its conclusions (as will be seen below) were considered by worldwide Air Transport Conferences and developed into recommendations which were endorsed by the Assembly.

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148. Id. The best known examples are the "Handbook on Administrative Clauses in Bilateral Air Transport Agreements", first published in 1962 and reprinted Sept. 1981; and the "Handbook on Capacity Clauses in Bilateral Air Transport Agreements", first published in 1965 and reprinted Nov. 1978.

The Twenty-First ICAO Assembly also passed Resolution A21-27 supporting the establishment of tariffs on a multilateral level. It stated that the scheduled service tariffs "should be established on the basis of uniform principles and procedures" and sought a study exploring the "relative benefits of either an international ICAO standard tariff clause or an international agreement embodying such a clause".[149] After four years of extensive studies, however, the ICAO Council opted for the first alternative and adopted on March 8, 1978, a Standard Bilateral Tariff Clause[150] intended to serve as "a guideline for States, for optional use and adaptation to particular situations".[151] In many ways, the Clause mirrors the 1967 ECAC Agreement,[152] but presents alternative terminology to allow for the reference to multilateral tariff coordina-

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149. See Assembly Resolution A21-27, ICAO Doc. 9118, A21-Res at 81. It is significant to note that this Resolution was a direct result of a joint proposal submitted by Sweden and Switzerland to the Assembly. See ICAO Doc. A21-WP/60, EC/8, July 30, 1974.

150. ICAO Doc. 9228-C/1036 (1978). For the text of the Clause, see Bradley & Haanappel Eds., op. cit., note 34, at 136.

151. Azzie, "Second Special Air Transport Conference and Bilateral Air Transport Agreements", 5 Annals of Air and Space Law at 10 (1980).

152. For the 1967 Agreement, see supra note 34.

tion procedures to be omitted. Another significant difference from the 1967 Agreement is that the Clause has been drafted in such terms that it could conceivably be applied not only to scheduled but also non-scheduled operations.[153] On the other hand, the traditional pattern of filing and governmental approval of fares and rates is maintained in the Clause. Governmental approval may be express or tacit.[154] After such approval, tariffs remain in force until new ones have been established or until one year after the date on which they otherwise would have expired. Finally, contracting Parties are under the obligation to ensure that within their jurisdiction active and effective tariff enforcement machinery exists.[155]

Aside from the above Assembly Resolutions, ICAO is also concerned with facilitating the task of governments in the fare and rate establishment process. This commitment was explicitly mentioned in Recommendation 19 of the 1977 Air Transport Conference, asserting that ICAO should

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153. In fact, this view was endorsed by Recommendation 15 of the 1980 Air Transport Conference. See infra (footnote 170).

154. There are two alternatives in Para. 6 of the Clause; the first for express and disapproval; the second for implicit approval.

155. See Para. 10 of the Clause.

increase its activities in the tariffs field by convening "regional workshops and preparation of relevant ICAO manuals" to assist governments in "their role in the process of establishing fares and rates". It was not, however, until 1983 that the ICAO "Manual on the Establishment of International Air Carrier Tariffs" was published.[156] It was developed by the ICAO Secretariat in several stages, involving consultation with States and various organizations to obtain information on their policies and practices, and reviews by the ICAO Fares and Rates Panel, the IATA and the ICAO Air Transport Committee. Sections of this Manual have already been used at a number of informal regional workshop meetings as a basis for discussion of tariff issues.[157]

The issuance of the ICAO Manual represents a new venture in ICAO's air transport work. It is designed to enable governments to accomplish efficiently their role in the process of establishing tariffs-including negotiating tariff agreements, dealing with administrative aspects of the filing of tariff proposals by airlines, and taking

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156. The Manual deals with the establishment of international passenger fares and freight rates (both scheduled and non-scheduled), but not charges for the carriage of mail. See ICAO Manual on Tariffs, op. cit., note 22, at 2.

157. See "ICAO Manual on Airline Tariffs Published", ICAO Bull. at 26 (Oct. 1983); id. at 20 (July 1985).

appropriate action on such proposals. The Manual is divided into four parts. The first part provides a description of the development of the present aviation regulatory system and information on the tariff policies pursued by governments individually and multilaterally within this regulatory framework. The second part comprises illustrative material on international organizations concerned with tariffs, with some emphasis on those organizations which have been empowered by States to provide tariff negotiating mechanisms. The third part supplies information concerning government practices in dealing with tariff proposals submitted to them. The last one suggests guidelines which governments may wish to apply in evaluating levels and structures of tariffs submitted for their approval. Finally, it should be noted that the Manual will be revised from time to time on the basis of changes in the air transport environment and experience gained with the Manual.

It is, however, significant to remember that an authorization to investigate the tariff structure or to review tariffs fixed by airlines, may not necessarily also encompass authority to fix tariffs. The conduct of governments, as evidenced by hundreds of bilateral air transport agreements, does not seem to contemplate the assignment of "original" ratemaking power to ICAO. Instead, the bilaterals either make specific references to IATA, or observe

meaningful silence on the issue thereby assenting to the existing IATA rate-fixing procedure.[158] ICAO has a clear mandate, though, to review or investigate tariffs fixed elsewhere. But giving ratemaking power to ICAO would undoubtedly meet with severe protests from the airlines and, of course, IATA. In addition, many governments prefer the IATA system, because they prefer to keep the controversial subject of airline tariffs at arms length, rather than have it complicating their foreign relations.[159] A good example can be taken (as mentioned below) from the worldwide 1980 Air Transport Conference, where the international aviation community recognized the universal IATA multilateral tariff - fixing machinery as the first choice in establishing tariffs. Indeed, IATA's multilateral process represents the optimal method of negotiating worldwide tariffs, as there is no realistic alternative available today to replace it. In the meantime, ICAO will and should remain a valuable multilateral forum to discuss and reflect upon worldwide air transport issues, including questions of ratemaking. Studies and deliberations on universal air

158. See supra note 12.

159. It was once described by one commentator that "the direct dealing by governments in the tariffs field might seem like using a hammer to crack nuts". See Pillai, op. cit., note 145, at 133.

transport matters should therefore be continued.

ICAO's Air Transport Conferences and International Ratemaking

Pursuant to the ICAO Assembly Resolution A21-26, the Council established a Panel of Experts on the Machinery for the Establishment of International Fares and Rates. On the basis of this Panel's reports, the machinery for the establishment of worldwide tariffs was examined at the 1977 and 1980 Air Transport Conferences.

The subject of international air transport fares and rates was discussed at large at the 1980 Air Transport Conference.[160] The following items were dealt with: mechanisms for the establishment of scheduled passenger fares; mechanisms for the establishment of non-scheduled passenger tariffs; mechanisms for the establishment of freight rates; co-existence and harmonization of methods by which fares and rates are established; and finally, tariff enforcement.

160. For the work of the 1977 Air Transport Conference on tariffs, see supra, Chapter IV, Section III (footnotes 152, 157 and 158).

Mechanisms for the Establishment of Scheduled Passenger Fares

The 1980 Conference examined Recommendation 17 of the 1977 Conference concerning the problem of special fares which restrict interlining and stopover rights and thus affect the principle of "fair and equal opportunity" for airlines of third countries to participate in the carriage of all traffic on the route concerned. This problem is emphasized by the new American tariff policy which focuses on third and fourth freedom traffic.[161] Recommendation 17 suggested that airlines should strictly follow the principle that, in adopting tariff agreements, each airline operating on a route or parts thereof should be given equal opportunity to participate in the carriage. Although some delegates supported the concept of a liberal interpretation of Recommendation 17, the 1980 Conference as a whole decided that the Recommendation should continue to be interpreted in a strict manner.

As to the question of currency conversion for tariffs construction, the 1980 Conference recognized the importance of developing a multilateral system of currency

161. Desmas, "The Second ICAO Air Transport Conference - Part Two", 14 ITA Bull. at 329-330 (Apr. 1980).

conversion. It recommended, therefore, that the Council examine this subject with the assistance of the Fares and Rates Panel, and that States "be invited to give due consideration to any multilateral solution to the problem of currency conversion".[162] The 1980 Conference also reaffirmed Recommendations 7 and 8 of the 1977 Conference which encourage both regional meetings of airlines and regular discussions between scheduled and non-scheduled carriers on tariff matters.[163]

In sum, the 1980 Conference showed that there was a firm support for a multilateral ratemaking system and condemned unilateral actions as contrary to the spirit of the Chicago Convention. The majority of participating States thus refused to incorporate the "country of origin" and the "dual disapproval" rule into the Standard Bilateral Tariff Clause (mentioned above). Recommendation 9, which was adopted in the context of international opposition to the CAB Show Cause Order,[164] is directly aimed against the new American ratemaking policy:

"The Conference:

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162. Recommendation 6, AT Conf/2, ICAO Doc. 9297, at 31. In this regard, the Conference encouraged IATA to continue its work in developing a multilateral system of currency conversion.

163. Recommendation 7, id. at 32.

164. See supra, Section I.

1. Recommends that the examination of any system for the multilateral establishment of international tariffs should involve the participation of the entire international aviation community;

2. Recommends that unilateral action by governments which may have a negative effect on carriers' efforts towards reaching agreement should be avoided;

3. Recommends that international tariffs should be established multilaterally, and when established at regional level the worldwide multilateral system should be taken into consideration; and

4. Recommends that the worldwide multilateral machinery of the IATA Traffic Conferences shall, wherever applicable, be adopted as a first choice when establishing international fares and rates to be submitted for the approval of the States concerned, and that carriers should not be discouraged from participation in the machinery."[165]

The 1980 Conference confirmed the validity of Recommendation 10 of the 1977 Conference which urged the Council to undertake a study in order to develop a new intergovernmental machinery for the establishment of tariffs

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165. It should also be noted that the 24th Assembly of 1983 adopted a Resolution requesting States to avoid unilateral measures that could inhibit the smooth flow of the worldwide system and to ensure that domestic policies are not applied to international air transport without taking due account of its special characteristics. See Assembly Resolution A24-14, ICAO Doc. 9414, A24-Res. at 56.

"without excluding the convenience of maintaining the existing machinery".[166] In this regard, one should recall Recommendation 9 of the 1980 Conference (mentioned above) which invited States to adopt the IATA tariff machinery as the preferable multilateral vehicle in the first instance. Although this Recommendation was not intended to supersede Recommendation 10 of the 1977 Conference, it is interesting to compare the two Recommendations. Support for the IATA machinery seems much stronger in 1980 than in 1977. This is, of course, because the intervening years had seen both the reorganization of IATA and the initiation of the Show Cause Order proceedings.[167]

Finally, Recommendation 13 of the 1977 Conference urged States to require that carriers discuss tariff proposals in advance with their government and to submit tariffs to the governments concerned for approval. These rules were enclosed in the ICAO Standard Tariff Clause which was endorsed by the 1980 Conference. It was also recommended that carriers should submit tariff proposals at least 60 days in advance of their proposed date of effectiveness and that each government should announce its decision within 30

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166. See Recommendation 10, SATC (1977), ICAO Doc. 9199 at 25; AT Conf/2, ICAO Doc. 9298, at 39.

167. See supra, Section I.

days after the submission of tariff proposals.

Mechanisms for the Establishment of Non-Scheduled Passenger Tariffs

The 1980 Conference concurred with the view of the Fares and Rates Panel that recommendations on non-scheduled passenger tariff machinery should be considered as applying essentially to affinity group, non-affinity group and inclusive tour charters. In each area, the Conference thereafter examined the role of intermediaries, carriers and governments in the establishment of tariffs. While some delegates did not consider it judicious to regulate non-scheduled operations,[168] the majority thought that the regulation of the two types of service should be harmonized since the distinction between them has become increasingly vague.

The maintenance of a balance between non-scheduled and scheduled passenger tariffs was likely to contribute towards stabilizing the economics of both non-scheduled and scheduled traffic. Consistent with this balance and in the interest of users, the 1980 Conference urged States to allow

168. According to those States, non-scheduled tariffs should be established by air carriers alone in accordance with the market forces.

non-scheduled operators the maximum flexibility possible.[169] Moreover, the ICAO Standard Bilateral Tariff Clause was recommended for use, wherever possible, for both scheduled and non-scheduled operations.[170] However, if it should become necessary for a State to regulate non-scheduled fares unilaterally, the particular tariff controls should then be decided with the participation from all concerned Parties; controls should be kept flexible and should be announced as far in advance of implementation as possible.[171] As for the intermediaries, given their important role, they should be subject to licensing and regulatory procedures, for a State's own originating traffic.

In conclusion to this subject, the Conference adopted a text which was a guideline to States in the establishment of non-scheduled passenger tariffs, and described the stages and procedures considered desirable.[172]

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169. Recommendation 19, AT Conf/2, ICAO Doc. 9297 at 45.

170. Recommendation 15, id. at 43.

171. Recommendation 20, id. at 45-46.

172. Recommendation 21, id. at 46-47.

Mechanisms for the Establishment of Freight Rates (Scheduled and Non-Scheduled)

While the IATA machinery for coordinating freight rates is similar to that for passenger fares, the process is more complicated, given the complexity and heterogeneity of airfreight. The role of freight forwarders and agents received major attention during the 1980 Conference. Since this group plays a significant role in the development, movement, and pricing of airfreight, its input in the development of airfreight rates was considered essential. In this regard, some participants considered a regulated multilateral environment to be a necessity, although they had serious objections to many aspects of the existing IATA system.[173]

Simplification, by elimination of the discriminatory elements of many specific commodity rates, is considered high on the list of priorities. It would also reduce tariff violations and improve the enforcement process. As to governments, some delegates recommended that the forwarders and agents be licensed, at least, for their own

173. This proposal was submitted by FIATA (International Federation of Freight Forwarders Association), see Id. AT Conf/2 WP/26. It is, however, interesting to note that both FIATA and IATA had recently agreed to establish a joint consultative Council.

originating traffic.[174] The Conference also recommended that airlines should provide governments with timely, accurate and adequate information to expedite the government decision-making process.[175] In brief, there was a strong consensus at the 1980 Conference for consultations both on a national and international level between airlines, users and intermediaries which aimed at a more flexible and simple freight rate structure.

The 1980 Conference further addressed the issues of the co-existence and harmonization of methods by which fares and rates are established,[176] and of tariff enforcement. As to the latter subject, the Conference took note of the change in the nature of IATA's compliance machinery, from a punitive to a preventive one,[177] and adopted Recom-

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174. See Recommendation 25, id. at 53.

175. Recommendation 26, id. at 54.

176. On this subject, the Conference adopted Recommendations 27 and 28 relating to the influence of fuel costs on tariffs.

177. See supra, Section I (IATA's 1978 Restructuring). It should also be noted that IATA in 1981 had established a "Fare Deal Monitoring Programme" having the functions of monitoring market conditions, assisting local airline action groups and regional airline associations, and recommending remedial action where appropriate. Such remedial action could include adjusting tariff levels and ensuring that the public was offered clear, practical and economic levels. See ICAO Secretariat Working Paper, "Enforcement of Air

mendation 29:

> "The Conference
> Recommends that States whose airlines participate in the tariff coordinating machinery of IATA support the IATA compliance system and urge their airlines to maintain an effective compliance system with respect to those participating airlines."

It should, however, be noted that the extent to which these enforcement procedures can be applied on a worldwide basis depends on the degree to which multilateral agreements are in effect. It is therefore necessary for governments to support even more strongly the establishment of multilateral agreements. The cases where multilateral agreements do not exist, there is a need for national enforcement programs, requiring the filing and approval of tariffs, authorizing the investigation of violations and the imposition of penalties.

During the period between 1981 and 1985, the Fares and Rates Panel held four meetings to continue its work programme.[178] In these meetings, the Panel studied a number of tariff related issues, such as baggage allowances and charges, denied boarding compensation, conditions of

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Carrier Tarrifs", submitted to the Economic Commission of the 24th Assembly, A24-WP/152, EC/27 (5/10/83).

178. See FRP/5/6/7/8 - Reports.

carriage and the IATA currency conversion system.[179] With regard to baggage allowances and charges, the fifth meeting of the Panel adopted one recommendation. As to the same issue, and also the subjects of denied boarding compensation and conditions of carriage, the Panel's sixth meeting adopted a total of seven recommendations. The seventh meeting of the Panel continued this work on tariff related conditions focusing on rules governing: (a) fare construction; (b) effectiveness date of fares; (c) restrictions on the availability of fares; (d) changes or cancellations of tickets; and (e) compensation for delay. Under these sub-titles, the Panel's seventh meeting adopted a total of eight reommendations. Finally, in its eighth meeting of October 1984, the Panel completed its examination of the diversity of fare conditions by reviewing the question of their presentation to governments, concluding that a standard format for tariff filing could, in certain instances, provide benefits to governments and users. In this regard, it was felt that ICAO could provide a role in developing a filing format for optional use by States in need of such guidance. Accordingly the Panel members developed the following Recommendation:

"ICAO should develop guidelines for the

179. This work has its origin in Recommendation 12 of the 1980 Conference. See infra (footnote 184).

> format for the tariff filings submitted by airlines to governments, for optional use by States and adaptation to particular situations."[180]

While this Recommendation does not specifically cover the question of tariff justification, reference material in this area will be included in the guidance developed by ICAO.

A review of the Fares and Rates Panel between 1981 and 1985 leads one to say that the Panel of Experts has lost steam. Instead of examining the structure of the international tariff machinery, the Panel has shifted its focus to considering the details of what the machinery produces. Small subjects such as baggage allowances and IATA's currency conversion system seem to be the main concern. The very detailed nature of the issues being taken up by the Panel may well undermine the importance and relevance of its main mission.

Evaluation of ICAO's Work

(1) In reviewing the work of ICAO's 1977 and 1980 Air Transport Conferences on air transport ratemaking, one can only conclude that there is a growing tendency towards interdependence in this field between IATA and ICAO. The

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180. Recommendation 2 of the Panel's eighth meeting, FRP/8 (Oct. 1984).

1977 Conference recommended that ICAO should be represented by observers at the IATA Traffic Conferences.[181] This Recommendation was implemented and an ICAO observer has attended a series of IATA Traffic Conferences. The 1980 Conference supported and encouraged the continuation of this approach.

(2) The two Air Transport Conferences recommended that ICAO's contracting States should take into account, when reviewing tariffs, the views of States whose airlines are not IATA members, but which are prepared to co-operate in a multilateral framework for the establishment of tariffs.[182] These Recommendations, in fact, may be confusing for it can be argued why the reverse situation should not be taken into consideration, that the non-IATA carriers be invited to take IATA tariffs into account.

(3) It can also be stated that some Recommendations were even aimed at making the IATA tariff structure less confusing for the man on the street. It was proposed that influence should be exerted by ICAO to achieve a simplifica-

181. Recommendation 6, SATC (1977), ICAO Doc. 9199 at 23. Egypt was behind adopting this Recommendation. It, in fact, submitted to the Conference a draft proposal to the same effect, see id.

182. Recommendation 5, id. at 22; Recommendation 8, AT Conf/2, ICAO Doc. 9297 at 33.

tion of the fare structure and types of fares by IATA.[183] In addition, the 1980 Conference directed the ICAO Council to undertake a general review of the rules and conditions related to international fares and rates in order to reduce complexity and protect user interests.[184]

(4) The 1977 and 1980 Conferences showed that there was a firm support by the international aviation community for a multilateral coordination ratemaking system and condemnation of unilateral actions as contrary to the spirit of the Chicago Convention. In this respect, the 1980 Conference recommended that the worldwide IATA Ratemaking machinery should, wherever applicable, be adopted as a first choice in the establishment of international tariffs.

(5) As evident from the above observations, the results of the two Conferences confirm the fact that a special relationship exists between IATA and ICAO, as both are dedicated to fostering of international air transport. Together, they have worked to ensure world progress through aviation, and they jointly contribute through co-operative efforts to the success of that complex enterprise which is

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183. Recommendation 12, SATC (1977), ICAO Doc. 9199 at 26.

184. Recommendation 12, AT Conf/2, ICAO Doc. 9297 at 38. This Recommendation was implemented by the Fares and Rates Panel. See supra (footnote 179).

international air transport. It is therefore, according to one commentator, "a unique relationship which must continue to the benefit of the international air transport industry".[185] Indeed, without organizations like ICAO and IATA, international air transport would probably be in a state of chaos.

(6) With regard to ICAO's work after the two Conferences, the Fares and Rates Panel held four meetings between 1981 and 1985. In the course of these meetings, one can say that the Panel has shown a willingness to involve itself in user-related problems encountered in air travel, for example: denied boarding, differing baggage systems, etc. These have nonetheless been tackled in a pragmatic manner. Of greater significance, however, was the Panel's examination of the complexity of the fare structure and the extent to which States through ICAO should seek greater simplification. The Panel concluded that the benefits of diversity in the fare structure outweigh the possible benefits of simplification or standardization - a position based on the belief that carriers should be left to apply their commercial judgement in the marketplace and that government intervention should be limited to defined

185. See Aagaard, "IATA and ICAO - A Unique Relationship", IATA Review at 16 (Oct.-Dec. 1984).

situations.[186] This is an important statement of principle for an ICAO Panel and, if adopted by the Third Air Transport Conference, indicates that there should be clear limits to government involvement in airline commercial matters, individually and through ICAO.

PRELIMINARY CONCLUSION

IATA is the trade association of the world's scheduled international airlines.[187] By far the great majority of significant scheduled international airlines are IATA members. IATA is more than an ordinary trade association, facilitating relations between member airlines, and representing and advocating the interests of the airline industry before (inter) governmental and other authorities. In addition to performing trade association activities, IATA's most important function has been the task to determine, under governmental supervision and approval, many of

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186. This is in direct contradiction to earlier Recommendations reached by the first two Air Transport Conferences and implies a threat to limit IATA's role in pricing.

187. IATA satisfies the definition of a trade association as a "non-profit organization whose members are business firms, usually competitors". See Lamb & Shields, Trade Association Law and Practice, Toronto at 3 (1971).

the world's scheduled international air fares and rates.

While governmental consent and guidance is imperative, governmental control and the day-to-day operation of the system is impractical. Inter-carrier fora have undoubtedly proven to be an effective catalyst into which governmental policies can be injected, with appropriate reference to economic and technical detail being added by the carriers themselves. In other words: IATA is a necessary need because of two facts - the economic characteristics of airline service virtually compel the same fare by all the airlines in a market, and the political division of the world into sovereign nations gives each government a veto over the fares to be charged by all airlines serving its territory. IATA, then, is only a mechanism reflecting a combination of the economic fact with the political fact.

There have been many modifications in the IATA Conference machinery and Conference processes over the past four decades, the most far-reaching occurring in 1979. Reflecting the need to respond flexibly to differing market situations, Conference negotiations were broken into smaller geographic areas, and new forms of "limited" agreements were introduced. Coordination with regional airline associations was expanded. The Conferences were opened to observers from the ICAO Secretariat and members of the Fares and Rates Panel. Recently, government participation was extended to

include observers from regional civil aviation organizations.

It should also be noted that the trend towards a more liberal approach to government regulatory oversight has meant adaptation of the IATA multilateral machinery and processes to provide for greater flexibility and increased scope for innovation. This trend does not undermine, however, the basic role of airline tariff coordination; indeed many of the benefits of multilateral tariff coordination are enhanced by these developments. For example, airline response to customer and market pressures has been the introduction of a broad range of products, fare options and associated conditions. For the traveller, the travel trade and the airlines themselves, this creates a greater need for the tariff and routing data coordinated through the IATA machinery. Additionally, this machinery provides a mechanism for the rapid introduction of innovative pricing or service concepts throughout the world.

Over the years, the issue of an alternative pricing system to the present IATA machinery has been raised. Based on past experience, however, it is doubtful if, despite all IATA's imperfections, an alternative system can be found that is acceptable to the international aviation community. Given the diverse objectives and policies of various nations, many of which regard their national flag carriers

as public utility operations as opposed to being simply commercial ventures, the IATA negotiated solutions may not have been ideal, but they have been generally successful.

This may be attributed to the fact that the IATA pricing machinery represents an effective compromise for maintaining an integrated worldwide air transportation system, with minimal governmental involvement in commercial operations and minimal intergovernmental confrontations. Cicero, over 2000 years ago, observed that "the only way to help yourself is to help others". Indeed, IATA has been and continues to be, the only universal multilateral working link, in an otherwise bilateral regulatory system, that has offered absolute benefits to the consumers, carriers, governments and the worldwide community at large.

CHAPTER VIII

FINAL REMARKS AND CONCLUSION

Dramatic changes have taken place in the regulatory regime of international aviation since the Chicago Convention of 1944 and the Bermuda I Agreement of 1946. Since then, not only have more participants entered the marketplace, but also air transportation has become a major factor in the economic, political and social development of all nations. These developments coupled with advances in aviation technology have created an air-transportation system that is massive in size and complexity. In recent years, airlines and their governments have found the regulatory regime developed after World War II to be incapable of accommodating the continuously changing air transportation system. As a consequence, the United States government adopted new aviation policies and attempted (between 1978 through 1982) to change certain features of the existing regulatory regime. This action on the part of the United States was received unfavourably by the international aviation community, which, as evidenced by ICAO's Air Transport Conferences, recommended that the difficulties faced by the system must be discussed and resolved through

common approaches, taking into consideration the interests of all participants.

In this sense, the worldwide regulatory changes have followed two distinct directions. For example, in the United States, deregulation has relaxed capacity and price control, whereas in other parts of the world capacity and price controls have expanded. Both forms of regulatory changes have allowed the introduction of deep discount fares to capture the price-sensitive market and increase productivity. The United States government favours free determination of capacity while the majority of other governments support predetermination (or at least ex post facto review) of capacity. The Americans support double disapproval or country of origin tariffs while others favour double approval, third and fourth freedom, or multilaterally coordinated fares. The proponents of each form of policy consider their policy to be optimal for the passenger, carrier and government. The conflicting policies are the consequence of how different countries view the function of their carriers and the roles these carriers play in national economies and political philosophies. The United States believes in competition and preservation of the free-market economy to the maximum extent possible. Other countries favour, in varying degrees, more direct government participation in the industrial sector of their economies.

In the United States, the domestic airline industry has been deregulated and, for all practical purposes, all carriers (and virtually all would-be-carriers) are now free to serve, or to cease serving, any and all domestic routes and cities. However, even though some seven years have passed since its enactment, deregulation remains controversial. Deregulation has had the potentiality of prompting competition and providing more price-service options. Passenger fares have been decreased for some areas, but drastically increased for others. There has been reduction in labor costs and continuing movement toward greater efficiency. In less visible ways, nevertheless, deregulation also has led to cost inefficiencies in some areas of carrier operation. The airline industry has not reached an equilibrium point, and there remains much doubt and misunderstanding over the deregulatory impacts being experienced.

In international air transportation, the "open skies" regime sought by the architects of domestic deregulation has been only partially realized, because of the resistance of most foreign governments. While a few nations saw advantages for their (usually single) national carriers in the concessions they could obtain by accepting more "liberal" bilateral agreements with the United States, most nations were unwilling to eliminate regulatory controls. On

many routes, competition was increased by the authorization of new carriers; (e.g., between the United States and the United Kingdom), but most often this has been accomplished within a framework which still retained governmental veto over entry, fares, and even the level of capacity operated.

Complete "liberalization" today would throw nations' flag carriers into a competitive fray in which only the "fittest" would survive. For reasons such as national pride, governments with the least efficient flag carriers would abruptly "slam the brakes" on competition. Also, because most international airlines are government-owned, unrestricted competition could cause "suicidal" price wars with the State footing the bill for any losses incurred. Given the divergent and conflicting objectives of various airlines and governments, it is believed, as indicated in the "Preliminary Conclusion" of Chapter III of this work, that the acceptable formula may lie between the two extremes of total freedom and total regulation - i.e. "enlightened regulation" or "regulated competition".

Unlike its principal aviation trading partners, the United States government initially subordinated the maintenance of a strong American-flag air transport system to the consumer benefits that it perceived in increased competition. In so acting, however, it failed to recognize that United States carriers face serious unfair competitive

practices, discrimination and biases toward their operations abroad. More recently, partly as a result of Congressional pressure, the trend in bilateral air transport negotiations has (as was noted in Chapter III, Section III) been to seek more balanced exchanges of economic opportunities for the carriers. The need for some regulation in international aviation is obvious. The United States carriers, despite their efficiency, are being forced to retrench, given the nature of their foreign-flag competition. The latter are mostly government-owned carriers with access to government subsidy and ability (in some cases government support) to control the market. Thus, for the sake of assuring a powerful national-flag industry, the United States policy toward international aviation may find it inevitable to back away even further from the initial extremes of "open skies" purposes.

Viewed over the long term, the various trends of regulation in international air transport reflect lack of cohesion among nations and an inability to resolve philosophical differences over precisely how international aviation should be structured. On the one hand, unilateralism and bilateralism have been more prevalent, particularly under international deregulation policy; on the other the majority of nations have advocated multilateral approaches, especially within the framework of ICAO. The regulatory

regime of international air transport has lost its uniformity. Some legal concepts have even become quite meaningless. One only has to mention the issues of the distinction between scheduled and non-scheduled operations and the Bermuda capacity principles as examples. From a consumer point of view, it is sometimes difficult to find one's way through this jungle, chiefly in the area of international air transport tariffs.

The ambiguity that now surrounding international aviation makes one unable to resist concluding that it is hard to discern an international economic law of air transport. Politics and ever expanding unilateral regulations are all that remains. This leaves one indeed to speculate about the forces that will shape the future regime of international aviation.

THE POSSIBLE SOLUTION

One can criticize the present regime of bilateral air transport agreements on grounds of extreme complexity and hence urge its replacement by a truly multilateral framework, for the sake of simplicity. However, the world aviation community is undoubtedly far too pluralistic to arrive in the near future at a comprehensive, global regime of rules. Also, it is highly unlikely, given present

national attitudes, that any system which does emerge will be based on principles of free competition and marketplace forces.

There is, however, another process which, if followed, could ultimately lead to global multilateralism. It is the writer's view that multilateralism in the form of regional air transport agreements are practicable and would constitute the first step in a method that could result in a worldwide multilateral air transport agreement. Indeed, international air transport is a worldwide system. Services covering great distances in a short time go nearly always beyond the geographical limits of the nations in the world. Aviation thus needs a global regulatory framework to permit operations on an international basis. Any legal framework for air transport set up on a regional geographical basis by a group of nations should therefore be conceived as a sub-system of the worldwide system. This means that regional co-operation should not be a defensive and isolated effort, but a way to better integrate into the global air services network of the future to arrive at a truly multilateral economic regulatory regime for aviation.

Chapter IV of this study discussed in detail the various forms and motives underlying regionalism. It should be noted here that perhaps the simplest yet most cogent reason for regional agreements is that a multilateral

system, by its very nature, presents opportunities and benefits which are unavailable in a strictly bilateral regime. For example, consider the exchange of cabotage rights with the United States. No nation could, in bilateral negotiations with the United States, secure intra-American cabotage rights for its carriers because it would have no comparably attractive rights to offer in return. In a multilateral setting, however, neighbouring nations or a group of countries (e.g. Western European States) could obtain such rights because they could together agree to extend to United States carriers operating privileges on their intra-routes. The fact that commercial traffic rights would be exchanged within a single negotiating framework would enable participants to strike otherwise unlikely deals.[1]

The same logic which illustrates why "collective"

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1. Proponents of multilateralism have frequently illustrated the possibilities available here with a reference to the exchange of fifth freedom rights. The exchange of such rights on a strictly bilateral level, it is argued can "become entirely valueless if traffic rights are not granted by the third country concerned". See Gertler, "Order in the Air and the Problem of Real and False Options", 4 Annals of Air and Space Law at 103 (1979). Thus, only in multilateral negotiations, with all three countries concerned taking part, can there be an effective exchange of fifth freedom rights. Of course, in the case of the U.S. such a grant under present legislation would be unlawful (see S. 1108(b) of the Federal Aviation Act of 1958).

bargaining may result in trade-offs not possible in a bilateral context also supports the argument that multilateral agreements are more likely to facilitate the creation of antidiscriminatory norms. For example, persuading a country to renounce the preference it extends to its carriers will be facilitated if collective pressure is brought to bear on that country rather than if any single nation attempts to bargain alone. The same would be true where another country levies discriminatory airport and user charges, unfair business and other charges, etc. Moreover, once the norms were established, a multilateral arrangement might serve as a more effective deterrent to unilateral or protectionist practices: the offender might be threatened with group sanctions, for instance, if it sought to raise user charges unreasonably. In addition, an international arbitration mechanism for the resolution of aviation disputes might be institutionalized, further reducing the possibility of disruptive unilateral action.[2]

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2. See supra, Chapter IV, Section III (footnote 136). Also, Inis Claude has once suggested that multilateralism can be most useful in "mobilizing the collective condemnation of a State whose behaviour is alleged to fall below acceptable international standards". Claude, "Multilateralism-Diplomatic and Otherwise", 12 Int'l Org. at 43-45 (1958). Such an arbitration mechanism has been proposed by Dutch officials advocating a "plurilateral" air transport agreement. See "Netherlands Again Pushes Plurilateral Air Transport Agreement", Aviation Week & Space Tech. at

Another significant quality of a multilateral order in aviation is that it would produce a more uniform body of air law than is presently possible. Currently, bilateral agreements "sectionalize" the world; they "crisscross and buffet one another to create a disorderly jigsaw puzzle"; and they form "a spiderweb of crossed and sometimes conflicting threads".[3] A multilateral system could create a single set of principles governing all airline operations in what many believe is functionally a single market.[4] This approach would be less cumbersome; and to the extent a majority of neighbouring nations join, significant operating efficiencies might be achieved. Finally, multilateralism might also introduce an element of stability into a highly volatile system. Former CAB Chairman Robson has noted that "what is desperately needed (in civil aviation) is focus and continuity",[5] and former Chairman Kahn has remarked that

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(continued from previous page)
40 (Nov. 3, 1980).

3. Doty, "U.S. Policies Spawn Resentment", Aviation Week & Space Tech. at 25 (May 8, 1978).

4. James Atwood, "Regional Aviation Agreements: A Desirable Alternative to Bilateralism", a lecture to the International Aviation Symposium in Kingston, Jamaica at 11 (Feb. 1, 1979).

5. "The Perils of No Policy on International Aviation", Bus. Wk. at 104 (Aug. 16, 1976).

the present state of international aviation calls for a "clear, overarching constitutional settlement" which is "comprehensive" and "organized".[6] Bilateral pacts, since they are flexible and easily renegotiated, promote a certain amount of instability in international air law. A multilateral pact would be more permanent, less susceptible to change, and hence would be norm-creative rather than norm-disruptive.

One might speak of a variety of types of regional air transport agreements on the basis of the existing examples of multilateral arrangements by regional groups of nations. However, in the interest of simplicity and practical purposes, such regionalism may be classified into the following two general forms:

(1) The first type would be a decision made by neighbouring nations to form an integrated union for purposes of their internal air transport, with all distinctions of national carriers eliminated. For example, the countries of a continent or subcontinent could decide to eliminate bilateral agreements among themselves and have all carriers within the region governed by a single document and a single aviation authority. This would undoubtedly promote more economically rational route structures, schedules and

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6. Gertler, op. cit., note 1, at 99.

tariff frameworks.

(2) The second form of regionalism would be an agreement among a group of neighbouring countries to treat itself as a single unit for purposes of conducting air transport negotiations with third nations. An example of this sort of co-operation is found, as indicated in Chapter IV, in Scandinavia, where Denmark, Norway and Sweden operate as a single entity (SAS) in their aviation negotiations with other States. Indeed, this is a concrete example of the potential effectiveness of regional co-operation, and one is hopeful that this concept could expand to cover wider geographic regions.

It should be noted that these two forms of regionalism can operate either independently or in conjunction. This means, a group of countries could build an integrated air union for purposes of their local air services but at the same time could negotiate with other nations on a bilateral, country-to-country basis. Similarly, a group of States that agrees to act as a unit vis-à-vis third nations might still practice bilateral agreements vis-à-vis each other. But it is also possible for a regional grouping to incorporate both concepts - to have a domestic air union and to act as a unit vis-à-vis third nations.

It can be argued, however, that political and economic incompatibilities as well as local nationalism

amongst different States, particularly the smaller ones, would preclude a significant role for regional participation in negotiations. There is also the very important issue of precisely what governing regime the neighbouring nations will adopt in case of eliminating bilateralism. It is not impossible to imagine replacement regimes that will retain all the disadvantages of bilateral agreements.

No one underestimates these difficulties. However, what is critical to the success of regionalism is that the importance of national boundaries and national-flag carriers diminish, and that airlines within the region have enhanced flexibility to develop economically rational route structures and schedules, and pricing techniques. Only in this way can airlines hope to take full advantage of the expanded markets. Some but not a total degree of competition is needed for the viability of airlines, i.e. evolutionary but not revolutionary approach. In this sense, any policy adopted within the context of regionalism should be adopted through an overall approach and not through piecemeal measures, and that such policy should be gradually implemented. This means that it should preserve the delicate balance between all interests involved (users, carriers, workers, taxpayers, etc.) and should refrain from creating a dual regulatory system.

Almost any form of regionalism presupposes a

voluntary reduction or modification of sovereignty rights. Regionalism in air transport can only be fully successful if the States/Parties are willing to closely coordinate their aviation policies with the aim to integrate the interests of their flag carriers into one "regional aviation interest". Such a regional interest would lead to an integrated air sovereignty, creating a "regional airspace" and eventually to the establishment of a "regional flag carrier". It is, however, significant to note that if no "regional nationality" replaces the nationality of the participating nations, the relations with non-participating States must be maintained on a bilateral State-to-State basis (i.e. the example of SAS).

To conclude, it is inevitable that regional co-operative efforts have a legitimate role in the development of international air transport, provided such projects take into account the broader advantages of an effective system of world aviation and communications and do not become unduly parochial in outlook. In additon, it appears that the legal problems created by such joint undertakings are capable of concrete solutions that would accommodate the interests of all the nations involved. The regional approach is eminently suited to eventually find and build a universally acceptable global regulatory framework for international aviation, adjusted to the needs of world air

transport and adjustable to changing circumstances. Progress towards this end, in addition to its own inherent benefits, will offer a substantial impetus to economic development and international co-operation in general.

However, if the present controversial regulatory regime remains unsettled, it will menace the world aviation order as continued and blatant confrontation will prompt friction and senseless economic wars. In the end, there will be no victor or vanquished but mass destruction of the finest system ever designed in the realm of public transportation. And it will be no use gloating over each other's discomfiture anymore than deriving pleasure from being proved right. But with wisdom, courage and a fair sense of play, nations are apparently capable of overcoming their problems and it behooves policymakers to heed Shakespeare when he made Alcibiades say in "Timon of Athens":

> "And I will use the olive with my sword;
> Make war breed peace; make peace stint
> war."

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