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Timothy M. Ravich[*]

ABSTRACT

In *Northwest Airlines, Inc. v. Minnesota*, a 1944 case of first impression about the constitutional limitations upon state power to tax airplanes, Justice Robert H. Jackson wrote in a concurring opinion that "[p]lanes do not wander about in the sky like vagrant clouds." Rather, "[t]hey move only by federal permission, subject to federal inspection, in the hands of federally certified personnel and under an intricate system of federal commands." Indeed, the "moment a ship taxies onto a runway it is caught up in an elaborate and detailed system of controls. It takes off only by instruction from the control tower, it travels on prescribed beams, it may be diverted from its intended landing, and it obeys signals and orders. Its privileges, rights, and protection, so far as transit is concerned, it owes to the Federal Government alone and not to any state government." Indeed, the skies are not open and unlimited for general, commercial, and military operations, but rather controlled in much the same manner as interstate highways and navigable waterways. Whether and how to restrict these global airways has been a concern for both American lawmakers domestically and international aviation stakeholders, particularly in the post-war 1940s.

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The international aviation community standardized certain safety measures at the Chicago Convention of 1944, but were less successful in reaching agreement on economic issues such as protocols allowing foreign airlines to fly commercially within another's territory at prices they set. In place of a comprehensive and uniform arrangement for international airline operations, bilateral and multilateral agreements have emerged to facilitate commercial air travel. Deregulatory impulses have since eroded protectionist philosophies in the late 1980s and early 1990s as the United States and Europe and other nations have pursued "Open Skies" policies that have liberalized wide swaths of international travel. While not entirely free to wander about the sky uncontrolled, airliners now journey to more destinations, more regularly, less expensively, and with fewer restrictive rules.

This Article overviews the seminal issues of "Open Skies" policy, including relevant federal laws respecting airline ownership and control. Also presented is a review of airline deregulation policy in the United States, argument in favor of the expansion of so-called cabotage rights allowing foreign carriers to fly domestic routes, and discussion of the emergence of strategic airline alliances. Finally, this Article concludes with coverage of an intense and brewing controversy between major U.S. airlines, on the one hand, and Persian Gulf carriers, on the other hand, that risks Open Skies policies in the Middle East. In presenting these issues, this Article aims to introduce the reader to the unusual and historically significant ways in which aviation laws are derived in the United States and abroad, and in doing so, raise a general question about the welfare of aviation consumers overall. In conclusion, this Article criticizes U.S. carriers seeking to reverse hard-won Open Skies policies, especially given the U.S. airline industry's habit of looking to the government to get out of the way except when it comes to its own welfare. Such practice is inconsistent with principles of free competition, avoids the real market-borne issue of product competition, and is hollow when asserted by carriers who have received substantial protections under U.S. bankruptcy law to survive in a global sector that should be performance- and not subsidy-based.

I. INTRODUCTION

When Continental Airlines Flight 28 arrived at Terminal 4 at London's Heathrow Airport on March 30, 2008, at 6:45 a.m., from New York, it was decades overdue in the minds of some airline executives.[1] Until that time, a

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1 *Open Skies Causes a Continental Shift*, TRAVEL TRADE GAZETTE (U.K.), Mar. 21, 2008, at 2008 WLNR 5741461 (quoting Continental Airlines Senior Director for the United Kingdom and Ireland: "The world's premier airport was permanently written out of our brief by the most anti-competitive air service agreement, which has protected the incumbents wonderfully."); *see also* Michelle Higgins, *Open-Skies*

1950s-era pact between the United States and Great Britain strictly restricted which foreign airlines could fly commercial airline passengers to Heathrow from the United States. Among other carriers, Continental Airlines had been excluded from one of the world's busiest aviation gateways as a result.[2] In fact, over the last thirty years, only four airlines—British Airways, Virgin Atlantic, American Airlines, and United Airlines—were authorized to operate between London's Heathrow Airport and select cities in the United States.[3] This restriction eased on April 30, 2007, when the United States and European Union Member States completed a landmark "Open Skies" treaty and ushered in a new era of international air transportation. Open Skies effectively liberalized transatlantic commercial airline operations.

Under the Air Transport Agreement (ATA),[4] American and European airlines agreed to reciprocal rights to serve city pairs between the 28-nation European Union and U.S. markets. The ATA liberalized the number of international flights, aircraft, and routes, and it permitted carriers to set fares according to market demand. Moreover, it enabled international carriers to

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Promises More Flights to Europe, CHI. TRIB., Mar. 30, 2008, at 2.

2 In 2008, United Airlines and Continental Airlines announced intentions to merge; the merger was completed in 2010. *See*, *e.g.*, *Truly United?*, ECONOMIST, Sept. 9, 2013, *available at* http://www.economist.com/blogs/gulliver/2013/09/united-continental-merger.

3 The "Bermuda II" accord is the 1977 agreement between Great Britain and the United States permitting only two airlines from each country to serve London Heathrow Airport, prohibiting U.S. carriers from serving inter-European routes originating from the United Kingdom, and restricting British carriers from servicing points between U.S. cities.

4 2007 O.J. (L 134) 4-41, 46 I.L.M. 470 (2007), http://www.state.gov/e/eb/rls/othr/ata/e/eu/114768.htm; *see also* Adrian Schofield, *Will the Skies Stay Open?*, AVIATION WK. & SPACE TECH., Apr. 7, 2008, at 41.

As detailed in a May 2008 Massachusetts Institute of Technology International Center for Air Transportation White Paper, Stage One of the U.S.-EU Open Skies agreement presents numerous opportunities for an air transport market that accounts for more than half of all global scheduled passenger traffic: (1) Grants "fifth freedom" rights to all U.S. and EU carriers (both cargo and passenger). For example, United Airlines is able to fly from Washington Dulles to Paris and onward to Athens carrying Paris-Athens local traffic; (2) U.S. and EU carriers are able to code-share on flights to previously-restricted nations (*e.g.*, Greece, Spain), allowing airlines to offer new routings and service to new markets; (3) Elimination of the nationality clause allows EU airlines to restructure or consolidate into cross-border entities without jeopardizing their right to fly to the U.S. For example, Air France and KLM could merge their dual-hub operations to achieve economies of scale without losing their rights into the U.S. (although their traffic rights to other countries may be jeopardized); (4) EU airlines are able to offer transatlantic services from any location in the EU as a result of elimination of the nationality clause. This will increase competition in many markets as every U.S. and EU carrier is eligible to compete in any U.S.-EU market. For example, Air France-KLM has begun nonstop service between Los Angeles and London Heathrow, which previously was limited to four carriers (two British and two American). Similarly, Lufthansa could choose to offer nonstop service between Miami and Barcelona with no connection to Germany; and (5) U.S. regulators will consider foreign requests to hold larger shares of non-voting equity, including combinations in which the total of voting and non-voting equity exceeds 50 percent. ALEX COSMAS ET AL., FRAMING THE DISCUSSION ON REGULATORY LIBERALIZATION: A STAKEHOLDER ANALYSIS OF OPEN SKIES, OWNERSHIP AND CONTROL 2 (MIT Int'l Ctr. for Air Transp. 2008) [hereinafter STAKEHOLDER ANALYSIS OF OPEN SKIES, OWNERSHIP AND CONTROL].

enter into cooperative arrangements, including code-sharing, franchising, and leasing.[5] As important, an "Open Skies" philosophy began to replace the outmoded restrictive arrangements of bilateral aviation agreements and fostered enhanced regulatory cooperation in the areas of competition law, government subsidies, the environment, consumer protection, and security.[6] The ATA agreement also welcomed U.S. investors to buy into a European Community airline, as long as the airline was majority owned and effectively controlled by a member state and/or nationals of member states.[7] Similarly, the ATA intended to clarify that, under U.S. law, European Union investors could hold up to 49.9 percent of the total equity in a U.S. airline and, on a case-by-case basis, even more, provided that foreign nationals did not own more than 25 percent of the voting stock and the airline remained under the actual control of U.S. citizens.[8] In all, the ATA was a part of a larger initiative by the U.S. Department of State to negotiate Open Skies treaties that gave European and American airlines mutual ability and mobility to serve markets across the Atlantic Ocean, as frequently as they desired, at prices they choose.[9]

This article outlines the trend in global airline transport between Europe and the United States toward liberalized market access and calls for greater efforts to allow foreign investors to participate reciprocally in the ownership and control of domestic airlines, especially after the global economic crisis following September 15, 2008. Within this substantive framework, Part II presents the historical background and current regulatory environment governing international airline operations and management. Part III overviews the salient features of the domestic and international regulatory environment in which commercial airlines operate, including an assessment of airline deregulation in the United States, impulses to achieve cabotage rights, strategic airline alliances, and a significant emerging controversy between major U.S. airlines and three Persian Gulf carriers that risks undoing open skies accords with Qatar and the United Arab Emirates. Finally, Part IV concludes by offering some recommendations for greater deregulation and reliance on market forces in international commercial air transportation.

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5 U.S. Dep't of State Fact Sheet No. 2007/340, *U.S.-E.U. Air Transport Agreement—Open Skies Plus* (Mar. 9, 2007). Bilateral agreements continue to be a regular feature of international air commerce, particularly in Asia. *See generally* Alan Khee-Jin Tan, *Singapore's New Air Services Agreements with the E.U. and the U.K.: Implications for Liberalization in Asia*, 73 J. AIR L. & COM. 351 (2008).

6 *Id.*

7 *Id.*

8 *Id.*

9 *See*, *e.g.*, Susan Cary, *U.S. Airline Clash Over Rivals from Persian Gulf*, WALL ST. J., Feb. 24, 2015, at B1 (reporting that the U.S. State Department had negotiated 114 open skies agreements since 1992).

II. Restrictions in International Aviation

Open Skies mean a common aviation marketplace. The main benefit of such a regime is unrestricted and mutual access for airlines of different nations to international destinations without the burden of capacity restrictions.[10] Open Skies policies also represent a fresh approach to international commercial aviation that should produce public benefits and may even increase the competitive health of the *domestic* aviation market. As detailed below, however, despite the theoretical and practical appeal of Open Skies, vexing practical, political, and legal issues shadow the subject—particularly the advent of bilateral agreements and antiquated airline ownership and control rules.[11]

The challenges of Open Skies arrangements originate in world events of the last century. International airline service was beginning to take off at the end of World War II. At the same time United States lawmakers were looking inward, restricting both the ownership and control of its airlines to its own citizens. This ownership restriction was predicated upon four grounds: (1) to protect and encourage the growth of a fledgling airline industry; (2) to regulate international air travel; (3) to restrict foreign access to American airspace; and (4) to protect the military's reliance on commercial airlines to supplement military operations.

Notwithstanding its protectionist philosophy respecting airline ownership, the United States advocated in favor of a post-war world in which it had complete market access to European and foreign markets.[12] The aviation opportunities for Americans and Europeans were asymmetrical, however. Europe's airports were all but obliterated as a result of World War II while a sophisticated airport infrastructure was emerging in the United States. Additionally, as is generally true today, fewer markets existed in Europe than in the United States. Any single European nation had one or perhaps two primary destinations (*e.g.,* Great Britain has London, France has

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10 In re Defining "Open Skies", 57 Fed. Reg. 48,130 (Dep't of Transp. May 5, 1992). *See generally* Ruwantissa Abeyratne, *The US/EU Open Skies Agreement—Some Issues*, 72 J. AIR L. & COM. 21 (2007).

11 While the focus of this article is on U.S-Europe and U.S.-Middle East open skies arrangements, streamlining U.S.-Asia routes and stitching together fragmented intra-European aviation operations are themselves subjects of significant study and comment. *See*, *e.g.*, Alan Khee-Jin Tan, *Singapore's New Air Services Agreements with the E.U. and the U.K.: Implications for Liberalization in Asia*, 73 J. AIR L. & COM. 351 (2008); Gabriel S. Meyer, *U.S.-China Aviation Relations: Flight Path Toward Open Skies*, 35 CORNELL INT'L L.J. 427 (2005); Garrick L. H. Goo, *Deregulation and Liberalization of Air Transport in The Pacific Rim: Are They Ready for America's "Open Skies"?*, 18 U. HAW. L. REV. 541 (1996); *see also* Cathy Buyck, *Ambition v. Decision*, AVIATION WEEK & SPACE TECH., Mar. 2-15, 2015, at 32 ("[A]fter more than 10 years of talks, a single airspace in Europe is not closer to reality.").

12 49 U.S.C. § 40102(a)(23) ("'[F]oreign air transportation' means the transportation of passengers or property by aircraft as a common carrier for compensation, or the transportation of mail by aircraft, between a place in the United States and a place outside the United States when any part of the transportation is by aircraft.").

Paris, and Italy has Rome) whereas the United States featured fifty different states, each with their own lucrative marketplaces (*e.g.*, Atlanta, Boston, Chicago, Dallas, Los Angeles, Las Vegas, Miami, New York, Orlando, Philadelphia, Phoenix, Seattle, etc.). In this imbalanced context, Heathrow was perhaps the only bargaining chip the English had in negotiations with Americans for Open Skies rights. The United Kingdom could grant U.S. carriers access to Heathrow, but only if the United States stipulated to the same rights in various of their markets. As such, "[t]he British[,] who rightly feared that the large undamaged aviation infrastructure, commercial fleet, and manufacturing capacity of the U.S. would dominate the war ravaged systems of Europe[,] saw the U.S. proposal as self-interest masquerading as philosophical principle."[13] Consequently, a framework of rules and restrictive bilateral and multilateral agreements evolved whereby individual nations negotiated accords that controlled the rates, routes, and frequency of international airline service.[14]

"Bermuda I" was the first in a generation of transatlantic bilateral agreements. Negotiated in 1946, it permitted the International Air Transport Association to establish and control fares and tariffs along international routes between the United States and Great Britain.[15] More than thirty years later, at a time when impulses to deregulate the vast domestic cargo and commercial airline industry within the United States were taking hold, the agreement was amended by "Bermuda II"[16] through which British interests

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13 DAWNA L. RHOADES, EVOLUTION OF INTERNATIONAL AVIATION: PHOENIX RISING 23 (2003).

14 *See, e.g.*, Jessica Finan, Comment, *A New Flight in the International Aviation Industry: The Implications of the United States-European Union Open Skies Agreement*, 17 TUL. J. INT'L & COMP. L. 225, 227 (2008); Stephen D. Rynerson, *Everybody Wants to Go to Heaven, but Nobody Wants to Die: The Story of the Transatlantic Common Aviation Area*, 30 DENV. J. INT'L L. & POL'Y 421, 422, 427-28 (2002); *see also* EUGENE SOCHOR, THE POLITICS OF INTERNATIONAL AVIATION (1990) (noting that President Franklin D. Roosevelt had once cautioned against bilateral and multilateral aviation accords, which potentially might form "great blocs of closed air [that] trac[ed] in the sky the conditions of future war").

15 Air Services Agreement, Feb. 11, 1946, U.S.-Gr. Brit.-N-Ir., 15 U.N.T.S. 295. *See, e.g.*, George P. Baker, Chairman of U.S. Delegation to the Bermuda Conference, The Bermuda Plan as the Basis for a Multilateral Agreement, lecture delivered at McGill University (Apr. 14, 1947), *reprinted in* ANDREAS F. LOWENFIELD, AVIATION LAW § 1.13, at 2-9-11 (2d ed. 1981). *See generally* Paul Stephen Dempsey, *Flights of Fancy and Flights of Fury: Arbitration and Adjudication of Commercial and Political Disputes in International Aviation*, 32 GA. J. INT'L & COMP. L. 231, 238 (2004); Adam L. Schless, *Open Skies: Loosening the Protectionist Grip on International Civil Aviation*, 8 EMORY INT'L L. REV. 435 (1994); H. A. Wassenbergh, *International Air Transport: Regulatory Approaches in the Nineties*, 17 AIR & SPACE L. 69, 74-75 (1992).

16 Agreement on International Aviation, U.S.-Gr. Brit., July 23, 1977, T.I.A.S. No. 8641. *See generally* Jose A. Gomez-Ibanez & Ivor P. Morgan, *Deregulating International Markets: The Examples of Aviation and Ocean Shipping*, 2 Yale J. on Reg. 107 (1984) ("The United States traditionally has encouraged competition in aviation by avoiding agreements that restrict airline capacity and by liberalizing the rules governing charter competition. More recently, pro-competitive U.S. policies have forced a review of international pricing mechanisms, and the U.S. government has used the threat of diverting traffic to neighboring countries to establish more liberal bilateral agreements for aviation. As a

leveraged the enormous economic opportunities of London's Heathrow airport, the busiest airport in the European market. Bermuda II strictly capped the number of U.S. carriers that could serve Heathrow and "gateway cities" in the U.S. from which non-stop service to London could be offered.

Rigid laws such as "Bermuda II" that manufacture artificial restrictions on aviation investment are arcane in today's networked world.[17] As one study noted,

> [d]espite today's trend toward global markets, free trade, the internet, and the economic integration of entire continents, one of the most globalized, technology-intensive industries remains encumbered by rules that stifle competition and prevent airlines, communities, passengers, and shippers from benefiting to the fullest. The "bilateral air services agreements" . . . that continue to govern much of world trade in aviation defined the terms under which airlines will link their two home territories. These [bilateral air services agreements] often frustrate market growth, force users to pay a premium price, and create a series of vested interests.[18]

Open Skies regimes are replacing the myriad nation-to-nation bilateral and multi-state multilateral agreements of the last century, however.[19]

A. From Bilateral Agreements to Open Skies

From a practical and political viewpoint, commercial aviation is a paradox. "In terms of its operations, [commercial airline transportation] is the most international of industries, yet in terms of ownership and control it is almost exclusively national."[20] For example, in the early days of international passenger flight, an airline was the *de facto* representative of the nation under whose flag it flew. Privately-owned Pan American Airlines, with its "Clipper" fleet, was iconic of the United States in much the same way that state-owned Aeroflot represented the former Soviet Union or Alitalia represented Italy. More broadly, international aviation symbolized an accessible and boundary-less global community. Microsoft CEO Bill Gates

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result, prices and services have generally improved.").

17 *See, e.g.*, James Gjerset, *Crippling U.S. Airlines: Archaic Interpretations of the Federal Aviation Act's Restrictions on Foreign Capital Investments*, 7 AM. U. J. INT'L L. & POL'Y 173, 181-82 (1991).

18 INTERVISTAS, THE ECONOMIC IMPACT OF AIR SERVICE LIBERALIZATION ES-3 (2006).

19 Brian F. Havel, *US / EU Open Skies Negotiations: The Second Stage Begins*, IATA Econ., Apr. 2008, *available at* https://www.iata.org/whatwedo/Documents/economics/Havel_Open_Skies.pdf.

20 RIGAS DOGANIS, THE AIRLINE BUSINESS IN THE 21ST CENTURY 19 (2001). *See also* Andreas F. Lowenfeld, *A New Take-Off for International Air Transport*, 54 FOREIGN AFF. 47 (1975) (International aviation has been "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 security arrangements by which we live today.").

captured the sense of global community and seamless mobility that human flight has represented from its earliest stage when he said that, "[t]he Wright brothers created the single greatest cultural force since the invention of writing. The airplane became the first world wide web, bringing people of different languages, ideas and values together."[21]

As a matter of law, however, international airline operations are contained not only by geographical boundaries, but also by policies intended to fortify national security, economic, and protectionist concerns. Dating back at least to the Paris Convention of 1919, international aviation policies have been predicted on the Westphalian principle of exclusive sovereignty within the context of airspace. In 1944, more than fifty nations gathered for the purpose of creating and implementing a global civil aviation marketplace that respected national sovereignty without also hamstringing the development of international aviation.[22] At this Convention of International Civil Aviation commonly referred to as the "Chicago Convention," delegates announced their objectives:

> WHEREAS the development of international civil aviation can greatly help to create and preserve friendship and understanding among the nations and peoples of the world, yet its abuse can become a threat to the general security; and
>
> WHEREAS it is desirable to avoid friction and to promote that cooperation between nations and peoples which the peace of the world depends;
>
> THEREFORE, the undersigned governments have 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 equal opportunity and operating soundly and economically[.][23]

To implement these goals, Chicago Convention delegates formed the International Civil Aviation Organization (ICAO), a United Nations agency that was charged with managing international aviation operations.[24]

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21 Gregory P. Sreenan, *Aviation Law*, 77-JUN. FLA. BAR J. 44, 47-48 (2003).

22 Convention on International Civil Aviation, *opened for signature* Dec. 7, 1944, 61 Stat. 1180, T.I.A.S. No. 1951 [hereinafter Chicago Convention].

23 Int'l Civ. Aviation Org., International Civil Aviation Conference: Chicago, Illinois, 1 Nov. to 7 Dec. 1994, *available at* http://www.icao.int/publications/Documents/7300_cons.pdf. Modernly, over 190 nations are signatories to the Chicago Convention and the success of ICAO in establishing international technical standards for aircraft (*e.g.*, a series of published Annexes known as International Standards and Recommended Practices (SARPs)) is widely recognized.

24 *See* International Civil Aviation Organization, *A United Nations Specialized Agency*, http://www.icao.int/Pages/default.aspx.

While ICAO successfully created international technical standards for global aviation,[25] it was less successful in achieving its second goal of both harmonizing airline economics (*e.g.*, airline rates, fares, frequency, and capacity in international commercial aviation) and overcoming restrictions on foreign competition in domestic airline markets.[26] Instead of agreeing to a fully liberalized operational space for commercial airline operations, Chicago Convention delegates affirmed "that every State has complete and exclusive sovereignty over the air space above its territory"[27] and defined "five freedoms of the air."

The Chicago Convention freedoms include: (1) the right to fly over the territory of another country without landing; (2) the right to land in another country for technical, non-traffic reasons such as refueling or maintenance; (3) the right to discharge traffic from the home country in a foreign country; (4) the right to pick up traffic in a foreign country bound for the home country; and (5) "beyond rights" or the right to pick up passengers in a foreign country and fly them to a different foreign country, provided that the flight originated or terminated in the home country.[28] Only the first two freedoms were annexed to the Chicago Convention, leaving the remaining "freedoms" to be negotiated individually between states as restrictive bilateral agreements. Under this regime, a complex framework of nearly 1,500 bilateral agreements between multiple different nations has arisen.[29]

B. Airline Ownership and Control

In 1926 Congress enacted the Air Commerce Act to restrict foreign ownership of United States airlines.[30] The 1926 Act gave the federal government a definitive role in economic and safety aspects of commercial aviation by creating the Bureau of Air Commerce and the Civil Aeronautics Administration—the ancestor of today's Federal Aviation Administration—to develop regulations, enforceable by civil penalties, for the registration and

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25 To this day, ICAO requires communications with air traffic facilities worldwide in the English language and establishes international standards for aircraft airworthiness, flight crew certification, and radio aids to navigation.

26 J. SCOTT HAMILTON, PRACTICAL AVIATION LAW 16 (3d ed. 2001).

27 *See supra* note 23.

28 *E.g.*, Bruce Stockfish, *Opening Closed Skies: The Prospects for Further Liberalization of Trade in International Air Transport Services*, 57 J. AIR L. & COM. 599, 603-04 n.12 (1992). *See also* A.J. THOMAS, JR., ECONOMIC REGULATION OF SCHEDULED TRANSPORT 174 (1955).

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

30 Air Commerce Act of 1926, Pub. L. No. 69-254, 44 Stat. 568 (1926) (formerly 49 U.S.C. §§ 171-184 (1951) (repealed 1958). *See generally* ISABELLE LELIEUR, LAW AND POLICY OF SUBSTANTIAL OWNERSHIP AND CONTROL OF AIRLINES 32 (2003).

licensing of aircraft, and the certification and medical examination of pilots. Two years later, Congress enacted the Civil Aeronautics Act of 1928, tying airline operations to citizenship. The 1928 law limited who could own an aircraft in America by limiting eligibility to register an aircraft to citizens (or partnerships of U.S. citizens) or corporations of which the president and at least two-thirds of its board members are citizens and at least fifty-one percent of the voting shares are controlled by U.S. citizens.[31]

These laws work in tandem with the Federal Aviation Act of 1958, which requires airlines to demonstrate their "fitness" for operation as a function of ownership and control.[32] To operate as a U.S. airline, therefore, a carrier must first obtain an operating certificate of public convenience from the United States Department of Transportation (DOT),[33] and, as a precondition of that showing, demonstrate its United States citizenship. The DOT issues operating certificates only to

> (a) an individual who is a citizen of the United States or one of its possessions, or (b) a partnership of which each members is such an individual, or (c) a corporation or association created or organized under the laws of the United States or of any State, Territory, or possession of the United States, of which the president and two-thirds or more of the board of directors and other managing officers thereof are such individuals and in which at least 75 per centum of the voting interest is

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31 49 U.S.C. § 44102. *See also* Fed. Aviation Admin., Aircraft Registry, *available at* https://www.faa.gov/licenses_certificates/aircraft_certification/aircraft_registry/register_aircraft/. *See generally* Ryan Patanaphan, Note, *Navigating the Complex Skies: A Caveat on Liberalizing Foreign Ownership Restrictions in U.S. Airlines*, 72 Ohio St. L.J. 191 (2011). Under the Civil Reserve Air Fleet Program (CRAF), airlines registered in the United States contract their aircraft and crew for use by the United States Department of Defense during emergencies. The commercial airlines receive no compensation for their participation unless their fleets are activated for national security purposes, but they are given an incentive to participate by being made eligible to bid for peacetime airlift business for which payment is made at predetermined rates based on a weighted average of their costs plus a return on investment. The Department of Transportation has announced that CRAF will not be impacted if foreign ownership restrictions are relaxed. STAKEHOLDER ANALYSIS OF OPEN SKIES, OWNERSHIP AND CONTROL, *supra* note 4, at 2, 4 n.1.

32 Pub. L. No. 85-726, 72 Stat. 731 (codified as amended at 49 U.S.C. §§ 1301-1557 (1988)). *See generally* Christopher McBay, *Airline Deregulation Deserves Another Shot: How Foreign Investment Restrictions and Subsidies Actually Hurt the Airline Industry*, 72 J. AIR L. & COM. 173 (2007); Seth M. Warner, Comment, *Liberalize Open Skies: Foreign Investment and Cabotage Restrictions Keep Noncitizens in Second Class*, 43 AM. U. L. REV. 277, 307 (1993). For a discussion of the state of foreign ownership and control restrictions of the United States cargo industry, see Christopher Furlan, *Foreign Ownership and Control Restrictions in United States Airlines: Barrier to Mergers and Restructurings* (2005), *available at* http://airlineinfo.com/public/furlan.pdf.

33 49 U.S.C. § 1372(a) (2008) ("No foreign air carrier shall engage in foreign air transportation unless there is in force a permit issued by the board authorizing such a carrier so to engage."); *see also id.* § 1508(b) (2008) ("[A]ircraft permitted to navigate in the United States . . . shall not take on at any point within the United States, persons, property, or mail carried for compensation or hire and destined for another point within the United States.").

owned or controlled by persons who are citizens of the United States or of one of its possessions.[34]

Ownership of an air carrier by an American citizen is not alone sufficient for an airline to obtain DOT operating licensure. Rather, actual control of an airline by Americans is a vital consideration for regulators in determining whether to allow a carrier to operate in the United States. This recognizes national security concerns, but also reflects the fact that most of the world's airlines are government-owned or subsidized.[35] Consequently, foreign interests cannot have *de facto* control of an airline, whatever their actual ownership share.[36]

In determining "actual control," DOT traditionally has evaluated seven factors, including supermajority or disproportionate voting rights, negative control or power to veto, buy-out clauses, equity ownership, significant contacts, credit agreements and debt, and family or business relationship between foreigners and U.S. officers.[37] "In practice, DOT has interpreted control to mean that day-to-day management decisions must be made by U.S. citizens, even if there is substantial foreign investment in the airlines. That is, the law has been construed as requiring actual control of the enterprise to rest with U.S. citizens."[38]

Legislators recently considered relaxing ownership and control rules, including the rule prohibiting foreign carriers from merging with U.S. airlines or foreign investors from purchasing more than twenty-five percent of a U.S. airline's voting rights. For example, in the early 1990s the National Commission to Ensure a Strong Competitive Airline Industry recommended

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34 49 U.S.C. § 40102(a)(15).

35 For example, of the major international airlines (based on millions of passenger miles flown), Aeroflot, Air China, Air France, Air India, Air New Zealand, Alitalia, China Southern Airlines, El Al Israel Airlines, Emirates, Finnair, KLM Royal Dutch Airlines, Malaysia Airlines, Qatar Airways, Saudi Arabian Airlines, Scandinavian Airlines System, South African Airways, TAP, Thai Airways, and Turkish Airlines are either totally or partially government-owned. AVIATION WEEK. & SPACE TECH. AEROSPACE SOURCE BOOK 344-381 (2008). Only Air Canada, All Nippon Airways, Asiana Airlines, British Airways, Cathay Pacific Airways, China Eastern Airlines, Japan Airlines, Korean Air, Qantas Airways, and Ryanair are 100 percent publicly traded. *Id.*

36 *See generally* Josh Cavinato, Note, *Turbulence in the Airline Industry: Rethinking America's Foreign Ownership Restrictions*, 81 S. CAL. L. REV. 311, 316 n. 27 (2008). Lufthansa German Airlines purchased a 19 percent stake in JetBlue in December 2007, representing the first major investment by a foreign airline in an American rival since British Airways invested in American Airlines in the early 1990s. *See e.g.*, Andrew Ross Sorkin et al., *JetBlue Sells Stake to Lufthansa for $300 Million*, N.Y. TIMES, Dec. 14, 2007, at C2 ("The interest . . . is the latest example of foreign investors leveraging the strength of their currencies against the dollar.").

37 Review of Data Filed by Certificated or Commuter Air Carriers to Support Continuing Fitness Determinations Involving Citizenship Issues, Fed. Reg. 44, 675 (July 30, 2003) (to be codified at 14 C.F.R. pt. 204).

38 49 U.S.C. § 40102(a)(15); *see also* GENERAL ACCOUNTING OFFICE, GAO-04-34R 2, ISSUES RELATING TO FOREIGN INVESTMENT AND CONTROL OF U.S. AIRLINES (2003).

that the

> Federal Aviation Act be amended to allow the U.S. to negotiate bilateral agreements that permit foreign investors to hold up to 49 percent voting equity in U.S. airlines, providing those bilateral agreements are liberal and contain equivalent opportunities for U.S. airlines; the foreign investor is not government-owned; there are reciprocal investment rights for U.S. airlines, and the investment will advance the national interest and the development of a liberal regime for air services.[39]

DOT itself proposed increasing the stake foreigners might hold in U.S. airlines to forty-nine percent, thereby enabling U.S. airlines access to international capital markets, encouraging U.S. airlines to develop more efficient market driven-networks, creating opportunities for airlines to enter into new markets, and achieving consistency with the European Union and other bilateral partners' foreign investment restrictions.

In all, airline ownership and control rules in the United States are byproducts of aviation policies formulated during the middle of the last century. While the legal requirement that only American citizens own and control an airline traditionally has been viewed as necessary to optimize national security and prevent airlines from flying under "flags of convenience" in countries with lax safety regulations, such arguments are more difficult to sustain in today's globally networked and interconnected marketplace.[40]

Indeed, strategic alliances between and among airlines have emerged as a partial step toward integrating airline operations across borders without violating strict ownership and control laws. Long a marketing tool in tourism and hospitality industries, strategic alliances have gained prominence in today's airline business. This is particularly true in light of the limitations of bilateral agreements and international aviation economic policies. In the airline industry strategic alliances have taken the particular form of "code-share" arrangements. These arrangements allow domestic and foreign carriers to pool selected resources, including frequent flyer programs, airport lounges, marketing strategies, scheduling, maintenance, revenues, and common ownership interests.[41]

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39 NATIONAL COMMISSION TO ENSURE A STRONG COMPETITIVE AIRLINE INDUSTRY, CHANGE, CHALLENGE AND COMPETITION, A REPORT TO THE PRESIDENT AND CONGRESS 22 (1993).

40 *See generally* L. F.E. Goldie, *Environmental Catastrophes and Flags of Convenience—Does the Present Law Pose Special Liability Issues?*, 3 PACE INT'L L. REV. 63, 64 n.5 (1991); Howard Kass, *Cabotage and Control: Bringing 1938 U.S. Aviation Policy into the Jet Age*, 26 CASE W. RES. J. INT'L L. 143, 150 (1994); Ved P. Nanda, *Substantial Ownership and Control of International Airlines in the United States*, 50 AM. J. COMP. L. 357, 359 (2002); Moritz Ferdinand Scharpenseel, *Consequences of E.U. Airline Deregulation in the Context of the Global Aviation Market*, 22 NW. J. INT'L & BUS. 91, 110 (2001).

41 *See, e.g.,* Stephen B. Moldoff, *Union Responses to the Challenges of an Increasingly Globalized*

While code-sharing is a recent marketing and business strategy, airline alliances existed well before airlines were economically deregulated in the United States. The first airline partnership may have arisen as far back as the 1940s when Air France helped to set up airlines in Africa, *e.g.*, Royal Air Maroc and Tunisair.[42] Airline alliances have grown from simple shared agreements at the carrier level to complex networks of dozens of international airlines serving hundreds of destinations with thousands of daily flights, for example, OneWorld, Sky Team, and Star Alliance.

Federal law defines "code-sharing" to mean "an arrangement whereby a carrier's designator code is used to identify a flight operated by another carrier."[43] A "designator code," in turn, is a multiple letter character code that identifies a particular flight, for example, "UA123" for United Airlines Flight 123. Code-sharing arrangements are smart business because they offer consumers what they want, namely "online" as opposed to "interline" connections. An interline itinerary involves travel on one airline from point A to point B and on a different airline from point B to point C. In contrast, code-sharing provides passengers one-stop shopping by allowing different airlines to offer one-stop service from point A to point C, with each airline independently setting the price for service between cities that it otherwise would not have served. After Congress enacted the Airline Deregulation Act code-sharing arrangements quickly replaced interline service, which declined as a percentage of all trips with a connection from about forty percent to a mere five percent.[44]

Several airline industry analysts have concluded that airline alliances have reduced fares by about five-to-seven percent on certain city pairs, while increasing total traffic by as much as six percent.[45] Continental Airlines leader Gordon Bethune described the benefits and efficiencies of code-sharing and airline alliances to Congress in 1998 in connection with a proposed alliance with Northwest Airlines:

> The creation of new online options for the U.S. consumer is a key benefit of any alliance. Take a market like Madison, Wisconsin. Northwest is currently one of nine airlines flying to Madison. Continental does not fly to Madison at all. Now let's consider destinations like Panama City, Panama or Midland, Texas. The only online option currently available

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Economy, 5 RICH. J. GLOBAL L. & BUS. 119 (2005).

42 Ero Vaara et al., *Strategies as Discursive Constructions: The Case of Airline Alliances*, 41 J. MGMT. STUDIES 1 (2004).

43 14 C.F.R. § 257.3(c).

44 *See e.g.*, Gustavo Bamberger & Dennis Carlton, *Airline Networks and Fares in* HANDBOOK OF AIRLINE ECONOMICS 269-88 (Darryl Jenkins, ed., 2003).

45 Gustavo Bamberger et al., *An Empirical Investigation of the Competitive Effects of Domestic Airline Alliances*, 47 J. L. & ECON. 195 (2004).

> between Madison and these points is American [Airlines]. Continental does not serve Madison; Northwest does not serve Panama City or Midland. By linking these systems, both airlines now serve these cities and offer online connections between them. Competition and choice have been created.[46]

Passengers also may benefit where code-shared flights operate as "single carrier" service, *e.g.*, accrual of frequent flier miles and coordinated baggage handling. In this sense, lawmakers might reevaluate deregulation policy and consider an expansion of cabotage rights while the airlines themselves should focus on improving the customer experience in a straightforward way.

III. DISCUSSION

Liberalized international airline service means economic growth. Some aviation industry observers believe that opening international aviation markets may stimulate new and better air services, together with traffic and job growth. According to one study, the deregulation of transatlantic aviation markets between the United States and Great Britain alone would produce an estimated twenty-nine percent increase in traffic, generate 117,000 new jobs, and produce an increase of approximately $7.8 billion in GDP.[47] These forecasts are creditable given that the creation of the Single European Aviation Market which fused together that region's commercial airline operations in 1993 produced approximately 1.4 million new jobs and doubled the traffic growth rate.[48] Meanwhile, another study concluded that "air service liberalization can promote traffic growth, with an accompanying growth in non-aviation sectors . . . [as] the travel and tourism industry drives 12 percent to 15 percent of the world output of goods and services."[49]

Whatever the theoretical and actual economic gains facilitated by liberalized aviation operations, the major or "legacy" carriers have not responded well to deregulatory impulses, domestically or internationally. Service has suffered by almost every account.[50] Foreign airlines, such as

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46 Michael J. AuBuchon, *Testing the Limits of Federal Tolerance: Strategic Alliances in the Airline Industry*, 26 Transp. L.J. 219, 222 n.16 (1999).

47 INTERVISTAS, THE ECONOMIC IMPACT OF AIR SERVICE LIBERALIZATION, *supra* note 18, at ES-2. (The *INTERVISTAS* study was sponsored by such organizations as the Airports Council International, Boeing, General Electric, International Air Transport Association, and Pratt & Whitney.).

48 *Id.*

49 *Id.* at ES-5; *see also* STAKEHOLDER ANALYSIS OF OPEN SKIES, OWNERSHIP AND CONTROL, *supra* note 4, at 4; EUGENE ALFORD & RICHARD CHAMPLEY, U.S. DEP'T OF COMMERCE, THE IMPACT OF THE 2007 U.S.-E.U. OPEN SKIES TRANSPORT AGREEMENT 2-3 (2007), *available at* http://trade.gov/media/publications/pdf/openskies_2007.pdf.

50 *See*, *e.g.*, Joe Sharkey, *Passengers Rip Airlines Over Service in Zagat Survey*, SUN-SENTINEL, Nov. 20, 2005, at 2 ("'Would rather take a donkey,' one [passenger] says. 'Good service' translates to, 'We won't bother you if you don't bother us,' says another.").

Singapore Airlines or Emirates, regularly top surveys about airlines offering the best in-flight amenities and experience—not U.S. airlines.[51] Moreover, while prices are generally low, they are artificially so, as airlines maintain the narrative of cheap travel while "unbundling" services in the form of ancillary fees for a la carte items ranging from seat size to baggage checking.[52] Meanwhile, every major airline has sought bankruptcy protection (at least once). At a certain point, industry will have to confront the reality that business practices, not regulations, may be the culprit.[53]

A. Assessing Deregulation in the United States

An examination of U.S. airline deregulation offers an important analytical dimension to Open Skies policies and the stances taken by some U.S. airlines towards liberalized international operations. The quality of domestic commercial airline service has suffered under the policies established by the Airline Deregulation Act of 1978; it is a perpetual subject of spirited concern and debate among travelers and travel industry observers.[54] Although Congress intended to promote free market competition

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51 *See, e.g.*, World Airline Awards, *Top Ten Airlines 2014*, *available at* http://www.worldairlineawards.com/.

52 *See*, *e.g.*, Timothy M. Ravich, *National Airline Policy*, 23 U. MIAMI BUS. L. REV. 1, 35 (2014) ("Going forward, and in the absence of a serious and voluntary effort by the airline industry as a whole to differentiate and improve their customer service offerings beyond an artificially low price laden by ancillary fees, a national airline policy should delineate direct and not merely derivative customer service upgrades—otherwise, re-regulation may be in the offing.").

53 *See*, *e.g.*, Jens Flottau, *Accept Reality*, AVIATION WEEK & SPACE TECH., Feb. 16–Mar. 1, 2015, at 19 ("It is time for the incumbents to accept reality and concede that parts of the market now offer a superior produce at competitive prices.").

54 Airline Deregulation Act of 1978, Pub L. No. 95-504, § 102(7), (10), 92 Stat. 1705, 1706-07 (codified as amended at 49 U.S.C. §§ 1301-1552 (1982)). The scholarship debating the merits of airline deregulation is extensive. *See, e.g.*, Melvin A. Brenner, *Airline Deregulation—A Case Study in Public Policy Failure*, 16 TRANSP. L.J. 179 (1988); KENNETH BUTTON & ROGER STOUGH, AIR TRANSPORT NETWORKS: THEORY AND POLICY IMPLICATIONS (2000); PAUL STEPHEN DEMPSEY & ANDREW R. GOETZ, AIRLINE DEREGULATION AND LAISSEZ-FAIRE MYTHOLOGY (1992); Laurence E. Gesell & Martin T. Farris, *Airline Deregulation: An Evaluation of Goals and Objectives*, 21 TRANSP. L.J. 105 (1992); Andrew R. Goetz & Paul Stephen Dempsey, *Airline Deregulation Ten Years After: Something Foul in the Air*, 54 J. AIR L. & COM. 927 (1989); Richard D. Gritta, *Profitability and Risk in Air Transport: A Case for Deregulation*, 7 TRANSP. L.J. 197 (1975); WILLIAM A. JORDAN, AIRLINE REGULATION IN AMERICA: EFFECTS AND IMPERFECTIONS (Johns Hopkins Press 1970); Alfred E. Kahn, *Airline Deregulation—A Mixed Bag, But a Clear Success Nevertheless*, 16 TRANSP. L.J. 229 (1988); Alfred E. Kahn, *Deregulation: Looking Backward and Looking Forward*, 7 YALE J. ON REG. 325 (1990); Theodore P. Harris, *The Disaster of Deregulation*, 20 TRANSP. L.J. 87 (1991); Michael E. Levine, *Why Weren't the Airlines Reregulated?*, 23 YALE J. ON REG. 269 (2006); Michael E. Levine, *Revisionism Revised? Airline Deregulation and the Public Interest*, 44 LAW & CONTEMP. PROBS. 179 (1981); Kevin P. Mitchell, *The U.S. Airline Industry Fate*, 15 KNOWLEDGE, TECH. & POL'Y 3 (2002); Thomas G. Moore, *U.S. Airline Deregulation: Its Effects on Passengers, Capital and Labor*, 29 J.L. & ECON. 1 (1986); Edward A. Morash, *Airline Deregulation: Another Look*, 50 J. AIR L. & COM. 253 (1985); C. Vincent Olson & John M. Trapani, III, *Who Has Benefited from Regulation of the Airline Industry?*, 24 J.L. & ECON. 75 (1981); Rose M. Rubin & Justin N. Joy, *Where are the Airlines Headed? Implications of Airline Industry Structure*

and encourage new carriers to readily enter contestable air transportation markets, some of the undesirable anticompetitive dynamics that typified the airline industry under the governance of the Civil Aeronautics Board from 1938 to 1978 are present in today's commercial aviation marketplace.[55]

Competition that flourished in the early period of deregulation has diminished significantly in the last three decades, prompting some members of Congress to recognize that "[m]ost of us would not have voted to deregulate if we thought it would mean a deterioration to only three carriers."[56] In fact, just ten years after implementation of the Deregulation Act, Alfred Kahn, a Cornell economist revered as the father of airline deregulation, observed that

> [j]ust as one of the most pleasant surprises of the early deregulation experience was the large-scale entry of new, highly competitive carriers, so probably the most unpleasant one has been the reversal of that trend—the departures of almost all of them, the reconcentration of the industry both nationally and at the major hubs, the diminishing disciplinary effectiveness of potential entry by totally new firms, and the increased likelihood, in consequence, of monopolistic exploitation.[57]

Indeed, in 1986 alone, eighteen national carriers became eight. Over time, well-known carriers such as Air California, Air Florida, Braniff, Eastern, Pan Am, and National Airlines ceased to exist. Several mergers occurred, including Northwest and Republic, TWA and Ozark, USAir and Piedmont, and Delta and Western. The first-generation of so-called "low-cost carriers" like People Express and New York Air were consumed by conglomerate holding companies, including Texas Air.[58] Over seventy percent of

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and Change for Consumers, 39 J. CONSUMER AFF. 215 (2005); Symposium, *The Impact of Government Regulation on Air Transportation*, 9 AKRON L. REV. 629 (1976); GEORGE WILLIAMS, AIRLINE COMPETITION: DEREGULATION'S MIXED LEGACY (2002); GEORGE WILLIAMS, THE AIRLINE INDUSTRY AND THE IMPACT OF DEREGULATION (1993).

55 From 1938 to 1978, Congress regulated airline economics through the Civil Aeronautics Board (CAB), which protected an oligopoly of air carriers and restricted market entry in almost the same way that Interstate Commerce Committee protected railroad cartels in the late 1800s. Civil Aeronautics Act of 1938, Pub. L. No. 75-706, 52 Stat. 917 (1938). *See generally* Frederick A. Ballard, *Federal Regulation of Aviation*, 60 HARV. L. REV. 1235 (1947); Herbert D. Kelleher, *Deregulation and the Troglodytes—How the Airlines Met Adam Smith*, 50 J. AIR L. & COM. 299, 304 (1985); SAMUEL B. RICHMOND, REGULATION AND COMPETITION IN AIR TRANSPORTATION (Columbia Univ. Press 1961); Howard C. Westwood & Alexander E. Bennett, *A Footnote to the Legislative History of the Civil Aeronautics Act of 1938 and Afterword*, 42 NOTRE DAME L. REV. 309, 311 (1967).

56 Janet L. Fix, *Picture of Airline Deregulation Not as Pretty as It Was Meant to Be*, DETROIT FREE PRESS, Feb. 28, 2001, at 26 (quoting Representative Jim Oberstar (D-Minn.)).

57 Alfred E. Kahn, *Surprises of Airline Deregulation*, 78 AM. ECON. REV. 316, 318 (1988).

58 *See generally*, Paul Stephen Dempsey, *Antitrust Law and Policy in Transportation: Monopoly Is the Name of the Game*, 21 GA. L. REV. 505, 514 (1987); L. Milton Glisson, *Is U.S. Domestic Airline Competition on a Flight to Oblivion?*, 58 TRANSP. PRAC. J. 217, 218 (1991); Robert L. Thornton, *Airlines and Agents: Conflict and the Public Welfare*, 52 J. AIR L. & COM. 371, 396 (1986) (concluding "[i]f [the

commercial airline traffic concentrated at the nations' twenty-eight largest facilities, where dominant carriers operate with limited competition,[59] *e.g.*, American (formerly USAir) at Charlotte, or Delta at Atlanta and Detroit.[60] Meanwhile, airline passengers fume over the poor state of airline service and repeatedly call for implementation of an Airline Passengers' Bill of Rights.[61]

The modern domestic airline industry is not consistent with the core theory of deregulation of perfect market contestability. Instead, mergers and consolidation, dominance and near-monoplization of hub-and-spoke systems, complex fare structures, frequent flyer programs, predation, manipulation of travel agents and computerized reservation systems, firm strategies centered around acquisition and maintenance of slots and gates, and new entrant casualties, are the norm.[62] Three airline bankruptcies—Skybus, Aloha, and ATA—in the span of one week in 2008 also underscored the fragility of the U.S. airline industry.[63] After thirty years of airline deregulation policy, low prices alone are touted as sufficient justification for airline deregulation. Justice Stephen Breyer, who served as an aide to the late Senator Edward Kennedy in helping to pass the Airline Deregulation Act of 1978, wrote:

> What does the [airline] industry's history tell us? Was this effort worthwhile? Certainly it shows that every major reform brings about new, sometimes unforeseen, problems. No one foresaw the industry's spectacular growth, with the number of air passengers increasing from 207.5 million in 1974 to 721.1 million [in 2010]. As a result, no one foresaw the extent to which new bottlenecks would develop: a flight-choked Northeast corridor, overcrowded airports, delays, and terrorist

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DOT] fail[s] to act soon, the number of effective competitors in the airline industry may fall below the point from which deconcentration is possible without a major crisis").

59 *See e.g.*, Laurence Zuckerman, *Preserving Hub Networks Is the Carriers' Motivation*, N.Y. TIMES, Nov. 20, 2001, at C1*; see also* Steven A. Morrison & Clifford Winston, *The Remaining Role for Government Policy in the Deregulated Airline Industry*, *in* DEREGULATION OF NETWORK INDUSTRIES: WHAT'S NEXT 1, 5 (Sam Peltzman et al., eds., 2000).

60 In April 2008, Delta and Northwest agreed to and sought Congressional approval of an "end-to-end" merger that would form the world's largest airline. *E.g.*, Adrian Schofield, *Critical Mass*, AVIATION WEEK. & SPACE TECH., Apr. 21, 2008, at 24 ("[B]ut even consolidation of this magnitude may not streamline the U.S. industry enough to snap it out of a downward spiral.").

61 Timothy M. Ravich, *Re-Regulation and Airline Passengers' Rights*, 67 J. AIR L. & COM. 935 (2002); Daniel H. Rosenthal, Notes, *Legal Turbulence: The Court's Misconstrual of the Airline Deregulation Act's Preemption Clause and the Effect on Passengers' Rights*, 51 DUKE L.J. 1857 (2002).

62 Bettina M. Whyte & Michael B. Cox, *Airline Industry Restructuring: From Stuck in the Mud to Flying High*, 16-JUN. AM. BANKR. INST. J. 24, 25 (1997) ("Since 1978, airline deregulation in the United States has been characterized by periods of over-capacity, bankruptcy, price discounting, fuel shortages, labor strife, government intervention, as well as the free market consequences of management mistakes.").

63 *E.g.*, Andrew Compart, *Free Fall*, AVIATION WEEK. & SPACE TECH., Apr. 14, 2008, at 57 ("Fuel, a troubled economy and tight credit markets have left airlines with a much smaller margin for error, and the rapid succession of bankruptcies highlights just how fragile the industry is.").

> risks consequently making air travel increasingly difficult. Nor did anyone foresee the extent to which change might unfairly harm workers in the industry.
>
> Still, fares have come down. Airline revenue per passenger mile has declined from an inflation-adjusted 33.3 cents in 1974, to 13 cents in the first half of 2010. In 1974 the cheapest round-trip New York-Los Angeles flight (in inflation-adjusted dollars) that regulators would allow: $1,442. Today one can fly that same route for $268. That is why the number of travelers has gone way up.
>
> So we sit in crowded planes, munch potato chips, flare up when the loudspeaker announces yet another flight delay. But how many now will vote to go back to the "good old days" of paying high, regulated prices for better service? Even among business travelers, who wants to pay "full fare for the briefcase?"[64]

Nevertheless, strained balance sheets, together with the poor state of airline customer service in the deregulated area, suggest that an infusion of foreign capital and service may improve the quality and experience of domestic passengers.[65]

B. Cabotage: Foreign Carriers, Domestic Routes

Stimulating cabotage rights as a supplement to Open Skies and in place of existing bilateral and multilateral agreement may stimulate competition in today's saturated domestic airline marketplace. Cabotage—an admiralty term—refers to the ability of a carrier to transport passengers, mail, or cargo between ports within a foreign country market.[66] In aviation, for example,

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[64] Stephen G. Breyer, *Airline Deregulation, Revisited*, BLOOMBERG BUSINESSWEEK (Jan. 20, 2011), http://www.bloomberg.com/bw/stories/2011-01-20/airline-deregulation-revisitedbusinessweek-business-news-stock-market-and-financial-advice.

[65] *E.g.*, Z. Joseph Gertler, *Nationality of Airlines: A Hidden Force in the International Air Regulation Equation*, 48 J. AIR L. & COM. 51, 58 (1982). Several smaller market countries that required infusions of capital, including El Salvador, resisted the nationalistic operation and control requirements of Bermuda I. *E.g.*, Marc L.J. Dierikx, *Bermuda Bias: Substantial Ownership and Effective Control 45 Years On*, 16 AIR L. 118, 120 (1991).

[66] BLACK'S LAW DICTIONARY 194 (7th ed. 1999). "*Cabotage* meant originally navigation and trade along the same stretch of coast between the parts thereof, such coast belonging to the same State." *Id.*; *see also* Douglas R. Lewis, Note, *Air Cabotage: Historical and Modern-Day Perspectives*, 45 J. AIR L. & COM. 1059 (1980); *see, e.g.*, Kirsten Böhmann, *The Ownership and Control Requirement in U.S. and European Union Air Law and U.S. Maritime Law—Policy; Consideration; Comparison*, 66 J. AIR L. & COM. 689, 690 n. 3 (2001) (noting that "[c]abotage is commonly defined as carriage of passengers and goods between two points within the territory of the same nation for compensation or hire"); Eli A. Friedman, Comment, *Airline Antitrust: Getting Past the Oligopoly Problem*, 9 U. MIAMI BUS. L. REV. 121, 143 (2001) (contending that "[t]he only way that a competitive, growing market can take hold with a considerable, long-term effect on price and service is if domestic and foreign airlines are able to individually establish competing hub and spoke systems on a domestic and international level, while in

British Airways would enjoy cabotage rights in the United States if it were permitted to offer service from Miami, Florida to Albany, New York without any connection to Great Britain. Similarly, a United States carrier would have cabotage rights in Italy if it could fly passengers, mail or cargo from Milan to Rome, without any connection to the United States. Dating back to the 1920s, however, Congress has protected domestic airlines from competition by prohibiting cabotage by foreign carriers within the United States, and cabotage is not otherwise available to United States carriers abroad.[67]

International law restricts cabotage rights, likewise. Article VII of the Chicago Convention expressly restricts cabotage. This limitation is predicated upon the concept of national sovereignty, whereby any signatory to the Chicago Convention has the right to withhold cabotage rights to any other single state:

> Each contracting State shall have the right to refuse permission to the aircraft of other contracting States to take on in its territory passengers, mail and cargo carried for remuneration or hire and destined for another point within its territory. Each contracting State undertakes not to enter into any arrangements, which specifically grant any such privilege on an exclusive basis to any other State or an airline of any other State, and not to obtain any such exclusive privilege from any other State.[68]

While interpretation of the word "specifically" and the phrase "an exclusive basis" is a subject of debate, the United States has viewed cabotage rights as a matter of "sovereign, unilateral judgment," and determined that conferring cabotage rights to one nation does not require cabotage rights to all nations.[69] Consequently, few circumstances exist for cabotage rights in the United States.

The International Air Transportation Act of 1979 offers some hope in this regard, as it allows limited cabotage rights, namely the right of foreign carriers to fly within the United States where an "unusual circumstances"

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compliance with the antitrust laws"); W.M. Sheehan, Comment, *Air Cabotage and the Chicago Convention*, 63 HARV. L. REV. 1157 (1950).

67 S. REP. NO. 1661, at 2 (1938)*; see also* Jonathan B. Wilson, Note, *The Lessons of Airline Deregulation and the Challenge of Foreign Ownership of U.S. Air Carriers*, 24 GEO. WASH. J. INT'L L. & ECON. 103, 111-12 (1990).

68 Chicago Convention, *supra* note 23, at art. 7. The Paris Convention of 1919, which was the first multinational convention on aviation, expanded the concept of maritime cabotage to the aviation industry. Convention Relating to the Regulation of the Aerial Navigation, Oct. 13, 1979, 11 L.N.T.S. 173 (1919). *See* F. Allen Bliss, Note, *Rethinking Restrictions on Cabotage: Moving to Free Trade in Passenger Aviation*, 17 SUFFOLK TRANSNAT'L L. REV. 382, 384 n.9 (1994).

69 Lewis, *supra* note 66, at 1063-64*; see also* Z. Joseph Gertler, *Towards a New, Rational and Fair Exchange of Opportunities for Airlines*, *in* EEC AIR TRANSPORT POLICY AND REGULATION AND THEIR IMPLICATIONS FOR NORTH AMERICA 199, 202-03 (Peter P.C. Haanappel et al. eds., 1990); Kass, *supra* note 40, at 152-53.

exist.[70] In this context, DOT

> may . . . to the extent it finds that such action is required in the public interest, exempt any foreign air carrier for a period not to exceed 30 days . . . to the extent necessary to authorize a foreign air carrier to carry passengers, cargo, or mail in interstate or overseas air transportation in certain markets if [it] . . . finds that because of an emergency created by unusual circumstances not arising in the normal course of business, traffic in such markets cannot be accommodated by air carriers . . . .[71]

DOT exceptions under the Air Transportation Competition Act are quite rare, however.[72]

In light of qualitative service deficiencies by many domestic carriers, perhaps the time has come for the enactment of laws that allow non-U.S. air carriers to serve domestic routes, a move that may inject needed capital and competition into the deregulated marketplace. Cabotage rights also may make sense given the way in which the airline market has been developing:

> Domestic markets could be left to low-cost carriers [such as JetBlue, Southwest, Frontier, and Allegiant]. International service would become the province of large multinational entities. The European fear that such an entity would be dominated by the U.S. mega-carriers is growing less likely given the financial weakness of U.S. carriers and the fact that the U.S. market is expected to recover more slowly than the rest of the world in terms of passenger and cargo traffic. Historically, U.S. carriers were thought to gain power from the fact that they brought with them a large domestic network, but this too is becoming less important as the domestic market shifts towards low-cost carriers.[73]

All this said, the events of September 11, 2001 raise a number of potential issues, including national security, that militate against liberalized cabotage rights.[74] Moreover, labor generally opposes cabotage, characterizing such rights as non-negotiable rights that "could destroy the ability of some U.S. airlines to compete and cause them to be replaced by foreign air carriers on both international and domestic routes [and] raise serious questions of safety and security in the minds of lawmakers who are

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70 International Air Transportation Competition Act of 1979, 49 U.S.C. § 1386 (1992).

71 *Id.*

72 For example, the United States Department of Transportation denied Lineas Aereas Del Caribe, S.A. the right to carry 90 cattle between Florida and Puerto Rico. DOT Order 86-8-37 (Aug. 15, 1986).

73 RHOADES, *supra* note 13, at 186.

74 Cavinato, *supra* note 36, at 350 ("Rethinking and retooling an almost century-old restriction, whose original justifications are either irrelevant or adequately addressable, is necessary if the U.S. airlines are to regain their leadership role in the global aviation."); *see, e.g.*, Timothy M. Ravich, *Is Airline Passenger Profiling Necessary?*, 62 U. MIAMI L. REV. 1 (2007).

concerned with protecting the traveling public."[75]

Also, with respect to transatlantic aviation, cabotage may be a non-starter given the disparity between the U.S. marketplace and everywhere else. That is, access to ownership of a U.S. domestic carrier is not equivalent to any reciprocal right to own and operate a European carrier. Simply, "[a]ccess to the huge American passenger aviation market through indirect cabotage is such a bonanza . . . that even open access to landing slots and flight routes to Europe are paltry rewards in comparison."[76] Indeed, at the Chicago Convention of 1944, the United States essentially offered a global free market for airlines if nations could agree to recognize the "five freedoms." That offer was resisted as national security interests trumped free-market impulses. Indeed,

> in late 1944 the United States was on the verge of being in position to monopolize the international airline industry at war's end. It would take little more than a change of paint and uniforms to transform the U.S. military airlift fleet into civil airlines having a greater capacity than all of the other nations on earth could hope to muster for many years.[77]

C. Reversing Open Skies? The Gulf Carrier Threat

In 1999, the United States reached an Open Skies deal with the United Arab Emirates, home to Emirates Airline and Eithad Airways. Two years later, in 2001, Qatar and the United States reached a similar accord. Since that time, the trio of state-owned Persian Airlines—Emirates, Eithad, and Qatar—have expanded rapidly, using hubs in Abu Dhabi and Doha to cut into the market share of U.S. carriers on choice international routes.[78] In fact, the customer experience on the Persian carriers—including wide-body planes, low fares, and in-flight amenities—is so attractive that passengers traveling from the United States to Asia will book their flights with a stop-over in Dubai rather than take nonstop service offered by U.S. carriers.

Recent scholarship has examined how Gulf carrier competition has affected U.S. carriers' traffic volumes and fare levels in international route markets. While consumer welfare has been enhanced, legacy carriers in the United States and Europe are threatened:

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75 Thomas D. Grant, *Foreign Takeovers of United States Airlines: Free Trade Process in the Airline Industry*, 31 HARV. J. ON LEGIS. 63, 114, 133 n.236 (1993) (referencing AFL-CIO Executive Council, Foreign Control of U.S. Aviation Industry, Bal Harbour, Florida (Feb. 22, 1991)).

76 Grant, *supra* note 75, at 114 n.153 (1993) (referencing AFL-CIO Executive Council, Foreign Control of U.S. Aviation Industry, Bal Harbour, Florida (Feb. 22, 1991)).

77 HAMILTON, *supra* note 26, at 16.

78 *See generally* Ruwantissa Abeyratne, *Civil Aviation in the United Arab Emirates—Some Legal and Commercial Perspectives*, 73 J. AIR L. & COM. 3, 15 n.11 (2008).

> First, Gulf carrier competition directly impacts route markets connecting the U.S. to the Middle East, such as the Washington Dulles to Dubai route, served by both Emirates and United Airlines. *Moreover there is a secondary effect since Gulf carriers transport passengers through their Middle East hubs to beyond markets (i.e., sixth freedom traffic), thus impacting affects U.S. carrier operations to cities in Africa, Asia, Australia, and Europe. This secondary effect is significant since the majority of the Gulf carriers' passengers connect to beyond markets.*
>
> [Second,] the empirical results suggest that . . . a 1% growth in total Gulf carrier traffic to or from the U.S. is associated with a less than 0.1% drop in U.S. carriers' international passenger traffic and a less than 0.1% decrease in air fares. From a consumer perspective, the latter is, of course, a desirable outcome of increased competition in international aviation markets. U.S. carriers, however, are likely worse off following Gulf carrier entry.[79]

American and European carriers have reacted to these circumstances more aggressively—by resorting to political and legal process as much or more than making improvements to customer service.

In December 2014, Air France-KLM and Lufthansa Group wrote the European Commission to criticize "the absence of a level playing field regarding the access of certain government-supported third-country carriers to the European Aviation Market . . . if the development is allowed to continue, both the economic and strategic role of European aviation will be permanently impaired."[80] According to one assessment:

> The European airline CEOs want a 'proposal for a revised and efficient defense instrument safeguarding fair competition in the European aviation market vis-à-vis third-country carriers.' They also are asking for strict enforcement of ownership and control regulations and are proposing an international dispute settlement mechanism for conflicts over fair competition. In essence, the European carriers are demanding the right for Europe to withhold traffic rights from Gulf carriers they believe care government-subsidized.[81]

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79 Martin Dresner et al., *The Impact of Gulf Carrier Competition on U.S. Airlines*, *available at* https://www.aeaweb.org/aea/2015conference/program/retrieve.php?pdfid=409 (emphasis added).

80 *See* Madhu Unnikrishnan & Jens Flottau, *Backing Up*, AVIATION WEEK & SPACE TECH., Feb–Mar. 2015, at 40.

81 *Id.* (Noting that the views shared by the CEOs of Europe's largest carriers are not shared by all: "In fact, powerful players are actually in favor of supporting the Gulf airlines[, which] are hugely important customers for Airbus and Boeing, which have a keen interest in the airline being able to continue their path. And non-hub airports, particularly in Europe, see the three Gulf carriers as their only opportunity to attract long-haul air service and grow passenger numbers as European legacy airlines focus on their own hubs.").

Airlines in the United States have asserted similar arguments designed to roll back or reverse Open Skies agreements with the UAE and Qatar. In January 2015, American Airlines Group, Inc., United Continental Holdings, Inc., and Delta Air Lines, Inc. distributed a fifty-five page briefing paper detailing how the state-owned Gulf carriers were dumping capacity on routes between the U.S. and the United Arab Emirates and Qatar and otherwise distorting global trade with the help of huge government subsidies.[82] The clash has been bitter and sheds light on important aeropolitical and protectionist impulses that shadow modern international airline operations.[83] *A fortiori*, they expose a disturbing pattern by some U.S. airlines to devalue trade principles when the consequences are painful:

> The U.S. carriers want capacity between Gulf States and the U.S. to be reduced to local demand. Yet it should be up to any company to determine whether it wants to pursue connecting traffic . . . . And then there is this issue of "fair competition" that European and U.S. majors argue should link traffic rights to the absence of subsidies. While it is true that access to enormous financial support from the state . . . can distort competition, other factors can do the same harm . . . . Chapter 11 bankruptcy protection in the U.S. is an incredibly powerful tool for airlines (and other companies) to reduce structural costs [and] it is a tool not available to carriers outside the U.S.
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> ***
>
> Reversing open skies is clearly not the answer, and one can only hope that governments stand firm.[84]

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82 *See* Partnership for Open & Fair Skies, *Fueled by Massive Government Subsidies, State-Owned Qatar Airways, Etihad Airways and Emirates are Aiming to Dominate Global Aviation by Exploiting Open Skies Policy* (2015), http://www.openandfairskies.com/. *See generally* Mike Tretheway & Robert Andriulatis, *What Do We Mean by a Level Playing Field* (2015), *available at* http://www.internationaltransportforum.org/jtrc/DiscussionPapers/DP201506.pdf.

83 Susan Carey, *U.S. Airlines Clash Over Rivals from Persian Gulf*, WALL ST. J., Feb. 24, 2015, at B1. The sharp rhetoric surrounding the charge of unfair competition has been amplified by unfortunate remarks about the terrorism of September 11th and terrorism originating in the Middle East to rebut the criticism leveled by several organizations, including Airports Council International North America, U.S. Travel Association, and Business Travel Coalition, that the three complaining U.S. airlines by pointing out that such carriers benefitted from government subsidies after the September 11 attacks. *Id.* at B2 (Reporting the comments of Delta CEO Richard Anderson: "It's a great irony to have the UAE from the Arabian Peninsula talk about that given the fact that our industry was really shocked by the terrorism of 9/11, which came from terrorists from the Arabian Peninsula;" Qatar Airway's CEO said that Mr. Anderson "should be ashamed to bring the issue of terrorism to try to cover his inefficiency in running an airline."); *see also 27 Questions the Big 3 Need to Answer in Seeking Government Protection from Foreign Airlines*, BUS. TRAVEL COALITION (Mar. 5, 2015), http://businesstravelcoalition.com/cgi-bin/dada/mail.cgi/archive/influencers/20150305162148/.

84 Flottau, *supra* note 53, at 19.

IV. CONCLUSION

While not going as far as providing cabotage freedoms, Open Skies policies have been enormously successful and a welcome departure from piecemeal bilateral agreements and antiquated ownership and control rules. Low-cost carrier JetBlue, itself a successful product of airline deregulation, could not have achieved success in serving the Caribbean and Latin America but for Open Skies, for example.[85] And as JetBlue's president noted: "[s]imilar to the domestic aviation landscape after deregulation, international services, traffic, and economic activity have correspondingly grown since the United States began pursuing its open-skies policies." Free trade policies in the aviation industry have indeed eliminated "government interference in commercial decisions on routes, capacity, and pricing."[86] Measured against this success, the protectionist position now taken by certain U.S. airlines in connection with robust competition from carriers in the Middle East is troubling.

The practice by some airlines of favoring deregulation when it comes to their customer service obligations while crying for government action when it comes to their own welfare is not pro- or anti-regulation, but simply self-serving.[87] Perhaps the comments of one aviation industry observer in this context are unsurprising given certain carriers' vacillation between Open Skies and deregulation, on the one hand, and restricted Open Skies and re-regulation, on the other hand: "[i]t was, after all, the airlines themselves who invited the government to impose regulation in order to save them from competition, and only United among the then trunk carriers supported deregulation in 1978."[88]

For now, the position taken by five of the largest airlines in the world is nothing short of pure protectionism that is out of step with today's global marketplace. Indeed,

> [T]hey want their governments to protect them from new market entrants that are beginning to dominate one part of the long-haul market—traffic to, from and between Southeast Asia, the Middle East, Europe, Africa and Australia. Gulf carriers are also growing their presence in North America, based upon long-established open skies deals for which the U.S. side has been pushing.

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85 Unnikrishnan & Flottau, *supra* note 80, at 41.

86 *Id.*

87 Ravich, *National Airline Policy*, *supra* note 53, at 1.

88 Michele McDonald, *Trouble on the Hill; Congress Considers Possible Airline Regulations*, AIR TRANSP. WORLD, June 1, 2001, at 95.

> The demands by United, American, Delta, Lufthansa and Air France-KLM are in pursuit of their interests only and have nothing to do with the principles of free competition.[89]

[89] Flottau, *supra* note 53, at 19. As this article went to publication, the U.S. Department of Justice raised concerns about demands by U.S. airlines that the federal government limit flights of three Middle Eastern rivals, warning of higher fares and fewer choices for airline passengers. *See generally* Jeffrey Dastin, *U.S. Airlines hit Justice Department Hurdle in Gulf Trade Dispute*, REUTERS (Oct. 12, 2015), http://www.reuters.com/article/us-usa-airlines-gulf-exclusive-idUSKCN0S621P20151012#KdzWoejhxS4X3rbI.97; *see also* Emirates Airlines, Emirates' Response to Claims Raised about State-Owned Airline in Qatar and the United Arab Emirates (June 29, 2015), http://content.emirates.com/downloads/ek/pdfs/openskies_rebuttal/EK_Response_Main.pdf.