

THE APRIL 2007 U.S.–EU “OPEN SKIES” AGREEMENT: A DREAM OF LIBERALIZATION DEFERRED

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Abstract: The April 2007 Open Skies Agreement between the United States and the European Union has been hailed as a landmark in aviation deregulation. Under the terms of the agreement, any U.S. or EU airline may fly between any city in the United States and Europe—a major departure from the byzantine restrictions that previously characterized transatlantic air travel. Nevertheless, in several key respects, the treaty stops short of full deregulation. This Note assesses the probable impact of the Open Skies Agreement and explores why EU negotiators were willing to compromise on several of their core objectives.

INTRODUCTION

On April 30, 2007, the first aviation agreement between the United States and the European Union (EU) was signed in Washington.¹ Hailed by European Commission Vice-President Jacques Barrot as a “centerpiece for today’s reinvigorated transatlantic relationship,”² the U.S.–EU Open Skies Agreement (Open Skies Agreement)³ marks a clear departure from the web of tangled bilateral treaties that have governed transatlantic aviation since World War II.⁴ For the first time in the history of modern aviation, any U.S. or EU airline will be permitted to fly between any city in the United States and Europe.⁵

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¹ 2007 O.J. (L 134) 4–41 [hereinafter Open Skies Agreement].

² EU News Release, Open Skies: Jacques Barrot in Washington to Sign Historic Aviation Deal at the EU-US Transatlantic Summit (Apr. 30, 2007), <http://www.eurunion.org/News/press/2007/2007044.htm> (last visited Nov. 13, 2007).

³ See generally John Bruton, *The Sky’s the Limit for Trans-Atlantic Air Travelers*, SEATTLE TIMES, June 23, 2006 (noting that in Europe, the treaty is generally referred to as “Open Aviation Agreement”).

⁴ See Robert M. Hardaway, *Of Cabbages and Cabotage: The Case for Opening up the U.S. Airline Industry to International Competition*, 34 TRANSP. L. J. 1, 2–12 (2007).

⁵ Open Skies Agreement, *supra* note 1, art. 2(a); see also *EU Backing for “Open Skies” Deal*, BBC NEWS, Mar. 22, 2007, <http://news.bbc.co.uk/2/hi/business/6477969.stm> (“any

Yet, just how significant is this departure in treaty law for airline passengers? Michael O'Leary, chief executive officer of the European low-cost airline Ryanair, has gone so far as to proclaim the advent of fifteen dollar transatlantic tickets by 2010.⁶ Others have heralded the Open Skies Agreement as a first step towards opening the U.S. domestic aviation market to foreign competition.⁷ In reality, however, unless the European Union manages to wrest more concessions from the United States in the next round of Open Skies treaty negotiations, such prognostications are likely to go unmet.⁸

This Note begins in Part I by providing historical context on the development of aviation regulatory law, offering a comparative view of trends in the United States and Europe before examining the transatlantic regulatory order. Part II discusses the negotiations leading up to finalization of the Open Skies Agreement and examines the most significant provisions of the treaty, namely those related to cabotage—the right to transport passengers within a given country—and foreign investment control. Part III analyzes the key concessions made to seal the Open Skies Agreement. Finally, Part IV concludes by arguing that passengers on both sides of the Atlantic would have benefited had the European Union realized more of its strategic objectives. Major issues for consideration during the second round of open skies negotiations, which is scheduled to commence by the end of 2008, are highlighted in closing.

I. BACKGROUND

A. *The United States*

For most of the Twentieth Century, the U.S. government smothered airline competition under a thick blanket of legislative regulation.⁹ In the early years of U.S. commercial aviation, foreign invest-

EU-based airline will be allowed to fly from any city within the EU to any city in the US, and vice versa").

⁶ Nicola Clark, *A Flight of Fantasy: €10 to Cross the Atlantic*, INT'L HERALD TRIB., Apr. 14, 2006, at 11.

⁷ *U.S. Airline Group Backs "Open Skies" Potential*, REUTERS, Mar. 22, 2007, <http://www.reuters.com/article/tnBasicIndustries-SP/idUSN2235098020070322> (noting some European carriers hope Open Skies Agreement will eventually lead to "full liberalization of the U.S. domestic air market").

⁸ See Dan Bilefsky & Nicola Clark, *EU Backs U.S. Deal on Atlantic Air Routes: "Open Skies" Accord Should Lower Fares but Draws Criticism*, INT'L HERALD TRIB., Mar. 23, 2007, at 1.

⁹ See Hardaway, *supra* note 4, at 2–12; see also Christopher McBay, *Airline Deregulation Deserves Another Shot: How Foreign Investment Restrictions and Subsidies Actually Hurt the Airline Industry*, 72 J. AIR L. & COM. 173, 175–80 (2007).

ment in U.S. airlines was heavily restricted.¹⁰ The Air Commerce Act of 1926 (ACA) mandated that U.S. citizens own at least fifty-one percent of any aircraft registered in the United States.¹¹ Moreover, the ACA also stipulated that the board of directors of any U.S. airline be comprised of at least two-thirds U.S. citizens.¹² Anxious to safeguard U.S. neutrality in the aftermath of World War I, Congress sought to block foreign control of U.S. aircraft that might conceivably be co-opted into armed service abroad.¹³

The Civil Aeronautics Act of 1938 (CAA) went considerably further in restricting competition.¹⁴ As an additional bar to foreign investment, the CAA required that U.S. citizens own or control at least seventy-five percent of the voting rights in any U.S. carrier.¹⁵ Beyond fixing prices for air transportation in a manner akin to the way in which the Interstate Commerce Commission fixed prices for U.S. railroads,¹⁶ the CAA also established “virtually absolute barriers to entry” for new competitors.¹⁷ Although new entrants into the U.S. market could theoretically obtain permission to fly, in reality the Civil Aeronautics Board established under the CAA did not allow a single new competitor to enter the market between 1938 and 1975.¹⁸ During that period, the U.S. aviation industry grew by a staggering 23,800 percent, even as the five largest carriers operating in the United States enjoyed a *de facto* oligopoly.¹⁹

By the 1970s, pressure for deregulation had reached a breaking point.²⁰ During the 1975 Kennedy hearings on aviation deregulation, industry experts testified that regulated airfares were between forty and one-hundred percent higher than they would be without government price fixing, with a resultant cost to consumers of roughly

¹⁰ See Hardaway, *supra* note 4, at 2–12.

¹¹ McBay, *supra* note 9, at 175.

¹² *Id.*

¹³ *Id.*

¹⁴ See Hardaway, *supra* note 4, at 4.

¹⁵ McBay, *supra* note 9, at 176.

¹⁶ See Hardaway, *supra* note 4, at 3 (noting how ICC obligated government to do “dirty work of fixing prices” in much same way that CAA would obligate government with regard to aviation industry).

¹⁷ See *id.* at 4.

¹⁸ Paul Stephen Dempsey, *The Rise and Fall of the Civil Aeronautics Board—Opening Wide the Floodgates of Entry*, 11 TRANSP. L.J. 91, 115 (1979).

¹⁹ Hardaway, *supra* note 4, at 4 (citing STEPHEN BREYER, REGULATION AND ITS REFORM 206 (1982)).

²⁰ See *id.* at 3–4; see also McBay, *supra* note 9, at 178.

\$3.5 billion annually in excess fares.²¹ Congress responded with the Airline Deregulation Act of 1978 (ADA), which eliminated government price fixing and opened the aviation industry to new entrants.²² Over the next few decades, a host of new airlines entered the U.S. market and fares fell considerably.²³ Nevertheless, foreign investors were still barred from taking any more than twenty-five percent of voting stock in a U.S. carrier.²⁴

B. Europe

In 1957, the European Economic Community (EEC)²⁵ was established under the Treaty of Rome.²⁶ Although the Treaty of Rome granted the EEC the authority to create “the framework of a common transport policy”²⁷ within Europe, it limited this authority to rail, road, and inland waterway transport.²⁸ The Treaty of Rome permitted pan-European regulation of maritime and air transport, but only in the event of a unanimous vote by the Council of Europe (Council).²⁹

Despite the language of the Treaty of Rome, throughout the 1970s and 1980s a number of European Court of Justice (ECJ) decisions lent support to the notion that the EEC had some power to regulate maritime and air transport within its member states, even without universal Council approval.³⁰ By 1987, the question had been made moot by the Single European Act, which formally amended the Treaty of Rome to change the Council’s voting system from a unanimous system to a qualified majority system.³¹

²¹ Hardaway, *supra* note 4, at 4.

²² *See id.* at 4.

²³ *See id.* at 5.

²⁴ McBay, *supra* note 9, at 176.

²⁵ The European Economic Community was formed in 1952. In 1992, the term “Economic” was removed by the Maastricht Treaty, which made the newly-termed European Communities one of three pillars of the European Union, along with Common Foreign and Security Policy and Police and Judicial Cooperation in Criminal Matters.

²⁶ Treaty Establishing the European Community, Nov. 10, 1997, O.J. (C 340) 3 (1997) [hereinafter Treaty of Rome].

²⁷ *Id.*

²⁸ *See* Jacob A. Warden, “Open Skies” at a Crossroads: How the United States and European Union Should Use the ECJ Transport Cases to Reconstruct the Transatlantic Aviation Regime, NW. J. INT’L L. & BUS. 227, 232 (2003).

²⁹ *Id.*

³⁰ *See id.* at 232–33 (citing Commission v. French Republic (*French Seaman*) (1974) (holding that general principles of Treaty of Rome could be applied to maritime travel); *Ministere Public v. Lucas Asjes (Nouvelles Frontieres)* (1986) (holding same to be true with regard to air travel)).

³¹ *Id.* at 233.

Aviation deregulation followed between 1987 and 1992 with enactment of the “three packages,” a series of regulatory reforms.³² Although the “first package” had little real impact, the “second package” increased the power of airlines to set fares and allowed for expanded travel within Europe.³³ By 1997, when the provisions of the “third package” had come into force, all EU Member States enjoyed full cabotage rights to fly routes within other EU countries.³⁴ As in the United States, a number of new low-cost airlines emerged to challenge the dominance of established legacy carriers.³⁵

C. *Transatlantic Aviation*

As the U.S. Third Army rumbled toward Nazi Germany in the closing months of World War II, trade negotiators from the Allied powers set about laying the foundation for a postwar transatlantic aviation order in Chicago.³⁶ Affirming the central precept of the 1919 Paris Aeronautical Convention—that states maintain sovereignty over their airspace—the 1944 Chicago Convention established the principle that although nations are free to bar foreign carriers from commercial access to their airports, they may not restrict foreign carriers from entering their national airspace.³⁷ As the strongest commercial aviation power, the United States pushed for further liberalization in air travel, although it was unable to achieve a broader multilateral consensus.³⁸

Instead, scores of bilateral agreements between the United States and other nations were enacted following the Chicago Convention.³⁹ The most significant of these early agreements was the 1946 “Bermuda I” agreement between the United States and Great Britain, which

³² *Id.*; see also Monica E. Antezana, *The European Union Internet Copyright Directive as Even More Than It Envisions*, 26 B.C. INT’L & COMP. L. REV. 415 (2003) (illustrating another effort at EU integration).

³³ Warden, *supra* note 28, at 233–34.

³⁴ *Id.* at 234.

³⁵ Among the most successful early low-cost European carriers were Selios Haji-Ioannou’s UK-based Easyjet and Ireland-based Ryanair. See *Ryanair Profits Take Off*, BBC NEWS, August 9, 2002, <http://news.bbc.co.uk/2/low/business/2175319.stm>.

³⁶ See E. Rebecca Kreis, *A Comparative Analysis of the Aviation Network Within the European Community and the Ad-Hoc Network Between the United States and Central America*, 24 TRANSP. L.J. 303, 305–11 (1997) (illustrating origins of early European aviation treaties during first decades of twentieth century).

³⁷ *Id.* at 307–09 (noting that Convention on International Civil Aviation signed at Chicago in 1944 established nine so-called “freedoms of the air”).

³⁸ See *id.* at 308.

³⁹ *Id.* at 311.

served as a model for hundreds of subsequent bilateral aviation agreements around the world.⁴⁰ Under Bermuda I and its progeny, fares and tariffs were set by an international body, the International Air Transport Association.⁴¹ Consequently, throughout much of the postwar period, airlines traveling international routes competed not on price but on “capacity and service frequency,” with the result that international air travel remained beyond the means of most U.S. and European travelers.⁴²

In 1977, the Bermuda I agreement was amended as “Bermuda II.”⁴³ Under Bermuda II, only two U.S. airlines—American Airlines and United Airlines—were permitted to service London’s Heathrow Airport.⁴⁴ In addition, non-stop service from Great Britain to America was restricted to a fixed number of “gateway cities” in the United States.⁴⁵ The agreement represented a successful effort by British protectionists to eliminate the supposed “excess capacity” of U.S. carriers traveling to Britain.⁴⁶ Although the U.S. government pushed strenuously for looser regulation, the British controlled access to Heathrow, Europe’s busiest airport, and thus exercised considerable leverage.⁴⁷

Despite the highly restrictive nature of Bermuda II, transatlantic aviation became increasingly open following passage of the U.S. Airline Deregulation Act of 1978.⁴⁸ Airline alliances⁴⁹ and code sharing agreements enabled U.S. carriers to circumvent restrictions on air travel within Europe by partnering with EU carriers.⁵⁰ Moreover, bilateral open skies agreements between the United States and individual European countries began to proliferate, enabling transatlantic service to new U.S. cities.⁵¹

⁴⁰ See Warden, *supra* note 28, at 230.

⁴¹ *Id.* at 230–31.

⁴² *Id.* at 231.

⁴³ Kreis, *supra* note 36, at 311–12.

⁴⁴ See *US Airways Group v. British Airways*, 989 F.Supp. 482, 485 (S.D.N.Y. 1997) (describing “nature” of U.S.-U.K. airline industry as of late-1990s).

⁴⁵ AIR SERVICE AGREEMENTS BETWEEN THE UNITED KINGDOM AND THE UNITED STATES, SELECT COMM. ON ENV’T., TRANSP. AND REGULATORY AFFAIRS, EIGHTEENTH REPORT (2000), <http://www.parliament.the-stationery-office.co.uk/pa/cm199900/cmselect/cmenvtra/532/53206.htm#note38>.

⁴⁶ Kreis, *supra* note 36, at 311–12.

⁴⁷ See *id.* at 312.

⁴⁸ See *id.* at 312–14.

⁴⁹ See Hardaway, *supra* note 4, at 24 (discussing Oneworld, SkyTeam and Star Alliance).

⁵⁰ See Kreis, *supra* note 36, at 312–14.

⁵¹ Warden, *supra* note 28, at 236–37.

The first of these bilateral agreements, a 1992 treaty between the United States and the Netherlands, permitted unrestricted landing rights within each signatory's territory.⁵² Prior to the agreement, flights between the United States and the Netherlands had been limited in number and restricted to certain airports.⁵³ As a result of the agreement, Dutch carrier KLM found itself at a significant competitive advantage as compared to other European carriers.⁵⁴ KLM not only enjoyed the flexibility to chart routes anywhere in the United States to meet market demand; as a further incentive to the Dutch government, the U.S. Department of Transportation also exempted KLM from U.S. antitrust restrictions in its alliance with Northwest Airlines.⁵⁵ Other bilateral Open Skies agreements soon followed between the United States and various members of the European Union.⁵⁶ By 2007, bilateral agreements had been concluded with sixteen EU Member States.⁵⁷

Although the bilateral Open Skies agreements negotiated between the United States and individual European countries may have helped to liberalize transatlantic aviation, they nevertheless fell flat in the face of European integration.⁵⁸ The ECJ signified its disapproval in a series of consolidated rulings in 2002.⁵⁹ Noting that bilateral Open Skies agreements between the United States and the European Union contradicted the spirit of the “three packages” reforms, the ECJ held that EU Member States entering into such agreements “infringed the rules on the division of powers between the Community and the Member States.”⁶⁰ The court extended its condemnation to the Bermuda II

⁵² Agis Salpukas, *U.S. and Dutch Agree on a Pact to Aid Airlines*, N.Y. TIMES, Sept. 5, 1992, at A1.

⁵³ *See id.*

⁵⁴ Warden, *supra* note 28, at 236–37.

⁵⁵ Kreis, *supra* note 36, at 314 (noting immunity as method of enticing countries to enter into open-skies agreements).

⁵⁶ In addition to its open skies agreement with the Netherlands, the United States negotiated similar agreements with Austria, Belgium, Denmark, Finland, Germany, Luxembourg and Sweden. *See* ALFORD & CHAMPLEY, THE IMPACT OF THE 2007 U.S.–EU OPEN SKIES AIR TRANSPORT AGREEMENT, INT’L TRADE ADMIN. OCCASIONAL PAPER NO. 07–001 2 (2007), http://trade.gov/media/Publications/pdf/openskies_2007.pdf.

⁵⁷ *Id.*

⁵⁸ *See* Press Release, Europa, Open Sky Agreements: Commission Welcomes European Court of Justice ruling (Nov. 5, 2002), <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/02/1609&format=HTML&aged=0&language=EN&guiLanguage=en> [hereinafter Commission Welcomes ECJ Ruling] (last visited Nov. 7, 2007).

⁵⁹ Cases C-466/98-C-469/98, C-471/98-C-472/98, C-475/98-C-476/98, *Comm’n v. UK, DK, S, FIN, B, L, AUS, G*, (31 Jan. 2002).

⁶⁰ *Id.* at Concluding Observations.

agreement.⁶¹ Yet even if the ECJ was unambiguous in its criticism of bilateral aviation treaties negotiated by individual EU Member States, it did not rule out a broader Open Skies agreement between the United States and the European Union as a whole.⁶² On the contrary, the ECJ explicitly endorsed the notion.⁶³ As European Commission Vice President for Transport and Energy Loyola de Palacio commented, “it is clear from the Court’s ruling that we will all have to work together in Europe to identify and pursue our objectives jointly.”⁶⁴

I. DISCUSSION

It took five years for the United States and the European Union to emerge from the rubble of the ECJ’s 2002 rulings.⁶⁵ Finally, in the spring of 2007, the United States and the European Union concluded a comprehensive Open Skies treaty.⁶⁶ The U.S.–EU Open Skies Agreement, signed on April 30, 2007 in conjunction with a U.S.–EU summit in Washington, took effect on March 30, 2008.⁶⁷ Although it touches on many aspects of commercial aviation, from code sharing to security, the most contentious provisions of the treaty relate to cabotage and foreign airline ownership rights.⁶⁸

Article 3 of the Open Skies Agreement deals with cabotage.⁶⁹ Under Article 3(c) (i), U.S. carriers have the right to fly from Europe to the United States via “intermediate points” in any EU Member State.⁷⁰ For example, American Airlines may fly from Berlin to Amsterdam before continuing on to Boston.⁷¹ Likewise, under Article 3(c) (ii), EU carriers are free to fly from any point in the European Union to any point in the United States without necessarily touching their “home country.”⁷² A British Airways flight, in other words, may

⁶¹ *Id.*

⁶² Commission Welcomes ECJ Ruling, *supra* note 58.

⁶³ *Id.*

⁶⁴ *Id.*

⁶⁵ Press Release, U.S. Mission to the EU, U.S., EU Agree to Reduce Regulatory and Trade Barriers (Apr. 30, 2007), available at <http://useu.usmission.gov/Article.asp?ID=74174DC1-203C-48EA-87F6-C58557DEB56A> [hereinafter U.S., EU Agree to Reduce Barriers] (last visited Nov. 1, 2007).

⁶⁶ Open Skies Agreement, *supra* note 1.

⁶⁷ *Id.*

⁶⁸ See Don Phillips, “Open Skies” Reality Still Proves Elusive, INT’L HERALD TRIB., June 5, 2006, at 10 (discussing cabotage and airline ownership rights).

⁶⁹ Open Skies Agreement, *supra* note 1, art. 3.

⁷⁰ *Id.* art. 3(c) (i).

⁷¹ See *id.*

⁷² *Id.* art. 3(c) (ii).

fly from Madrid to Chicago without landing in London.⁷³ Notably, however, Article 3 does not authorize EU carriers to fly between points in the United States before returning to Europe.⁷⁴ Thus, Virgin Atlantic may not operate flights within the United States, although it may take a limited equity stake in U.S. carriers.⁷⁵

Ownership rights under the Open Skies Agreement are discussed in Article 6 of the treaty and elaborated in Annex 4.⁷⁶ U.S. investors are guaranteed the right to participate as minority shareholders in any EU carrier, provided that the carrier is majority-owned and controlled by EU Member States or nationals.⁷⁷ EU investors may hold up to 49.9 percent of total equity in a U.S. carrier, but are limited to twenty-five percent voting equity.⁷⁸ On a case-by-case basis, ownership by EU nationals of fifty percent or more of the total equity of a U.S. carrier is permitted under the agreement, although such ownership “shall not be presumed to constitute control of that airline.”⁷⁹ Notwithstanding the other provisions in Annex 4, the European Community reserves the right to limit investment by U.S. nationals in the voting equity of EU carriers “to a level equivalent to that allowed by the United States for foreign nations in U.S. airlines.”⁸⁰

The issue of foreign ownership rights is not technically linked to the concept of cabotage, but European negotiators insisted from the beginning that the European Union would not implement an open skies agreement unless the United States relaxed its “regulatory grip on airline investment.”⁸¹ While foreign investors may participate passively on the corporate boards of U.S. carriers, they have nonetheless been historically restricted under the CAA from taking an active role in most operational decisions.⁸² As a prerequisite to any Open Skies agreement, European negotiators demanded that their U.S. counter-

⁷³ See *id.*

⁷⁴ *Id.* art. 3.

⁷⁵ See John Hughes, *Branson, Rejected or Not, May Win in U.S. Airline Bid*, BLOOMBERG, Dec. 5, 2006, <http://quote.bloomberg.com/apps/news?pid=20601109&sid=aQs7zO5NbyQw> (noting that this is essentially what UK-based Virgin Atlantic has done by putting up twenty-five percent of the initial \$177 million investment to start Virgin America).

⁷⁶ Open Skies Agreement, *supra* note 1, art. 6 & annex 4.

⁷⁷ *Id.* art. 2.

⁷⁸ *Id.* annex 4, art. 1(a).

⁷⁹ *Id.* annex 4, art. 1(b).

⁸⁰ *Id.* annex 4, art. 3.

⁸¹ Phillips, *supra* note 68, at 10.

⁸² *Id.*

parts agree to loosen their restrictions on foreign investment.⁸³ Early on, at least, it seemed this might happen.⁸⁴

U.S. and EU negotiators reached a preliminary Open Skies agreement in November 2005.⁸⁵ The terms of the tentative agreement granted each U.S. and EU carrier the right “to fly between every city in the EU and every city in the United States,” and “to operate without restrictions on routes or capacity.”⁸⁶ EU Commission support for the agreement was predicated upon U.S. congressional approval of an administrative rule proposed by the Department of Transportation (DOT) to allow foreign investors a greater role in the management of U.S. carriers.⁸⁷ Under the proposed DOT rule, foreign investors from Open Skies partner nations would be free to make “operational decisions” on issues such as rates and routes, although they would still be prohibited from having control over “security, safety and defense issues related to the airlines.”⁸⁸ According to the DOT, the proposed rule would reinterpret, rather than replace, the ownership requirements of the CAA.⁸⁹

After a preliminary Open Skies agreement was negotiated in November 2005, the proposed DOT rule was submitted to Congress for comments.⁹⁰ Officials from the DOT testified at length in favor of the proposal.⁹¹ Nevertheless, this did little to allay congressional concerns

⁸³ *See id.*

⁸⁴ *See* Press Release, U.S. Mission to the EU, Airline Foreign Control Rule Might Be Delayed, U.S. Official Says (Apr. 25, 2006), <http://useu.usmission.gov/Article.asp?ID=CE1729F4-EBB4-451F-ABA7-163A2766A059> [hereinafter Foreign Control Rule Might be Delayed] (last visited Nov. 1, 2007) (discussing preliminary November 2005 open skies agreement).

⁸⁵ *Id.*

⁸⁶ *Id.*

⁸⁷ *See* Press Release, U.S. Mission to the EU, U.S., EU Reach Long-Sought Accord To Liberalize Air Traffic U.S. Mission to the European Union (Mar. 2, 2007), <http://useu.usmission.gov/Article.asp?ID=E315F141-7EFD-4CBB-B249-F7F5FED60445> [hereinafter U.S., EU Reach Long-Sought Accord] (last visited Nov. 1, 2007).

⁸⁸ Press Release, Andrzej Zwanecki, U.S. Mission to the EU, U.S. Remains Committed to Airline Deal with Europe, Officials Say (Aug. 17, 2006), <http://useu.usmission.gov/Article.asp?ID=CDF512F7-24CA-47EC-A090-D4B050658B16> [hereinafter U.S. Remains Committed to Airline Deal] (last visited Nov. 1, 2007).

⁸⁹ *Id.*

⁹⁰ Press Release, Andrzej Zwanecki, U.S. Mission to the EU, House Approves Moratorium on Airline Foreign Ownership Rule (Mar. 17, 2006), <http://useu.usmission.gov/Article.asp?ID=A2DF41A5-F981-4C72-9636-E02FEF1C3C3A> [hereinafter House Approves Moratorium] (last visited Nov. 1, 2007).

⁹¹ Press Release, Andrzej Zwanecki, U.S. Mission to the EU, U.S. Officials Urge Congress Not to Block Airline Investment Rule (Feb. 8, 2006), <http://useu.usmission.gov/Article.asp?>

related to labor and aviation security.⁹² Additional concerns regarding the breadth of DOT's power to issue rules reinterpreting established law were also raised.⁹³ By the end of 2006, the proposed rule had been withdrawn from consideration.⁹⁴ "It is necessary now," said lead U.S. negotiator John Byerly, "on both sides of the Atlantic to accept the reality that a major change in U.S. rules governing control of U.S. airlines is simply not in the cards."⁹⁵

One might infer from the great efforts taken by the White House to implement the proposed DOT rule that no Open Skies agreement with the European Union would be feasible without it.⁹⁶ On the contrary, once the DOT proposal was withdrawn from Congress, a U.S. delegation rushed to Brussels in January 2007 "to discuss possible solutions to the stalemate."⁹⁷ Less than two months later, U.S. and EU negotiators reported a breakthrough—without any change to U.S. aviation foreign investment law.⁹⁸ How was the seemingly intractable gap between the U.S. and EU positions closed? What concessions were made by each side, and just how meaningful were they? Finally, what implications do these concessions have for passengers on both sides of the Atlantic?

III. ANALYSIS

On its face, there is little question that the U.S.–EU Open Skies Agreement favors the United States.⁹⁹ In terms of cabotage rights, the agreement is clearly lopsided.¹⁰⁰ Although it grants U.S. carriers the right to fly routes within Europe, the Open Skies Agreement does not

ID=EAF3C76D-580D-49D8-906E-133A1F8245EC [hereinafter U.S. Officials Urge Congress] (last visited Nov. 1, 2007).

⁹² See *id.*

⁹³ See *id.* (noting "members of the House Transportation and Infrastructure Subcommittee on Aviation uniformly questioned not only the rule itself but even [DOT's] authority to issue it").

⁹⁴ Foreign Control Rule Might be Delayed, *supra* note 84.

⁹⁵ Press Release, Andrzej Zwanecki, U.S. Mission to the EU, U.S., EU to Look at Options to Finalize Open Skies Deal (Jan. 17, 2007), <http://useu.usmission.gov/Article.asp?ID=A3BCB68A-DC58-4745-A0E3-F968A435228A> [hereinafter U.S., EU to Look at Options] (last visited Nov. 1, 2007).

⁹⁶ See *id.*

⁹⁷ *Id.*

⁹⁸ U.S., EU Reach Long-Sought Accord, *supra* note 87.

⁹⁹ See "Open Skies" Agreement Favors U.S., FORBES.COM, Mar. 27, 2007, http://www.forbes.com/business/2007/03/26/open-skies-airlines-biz-cx_0327oxford.html.

¹⁰⁰ See Open Skies Agreement, *supra* note 1, art. 3.

permit EU carriers the right to fly within the United States.¹⁰¹ In terms of foreign investment rights, the picture is murkier.¹⁰² U.S. and EU investors alike are proscribed from gaining “control” of each other’s carriers.¹⁰³ On the other hand, while U.S. nationals are limited to a minority stake in EU carriers, EU nationals may, on a case-by-case basis, take more than a fifty percent equity stake in U.S. carriers, provided that the investment is not interpreted as signifying control.¹⁰⁴ Given that the discretion to adjudicate on a case-by-case basis will presumably be vested in the DOT, it is unclear how real the impact of this provision will be.¹⁰⁵ Certainly, the provision is a far cry from the initial EU demands that engendered the DOT’s proposed rule on foreign management control.¹⁰⁶ The question thus arises: why were EU negotiators willing to accept such unbalanced terms on cabotage in exchange for what is arguably a negligible enhancement in foreign investment rights?

U.S. concessions undoubtedly played some role in bringing EU negotiators to the table.¹⁰⁷ When the U.S. delegation flew to Brussels in January 2007 following withdrawal of the DOT proposal, it reiterated a number of modest proposals, including one to open some forms of U.S. government-funded travel to EU carriers.¹⁰⁸ The U.S. delegation also reiterated Washington’s support for granting antitrust immunity to U.S. and EU carriers entering into airline alliances, even though the persuasive impact of such assurances was no doubt negligible because the United States already granted antitrust immunity to most of its bilateral Open Skies partners.¹⁰⁹ The U.S. delegation seems to have gained real ground when it shifted the dialogue on foreign investment rights from a focus on “control” to a focus on “ownership.”¹¹⁰ Even though the European Union had demanded broader

¹⁰¹ *Id.* art. 3(c)(i).

¹⁰² *See id.* art. 6 & annex 4.

¹⁰³ *Id.*

¹⁰⁴ *Id.*

¹⁰⁵ *See id.*

¹⁰⁶ *See* U.S., EU Reach Long-Sought Accord, *supra* note 87.

¹⁰⁷ *See id.*

¹⁰⁸ *See* David Jonas, *EU, US to Evaluate New Open Skies Deal*, TRANSNATIONAL, Mar. 7, 2007, <http://www.thetransnational.travel/news.php?cid=eu-us-open-skies.Mar-07.07> (noting that since no routes from Washington D.C. were actually included in proposal, British Airways Chairman Martin Broughton described such access rights as “miniscule concessions dressed up as significant breakthroughs”).

¹⁰⁹ *See* Kreis, *supra* note 36, at 314; *see also* Foreign Control Rule Might be Delayed, *supra* note 84.

¹¹⁰ *See* U.S., EU to Look at Options, *supra* note 95.

investment control from the start of negotiations, by January 2007 the U.S. delegation could point towards Congress's intractability as a way of arguing credibly that if the European Union wanted any sort of Open Skies agreement, it would have to retreat from its initial position.¹¹¹ Ultimately, the proposal to grant EU nationals greater than fifty percent ownership of U.S. carriers on an ad hoc basis—albeit without traditional majority shareholder control rights—appears to have tilted the balance.¹¹²

Broader considerations played a crucial role in motivating the European Union to finalize an open skies agreement with the United States.¹¹³ For one thing, EU negotiators viewed any potential Open Skies agreement with the United States as simply the first in a series of commercial aviation agreements.¹¹⁴ The language of the Open Skies Agreement reflects this understanding.¹¹⁵ Article 21 of the agreement explicitly calls for “second stage negotiations” and stipulates that negotiations must begin “not later than 60 days after provisional application” of the treaty.¹¹⁶ Among the “items of priority interest” identified for second stage negotiations are “further liberalisation of traffic rights” and “foreign investment opportunities.”¹¹⁷ Thus, in the second stage of negotiations following application of the Open Skies Agreement, EU cabotage rights within the United States, along with broader foreign investment control rights, will presumably be issues for discussion.¹¹⁸ Whether this will do anything to alter the current U.S. position, however, is another matter.¹¹⁹

Perhaps the single greatest motivating factor for EU negotiators was the perceived economic value of a transatlantic Open Skies agreement.¹²⁰ In March 2007, the EU Commission issued a press statement predicting that if approved, the Open Skies Agreement

¹¹¹ *See id.*

¹¹² *See id.* (noting that following the U.S. delegation's January 2007 trip to Brussels, one observer suggested that, “ownership is an area where the U.S. administration can do something to allay European concerns”).

¹¹³ *See* Press Release, Andrzej Zwanecki, U.S. Mission to the EU, United States Hails Aviation Pact with EU as Win for both Sides (Mar. 22, 2007), <http://useu.usmission.gov/Article.asp?ID=61FC06B4-E9C4-4AEE-B906-CA6A8BA34D1C> [hereinafter United States Hails Aviation Pact] (last visited Nov. 7, 2007).

¹¹⁴ *Id.*

¹¹⁵ Open Skies Agreement, *supra* note 1, art. 21.

¹¹⁶ *Id.*

¹¹⁷ *Id.* art. 21(2).

¹¹⁸ *See id.*

¹¹⁹ *See id.*

¹²⁰ U.S., EU Reach Long-Sought Accord, *supra* note 87.

would “provide for a thirty-four percent increase in trans-Atlantic air passenger traffic, [generating] up to \$16 billion in economic benefits over five years and [creating] a total of 80,000 new jobs on the two sides of the Atlantic.”¹²¹ Another study prepared for the EU Commission by the consultancy Booz Allen Hamilton put the economic benefits of a transatlantic Open Skies agreement between \$9 billion and \$17 billion over five years.¹²² Such perceptions seem to have been genuinely held by the European Union and the U.S. Department of State.¹²³ Faced with such potentially immense benefits, EU negotiators were hardly in a position to walk away from negotiations in January 2007, even after the U.S. Congress repudiated the compromise they had wrested from U.S. negotiators.¹²⁴

Ironically, the 2002 ECJ rulings concerning bilateral Open Skies agreements with EU Member States may have also undermined the European Union’s bargaining position.¹²⁵ In its 2002 rulings, the ECJ held that bilateral aviation agreements with individual EU Member States would no longer be permitted, yet the existing agreements were not immediately nullified.¹²⁶ During negotiations leading up to completion of the Open Skies Agreement, the EU Commission “made clear that it would ask the [ECJ] to require EU members to terminate their bilateral agreements with the United States” in the event that no agreement was reached.¹²⁷ Undoubtedly, the EU Commission took this tack in the hope of wresting further concessions from U.S. negotiators.¹²⁸ Nevertheless, the prospect of unraveling the entire transatlantic aviation regulatory order effectively acted as a double-edged sword, serving, if anything, to underscore the necessity of reaching an Open Skies agreement, whatever the cost.¹²⁹

¹²¹ *Id.*

¹²² See THE ECONOMIC IMPACTS OF AN OPEN AVIATION AREA BETWEEN THE EU AND THE US (EXECUTIVE SUMMARY), BOOZ ALLEN HAMILTON, at iii (2007), http://ec.europa.eu/transport/air_portal/international/pillars/global_partners/doc/us/eu_us_study_executive_summary.pdf.

¹²³ See ALFORD & CHAMPLEY, *supra* note 56, at 3 (noting that “[t]he EU estimates are reportedly drawn from a Brattle Group study concluded in 2002” and that “State Department representatives have indicated they broadly agree with those figures.”).

¹²⁴ *See id.*

¹²⁵ *See* U.S., EU to Look at Options, *supra* note 95.

¹²⁶ Press Release, U.S. Dept. of State, Open Skies Partners (July 2, 2007), <http://www.state.gov/e/eeb/rls/othr/2007/22281.htm> (commenting that bilateral open skies treaties between United States and EU member states remain “in force” until application of U.S.–EU Open Skies Agreement).

¹²⁷ U.S., EU to Look at Options, *supra* note 95.

¹²⁸ *See id.*

¹²⁹ *See id.*

Moving forward, the European Union will face real challenges as it attempts to address some of the second stage objectives enumerated in Article 21.¹³⁰ It will not, however, be without negotiating power.¹³¹ Congress invoked the talisman of aviation security to condemn the DOT's proposed rule on foreign management rights.¹³² There is no reason to believe that it would not do so again if the White House entertained the notion of granting broader management control rights to EU investors, let alone cabotage rights for foreign air travel within the United States.¹³³ Labor groups, in particular, would be adamantly opposed.¹³⁴ Nevertheless, EU negotiators have two powerful levers to pull as a way of drawing their U.S. counterparts to the table.¹³⁵ First, the Open Skies Agreement contains an exit provision that permits EU Member States to suspend cabotage rights for U.S. carriers operating within Europe if there is no consensus on a second stage accord by 2010.¹³⁶ Second, the critical issue of airport slot allocations remains unsettled.¹³⁷ Currently, slots are distributed to airlines on a legacy basis that favors carriers which have been flying the same routes for years.¹³⁸ If the slot system were altered, however, to permit greater U.S. carrier access to Heathrow, for example, a powerful incentive could be created to wrest concessions from the United States.¹³⁹

CONCLUSION

The U.S.–EU Open Skies Agreement will undoubtedly benefit passengers on both sides of the Atlantic. New routes will link hitherto unconnected cities in the United States and Europe. Artificial restrictions on flight routing will be lifted, enabling carriers to chart their routes in greater accord with market forces. U.S. carriers will soon be permitted to compete within Europe, offering European travelers more options for air travel. Whether the economic benefits it yields

¹³⁰ See Open Skies Agreement, *supra* note 1, art. 21.

¹³¹ See *id.*

¹³² House Approves Moratorium, *supra* note 90.

¹³³ See *id.*

¹³⁴ See *id.*

¹³⁵ See U.S., EU Reach Long-Sought Accord, *supra* note 87; see also United States Hails Aviation Pact, *supra* note 113.

¹³⁶ United States Hails Aviation Pact, *supra* note 113.

¹³⁷ U.S., EU Reach Long-Sought Accord, *supra* note 87.

¹³⁸ See *Slot trading under Open Skies—the implications for allocating capacity*, EURACTIV.COM, Aug. 30, 2007, <http://www.euractiv.com/en/transport/slots-trading-open-skies-implications-allocating-capacity/article-166329>.

¹³⁹ See *id.*

over the next five years are closer to \$9 billion or \$17 billion, the Open Skies Agreement will certainly usher in a more competitive transatlantic aviation order. Indeed, the only clear losers from the treaty are the carriers that benefited from the former protectionist regime, most notably British Airways and Virgin Atlantic. It is no coincidence that the greatest resistance to implementing the Open Skies Agreement came from Westminster.¹⁴⁰

And yet, despite its promise, the Open Skies Agreement is hardly an optimal accord. There is little question that EU investors would have benefited from a more assertive EU negotiating stance, particularly with regard to foreign management control rights. At the same time, the benefits to passengers—ironically, to U.S. passengers, in particular—would also have been considerable. With the notable exception of certain low-cost carriers, the troubled U.S. aviation industry has been cash-strapped for years and heavily reliant on government bailouts. Had EU negotiators enjoyed more success in securing traditional management control rights for EU investors, greater EU investment in U.S. carriers might have been encouraged, thereby fostering a more financially solvent industry, with potential benefits to passengers, as well as to stockholders. Spurred by a desire to grow the market share of their carriers, foreign investors might well have used their control to offer passengers new routes, better service and more modern aircraft.

Regardless of how far the current Open Skies Agreement evolves, transatlantic travel is certain to change. At least in the near term, the domestic U.S. aviation market is unlikely to benefit from a dramatic infusion of foreign capital. The North Atlantic market, however, appears destined to grow and to become ever more competitive. Ryanair and its progeny will probably never fly between JFK and Heathrow, but over the next several years they could feasibly launch flights between Hartford, Connecticut, or Providence, Rhode Island and some of the satellite airports ringing London. Budget airlines flying out of mid-market airports would not draw many corporate travelers from the main urban hubs, but they might well carve out a niche for themselves amongst leisure travelers and small business owners. In the end, this could potentially drive down the price of economy-class tickets on more established carriers. It is ironic that the United States, a pioneer

¹⁴⁰ See *Q&A: Open Skies*, BBC News, Mar. 22, 2007, <http://news.bbc.co.uk/2/hi/business/6478651.stm> (noting that at Britain's insistence EU ministers pushed to have implementation of Open Skies Agreement delayed from October 2007 to March 2008).

in air travel liberalization, has taken such a resolutely protectionist position toward foreign ownership rights and domestic cabotage. At the same time, the United States may ultimately find the costs of intractability untenable.