

## **Special Topic—International Transportation Law**

### **Liberalizing Scheduled Air Transport Within the European Community: From the First Phase to the Second and Beyond**

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#### I. INTRODUCTION

During the founding years of the European Community,<sup>1</sup> the law and

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1. Although the European Community ("EC" or "Community") is often thought of as a single entity, there are three legally independent Communities: the European Coal and Steel Community ("ECSC"), the European Economic Community ("EEC"), and the European Atomic Energy Community "Euratom". See Treaty Instituting the European Coal and Steel Community, Apr. 18, 1951, 261 U.N.T.S. 140 (1957); Treaty Establishing the European Economic Community, Mar. 25, 1957, 298 U.N.T.S. 11 (1958) [hereinafter EEC Treaty or Treaty]; Treaty Establishing the European Atomic Energy Community, Mar. 25, 1957, 298 U.N.T.S. 167 (1958). The Merger Treaty of 1965 did not merge the three Communities as such: rather, the Treaty instituted a single Commission ("EC Commission" or "Commission") to replace the High Authority of the

policy of air transport was largely ignored.<sup>2</sup> It was not until the end of the 1970's that the First Memorandum of the EC Commission on Air Transport brought about a change to this situation.<sup>3</sup> This memorandum was the catalyst for the dialogue between the EC Commission, the EC Council, the European Parliament, and the Member States concerning the future development of civil aviation within the Community and beyond. The efforts were reinforced by the publication of the Second Memorandum of the EC Commission in 1984.<sup>4</sup>

As a result of two decisions rendered by the European Court of Justice in 1985<sup>5</sup> and 1986<sup>6</sup> and the impetus provided by the Single European Act,<sup>7</sup> there has been a considerable increase in legislative activity concerning air transport during the last few years.<sup>8</sup> The Commission has

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European Coal and Steel community and the Commissions of the European Economic Community and the European Atomic Energy Community. The Merger Treaty also established a single Council ("Council of Ministers" or "Council") to replace the separate councils of the three Communities. See Treaty Establishing a Single Council and a Single Commission of the European Communities, Apr. 8, 1965, 4 I.L.M. 776 (1965). For a general discussion of EC institutions, see T. HARTLEY, *THE FOUNDATIONS OF EUROPEAN COMMUNITY LAW* 8-87 (2d ed. 1988).

2. For a detailed explanation of the reasons, see J. BASEDOW, *WETTBEWERB AUF DEN VERKEHRSMÄRKTEN* 157-63 (1989).

3. See AIR TRANSPORT: A COMMUNITY APPROACH (Memorandum of the Commission), COM(79) 311 final (July 4, 1979), reprinted in BULL. EUR. COMM. SUPP. 5/79 [hereinafter First Memorandum].

4. See CIVIL AVIATION MEMORANDUM NO. 2—PROGRESS TOWARDS THE DEVELOPMENT OF COMMUNITY AIR TRANSPORT POLICY, Mar. 15, 1984, COM(84) 72 final, 27 O.J. EUR. COMM. (No. C 182) 1 (July 9, 1984) [hereinafter Second Memorandum].

5. European Parliament v. Council, Case 13/83, [1985] Sammlung der Rechtsprechung des Gerichtshofes (European Court of Justice Reports) [hereinafter Slg.] 1513.

6. Ministère Public v. Asjes et al., Cases 209-213/84, [1986] Slg. 1425 [hereinafter *Nouvelles Frontières* case].

7. Single European Act, Feb. 28, 1986, 30 O.J. EUR. COMM. (No. L 169) 1 (June 29, 1987) (effective July 1, 1987) [hereinafter SEA]. See also the Decision adopted by the Foreign Ministers on the Occasion of the Signing of the Single European Act, containing a series of implementing details, 19 BULL. EUR. COMM. 1986/2, at 115-16.

8. See Council Regulation (EEC) No. 3975/87 of 14 December 1987 laying down the procedure for the application of the rules on competition to undertakings in the air transport sector, 30 O.J. EUR. COMM. (No. L 374) 1 (Dec. 31, 1987); Council Regulation (EEC) No. 3976/87 of 14 December 1987 on the application of article 85(3) of the Treaty to certain categories of agreements and concerted practices in the air transport sector, 30 O.J. EUR. COMM. (No. L 374) 9 (Dec. 31, 1987); Council Directive 87/601/EEC of 14 December 1987 on fares for scheduled air services between Member States, 30 O.J. EUR. COMM. (No. L374) 12 (Dec. 31, 1987); Council Decision 87/602/EEC of 14 December 1987 on the sharing of passenger capacity between air carriers on scheduled air services between Member States and on access for air carriers to scheduled air-service routes between Member States. 30 O.J. EUR. COMM. (No. L 374) 19 (Dec. 31, 1987). See also Commission Regulation (EEC) No. 2671/88 of 26 July 1988 on the application of Article 85(3) of the Treaty to certain categories of agreements between undertakings, decisions of associations of undertakings and concerted practices concerning joint planning and coordination of capacity, sharing of revenue, and consultations on tariffs on scheduled air services and slot allocation at airports. 31 O.J. EUR. COMM. (No. L 239) 9 (Aug. 30, 1988); Commission Regulation (EEC) No. 2672/88 of 26 July 1988 on the application of Article 85(3) of the

proved itself in this respect, to be a major force behind the liberalization movement. The Council of Ministers only recently came to a decision concerning the important question of the Second Phase of the liberalization of scheduled air transport.<sup>9</sup> The pertinent regulations became effective on November 1, 1990, and they represent a major step towards entry into the Single European Market on January 1, 1993. The purpose of this article is to present and critically evaluate the current state of scheduled air transport deregulation within the EC. The analysis will focus primarily upon the legislative measures promulgated by the Council of Ministers concerning the Second Phase of air transport liberalization which were published in August 1990.

In order to evaluate the regulations enacted by the Council, it is necessary to throw some light on the general legal framework of international air transport. The article will then take a closer look at the pertinent provisions of the EEC Treaty. Finally, the historical process of the liberalization of air transport within the EC and the prospects for air transport deregulation will be analyzed.

## II. THE LEGAL FRAMEWORK OF WORLD AIR TRANSPORTATION

The present world air transport system is based upon the Convention on International Civil Aviation, commonly referred to as the Chicago Convention.<sup>10</sup>

### A. THE CHICAGO CONVENTION

The Chicago Convention was negotiated by 52 nations in 1944,

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Treaty to certain categories of agreements between undertakings relating to computer reservation systems for air transport services. 31 O.J. EUR. COMM. (No. L 239) 13 (Aug. 30, 1988); Commission Regulation (EEC) No. 2673/88 of 26 July 1988 on the application of Article 85(3) of the Treaty to certain categories of agreements between undertakings, decisions of associations of undertakings and concerted practices concerning ground handling services. 31 O.J. EUR. COMM. (No. L 239) 17 (Aug. 30, 1988). For a discussion of these Regulations, see Banowsky, *Cutting Drag and Increasing Life: How Well Will a More Competitive EEC Air Transport Industry Fly?*, 24 INT'L LAW. 179 (1990); Dempsey, *Aerial Dogfights Over Europe: The Liberalization of EEC Air Transport*, 53 J. AIR L. & COM. 615 (1988).

9. The "Second Phase" of the liberalization of scheduled air transport consists of the following three Regulations: Council Regulation (EEC) No. 2342/90 of 24 July 1990 on fares for scheduled air services. 33 O.J. EUR. COMM. (No. L 217) 1 (Aug. 11, 1990); Council Regulation (EEC) No. 2343/90 of 24 July 1990 on access for air carriers to intracommunity scheduled air-service routes and on the sharing of passenger capacity between air carriers on scheduled air services between Member States. 33 O.J. EUR. COMM. (No. L 217) 8 (Aug. 11, 1990); Council Regulation (EEC) No. 2344/90 of 24 July 1990 amending Council Regulation (EEC) No. 3976/87 on the application of Article 85(3) of the Treaty to certain categories of agreements and concerted practices in the air transport sector. 33 O.J. EUR. COMM. (No. L 217) 15 (Aug. 11, 1990).

10. Convention on International Civil Aviation, Dec. 7, 1944, 61 Stat. 1180. T.I.A.S. No. 1591, 15 U.N.T.S. 295 (1948) [hereinafter Chicago Convention].

shortly before the end of World War II when it became apparent that a new legal framework for world air transport would be necessary.<sup>11</sup> The Chicago Convention went into effect on April 4, 1947.<sup>12</sup> One of the basic principles of the Convention is that of national air sovereignty. According to this principle, every nation has complete and exclusive sovereignty over the airspace above its territory.<sup>13</sup> As a result, every nation has the right to decide upon the distribution of air transport rights to and from its territory on a case by case basis.

Initially, the parties to the Chicago Convention intended to establish a multilateral system of transport rights. Due to the uncompromising positions of the United States which took a very liberal view, and the United Kingdom which followed a protectionist approach, a comprehensive agreement could not be reached.<sup>14</sup> Agreement was only reached with respect to two of the eight "Freedoms of the Air."<sup>15</sup> The two freedoms agreed upon are commonly known as the "technical freedoms." The failure to achieve an all-encompassing multilateral agreement concerning air transport rights at the Chicago conference led, in the following years, to the system of bilateral agreements that still forms the legal basis of the current international air transport system.

### B. BILATERAL AGREEMENTS

Over the years, a tight international network of bilateral air transport agreements concerning scheduled air services has developed between

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11. See A. KARK, DIE LIBERALISIERUNG DER EUROPÄISCHEN ZIVILLUFTFAHRT UND DAS WETTBEWERB SRECHT DER EUROPÄISCHEN GEMEINSCHAFT 73 (1989).

12. See Chicago Convention, *supra* note 10, art. 91. For a list of countries that have signed the Chicago Convention, see S. ROSENFELD, THE REGULATION OF INTERNATIONAL COMMERCIAL AVIATION, Booklet 5, 52-54 (1984).

13. See Chicago Convention, *supra* note 10, art. 1.

14. For details, see A. KARK, *supra* note 11, at 73-75; M. DAUTZENBERG, DER BRITISCH/AMERIKANISCHE KARTELL-RECHTSSTREIT UM DIE IATA-FLUGTARIFE AUS DEM BLICKWINKEL DES PROTECTION OF TRADING INTERESTS ACT 70-72 (1987).

15. The First through the Fifth Freedoms are defined in article 1(1) of the International Air Transport Agreement, an appendix to the Chicago Convention, *supra* at 10. The Sixth through the Eighth Freedoms are combinations of the Third through the Fifth Freedoms. For a detailed discussion of the First through the Eighth Freedoms, see S. ROSENFELD, *supra* at 12, Booklet 3, at 3-6. The First through Fifth Freedoms of the Air read as follows:

First Freedom: The right to fly across the territory of a foreign country without landing,

Second Freedom: The right to land for non-commercial purposes (technical operations relating to the aircraft, the crew, refueling, etc.) in the territory of a foreign country,

Third Freedom: The right to fly from the country of registration to another country and put down, in the territory of the other country, passengers, freight, or mail taken aboard in the country of registration.

Fourth Freedom: The right to fly from a foreign country with passengers, cargo, or mail loaded in that foreign country, to the country of its registration.

Fifth Freedom: The right to transport passengers, mail, or cargo between another contracting state and a third country.

almost all countries of the world.<sup>16</sup> The agreement between the United States and the United Kingdom that was negotiated in Bermuda in early 1946 ("Bermuda I Agreement"), served as a model for the majority of such bilateral agreements.<sup>17</sup> The bilateral air transport agreements of the Federal Republic of Germany were, and still are, based upon the German Model Draft of a Bilateral Air Transport Agreement, which in turn is based upon the Bermuda I Agreement.<sup>18</sup> Almost all of the agreements based upon the Bermuda I Agreement contain the following provisions:

1. The distribution of air transport rights with respect to the First, Second, Third, and Fourth Freedoms.<sup>19</sup> In some bilateral agreements, the Fifth Freedom is also granted;<sup>20</sup>
2. The determination of particular flight routes;<sup>21</sup>
3. The number of air carriers permitted to make use of the transport rights mentioned above (single or multiple designation);<sup>22</sup>
4. Determination of capacity (size of aircraft and frequency of service);<sup>23</sup>
5. The tariff approval process, usually including a double approval clause.<sup>24</sup>

Bilateral air transport agreements based upon such provisions thus regulate market access, the number and scope of air transport rights, capacity, and tariffs. Almost all bilateral agreements considerably restricted competition between airlines well into the 1980's, and some of them continue to do so to this day.<sup>25</sup> Specifically, a number of significant aspects of market structure were excluded from the forces of competition. This is also true with respect to most bilateral air transport agreements between Member States of the EC.

### C. TARIFF AGREEMENTS

The network of bilateral air transport agreements has been supplemented by tariff agreements between airlines. These tariff agreements

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16. There are approximately 2,500 bilateral air transport agreements today. See also L. WEBER, *DIE ZIVILLUFTFAHRT IM EUROPÄISCHEN GEMEINSCHAFTSRECHT* 47 (1981).

17. See Bermuda Agreement, 60 Stat. 1499, 3 U.N.T.S. 253 [hereinafter Bermuda I]. The Bermuda I Agreement of 1946 was replaced, in 1977, by another bilateral agreement between the United States and the United Kingdom ("Bermuda II"). See 1 AIR LAW, ch. IV, at 30 (C. Shawcross & M. Beaumont eds., 4th ed. 1990).

18. See German Model Draft of a Bilateral Air Transport Agreement, reprinted in D. KLOSTER-HARZ, *DIE LUFTVERKEHRSABKOMMEN DER BUNDESREPUBLIK DEUTSCHLAND* Appendix I (1976) [hereinafter Model Agreement].

19. *Id.* art. 2(1)(c).

20. *Id.* art. 8(3).

21. *Id.* art. 2(2).

22. *Id.* art. 3(1).

23. *Id.* art. 8(4).

24. *Id.* art. 10(1).

25. See A. KARK, *supra* note 11, at 77-78.

were, and still are, negotiated within the International Air Transport Association ("IATA").<sup>26</sup> As a general rule, tariffs are set at IATA conferences and then approved by national governments.<sup>27</sup> Such tariff agreements are reinforced by both EC law and the laws of EC Member States.

### 1. EC LAW

Under article 85(3) of the EEC Treaty, tariff agreements may be exempt from European antitrust laws.<sup>28</sup> Article 85(3) of the EEC Treaty has been implemented by two EC Regulations.<sup>29</sup> Under these Regulations, tariff "consultations" between airlines are permitted to the extent that the various conditions of article 4 of Commission Regulation 2671/88 are met.<sup>30</sup> Most importantly, article 4(1)(e) of this Regulation requires that

26. For a general discussion of the functions of IATA, see W. SCHWENK, *HANDBUCH DES LUFTVERKEHRSRECHTS* 327-332 (1981); J. BRANCKER, *IATA AND WHAT IT DOES* (1977).

27. See generally Bermuda I, *supra* note 17, Annex II h.

28. See EEC Treaty, *supra* at 1, art. 85(3) reads as follows:

1. The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings, and concerted practices which may affect trade between Member states and which have as their object or effect the prevention restriction or distortion of competition within the common market, and in particular those which:

- (a) directly or indirectly fix purchase or selling prices or any other trading conditions;
- (b) limit or control production, markets, technical development, or investment;
- (c) share markets or sources of supply;
- (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
- (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which by their nature or according to commercial usage, have no connection with the subject of such contracts.

2. Any agreements or decisions prohibited pursuant to this Article shall be automatically void.

3. The provisions of paragraph 1 may, however, be declared inapplicable in the case of:

- (a) any agreement or category of agreements between undertakings;
  - (b) any decision or category of decisions by associations of undertakings;
  - (c) any concerted practice or category of concerted practices;
- which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not;

(a) impose on the undertakings concerted restrictions which are not indispensable to the attainment of these objectives;

(b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

29. See Council Regulation 3976/87 and Commission Regulation 2671/88, *supra* at 8.

30. See Commission Regulation 2761/88, *supra* note 8, art. 4 that reads, in its pertinent part, as follows:

1. The exemption concerning the holding of consultations on tariffs shall apply only if:

(a) the consultations are solely intended to prepare jointly tariff proposals covering scheduled air fares to be paid by members of the public directly to a participating air carrier or to its authorized agents for carriage as passengers with their accompanying baggage on a scheduled service and the conditions under which those fares apply, in application of Article 4 of Directive 87/601/EEC;

(b) the consultations only concern tariffs subject to approval by the aeronautical

tariff proposals resulting from such "consultations" not be binding.<sup>31</sup>

Until 1978, IATA member airlines were legally bound to participate in IATA tariff coordination conferences and to adopt tariffs that were negotiated at such conferences.<sup>32</sup> As a result of the 1978 "show cause order"<sup>33</sup> of the Civil Aeronautics Board ("CAB") of the United States, the IATA regulations were changed. Beginning in 1979, member airlines were no longer required to participate in, nor to adopt tariffs agreed upon by the IATA conferences. Because of the non-binding tariff setting process within IATA, the participation of European carriers is consistent with the two Regulations aforementioned.<sup>34</sup>

## 2. GERMAN LAW

Until December 31, 1989, tariff agreements among airlines were also exempt from Germany's antitrust laws. According to German law,<sup>35</sup> the Antitrust Statute did not apply to contracts of companies dealing with the transportation of persons or goods, if the tariffs for the transport services had to be approved by a state agency.<sup>36</sup> Under German law,<sup>37</sup> airline tariffs must be approved by the Federal Department of Transportation (*Bundesverkehrsministerium*).<sup>38</sup> Consequently, tariffs agreed upon at IATA conferences were exempt as a matter of law.

Effective January 1, 1990, however, this policy changed. Under the

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authorities of the Member States concerned, and do not extend to the capacity for which such tariffs are to be available;

(c) the tariffs which are subject [sic] of the consultations are applied by participating air carriers without discrimination on grounds of passengers' nationality or place of residence within the Community;

(d) participation in the consultations is voluntary and open to any air carrier who operates or has applied to operate on the route concerned;

(e) any draft tariff proposals which may result from the consultations are not binding on participants, that is to say, following the consultations the participants retain the rights to act independently, both in putting forward tariff proposals for approval independently of the other participants and in freely applying such tariffs after they have been approved;

(f) the consultations do not entail agreements on agents' remuneration or other elements of the tariffs discussed;

(g) in respect of each tariff which was the subject of the consultations, each participant informs the Commission without delay of its submission to the aeronautical authorities of the Member States concerned.

31. See *id.* art. 4(1)(e).

32. See M. DAUTENBERG, *supra* note 14, at 80.

33. For details of the "show cause order," see P. BARLOW, AVIATION ANTITRUST 21-23 (1988).

34. See *supra* note 29 and accompanying text.

35. See Antitrust Statute [*Gesetz gegen Wettbewerbsbeschränkungen*], Sept. 24, 1980, 1980 *Bundesgesetzblatt* [*German Official Gazette*] I 1761 [hereinafter "BGBl"].

36. See *id.* art. 99(1).

37. See Air Transport Statute [*Luftverkehrsgesetz*], Jan. 14, 1981, 1981 BGBl, I 61.

38. See *id.* art. 21(1).

new law,<sup>39</sup> contracts of airlines concerning interstate transportation with the EC are no longer subject to Germany's Antitrust Statute.<sup>40</sup> The German legislature has thereby taken account of the fact that EC law takes priority over the laws of the Member States when air transportation involving at least two Member States is concerned. How the new law will affect air transport services rendered solely within Germany remains to be seen.

### 3. IMPLEMENTATION OF IATA TARIFF CONSULTATIONS

In order for a tariff that has been negotiated by participating airlines at an IATA conference to become effective in a given country, it is necessary that the tariff proposal be approved by the government of that country.<sup>41</sup> In the past, such proposals have almost always been approved.<sup>42</sup> Accordingly, IATA airlines may in fact be viewed as a price cartel.<sup>43</sup>

#### D. POOLING AGREEMENTS

Bilateral air transport agreements are typically supplemented not only by tariff agreements but also by pooling agreements. Such agreements concern the financial or organizational cooperation of two or more airlines. Pooling agreements may contain a multitude of regulations.<sup>44</sup> Very often they deal with the distribution of earnings from a particular flight route serviced by two or more airlines.<sup>45</sup> In pooling agreements, airlines occasionally agree to restrict the number of flights on a particular route and to regulate the joint use of airport services.<sup>46</sup> Pooling agreements, along with tariff agreements and bilateral agreements, have been the foundations upon which an almost completely regulated market has been built.

#### E. LIBERALIZATION TENDENCIES IN EUROPE

In the last ten years, there has been a tendency towards more liberal bilateral air transport agreements. In particular, since the 1980's, the British Government has negotiated procompetitive bilateral air transport agreements with Luxembourg, the Netherlands, Belgium, and the Federal

39. See Antitrust Statute, Dec. 22, 1989, 1989 BGBl, I 2486 [hereinafter 1989 Antitrust Statute].

40. See *id.* art. 99(1); No. 1.

41. See Council Regulation 2342/90, *supra* note 9, art. 4(1). See also *Luftverkehrsgesetz*, *supra* note 37, art. 21(1).

42. A. KARK, *supra* note 11, at 86.

43. Accord J. BASEDOW, *supra* note 2, at 26. See also D. KASPER, DEREGULATION AND GLOBALIZATION 49 (1988); G. KNIIPS, DEREGULIERUNG IM LUFTVERKEHR 52 (1987).

44. L. WEBER, *supra* note 16, at 51-52.

45. See DEREGULATION AND AIRLINE COMPETITION 33-34 (Organisation for Economic Cooperation and Development ed. 1988).

46. W. SCHWENK, *supra* note 26, at 205.

Republic of Germany. These bilateral agreements were modeled after the Agreement between the United Kingdom and Luxembourg of March 1985.<sup>47</sup> The Air Route Agreement provides for a dismantling of market access and capacity restrictions, as well as introducing the double disapproval procedure for tariffs. According to the double disapproval principle, a tariff proposed by an airline becomes effective unless the governments of both countries voice their disapproval within an agreed period of time. Each of the agreements between the United Kingdom and the aforementioned countries contain similar provisions.<sup>48</sup>

While such bilateral agreements may be likely to further the liberalization process within the EC, they are unlikely to accomplish a complete liberalization of air transport, as not all Member States are prepared to agree to similar, let alone even more liberal measures.<sup>49</sup> If the Single European Market is to become reality, a comprehensive air transport law applicable to all EC Member States in an absolute requirement.<sup>50</sup> The regulations of the Council of Ministers that went into force on November 1, 1990, are an important step towards this goal.<sup>51</sup>

### III. THE EEC TREATY AND EUROPEAN AIR TRANSPORT POLICY

The EEC Treaty lays the foundations for a European air transport policy. According to the EEC Treaty, the establishment of a common market is the Community's primary goal.<sup>52</sup> The introduction of a common transport policy is expressly stated in the Treaty as one of the means of establishing a common market.<sup>53</sup> In view of the important role that transport

47. See Agreement between the United Kingdom of Great Britain and Northern Ireland and Luxembourg to liberalize route access, capacity and tariff approvals, Mar. 21, 1985 [hereinafter Air Route Agreement].

48. For details of the various agreements, see A. KARK, *supra* note 11, at 95-98.

49. *Accord* A. KARK, *supra* note 11, at 98.

50. It should be noted that the EC air transport laws enacted in recent years (*supra* at 8) do not displace the bilateral agreements presently in force between EC Member States. The EC laws do, however, limit the sovereignty of the Member States where such bilateral agreements are inconsistent with EC laws.

51. For details of the new regulations, see *infra* notes 181 through 253 and accompanying text. For a discussion of the EC Commission's proposals on which the new regulations are based, see Ebke & Wenglorz, *Die zweite Stufe der Liberalisierung des Linienluftverkehrs in der EG: Open Skies in Europa?*, 36 RECHT DER INTERNATIONALEN WIRTSCHAFT [RIW] 468, 475-77 (1990).

52. See EEC Treaty, *supra* note 1, art. 2. Article 2 reads as follows:

The Community shall have as its task, by establishing a common market and progressively approximating the economic policies of Member States, to promote throughout the Community a harmonious development of economic activities, a continuous and balanced expansion, an increase in stability, an accelerated raising of the standard of living and closer relations between the States belonging to it.

53. See EEC Treaty, *supra* note 1, art. 3(e). Article 3, in its pertinent part, reads as follows:

3. For the purposes set out in art. 2, the activities of the Community shall include, as provided in this Treaty and in accordance with the timetable set out therein: . . .

services play in the process of integration of the economies of EC Member States, the EEC Treaty contains special provisions dealing with transportation.<sup>54</sup> Of these provisions, only one directly addresses air transport,<sup>55</sup> the other provisions apply to road transport, railways, and inland waterways. Article 84(2) of the EEC Treaty grants the EC Council of Ministers the power to decide "whether, to what extent and by what procedure appropriate provisions may be laid down for sea and air transport."<sup>56</sup> It was not until 1983 that the Council acted pursuant to the powers granted by article 84(2). This is due to the fact that individual Member States' views with respect to both the function of civil aviation and its implications for the European transport policy differed significantly, and still do today.<sup>57</sup>

#### A. THE FRENCH SEAMEN'S CASE

EC Member States and the EC Commission have long disagreed on whether or not the general provisions of the EEC Treaty, including the antitrust provisions of the Treaty, apply to air transport. The Commission has always taken the position that the Treaty's general provisions are applicable to air transport, even though the Treaty leaves the shaping of specific air transport rules and policies to the Council.<sup>58</sup> France, on the other hand, was of the opinion that the general provisions of the EEC Treaty did not apply to air transport.<sup>59</sup> The French government argued that under article 84(2) of the EEC Treaty, air transport, like sea transport, is regulated exclusively by the Council of Ministers.<sup>60</sup> Prior to 1983, the Council had not, however, taken any action with regard to air transport.

In 1974, the European Court of Justice had an opportunity, in the *French Seamen's* case, to address the related issue of whether the general provisions of the EEC Treaty apply to sea transport.<sup>61</sup> The case arose in connection with a French law requiring that "leading" positions abroad French ships be given to French citizens only. The EC Commis-

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(e) the adoption of a common policy in the sphere of transport.

54. See EEC Treaty, *supra* note 1, art. 74-84.

55. See EEC Treaty, *supra* note 1, art. 84(2), which in 1974 read as follows:

2. The Council may, acting unanimously, decide whether, to what extent and by what procedure appropriate provisions may be laid down for sea and air transport.

Due to the Single European Act (*see supra* at 7) art. 84(2) was changed in 1987. It now reads:

2. The Council may, acting by a qualified majority, decide whether, to what extent and by what procedure appropriate provisions may be laid down for sea and air transport.

56. See EEC Treaty, *supra* note 1, art. 84(2).

57. For a detailed exposition of the reasons for the different views of the Members States, see L. WEBER, *supra* note 16, at 88-89.

58. *Id.* at 97-98.

59. *Id.* at 98.

60. *Id.*

61. Commission v. France, Case 167/73, [1974] Sig. 359.

sion was of the opinion that the French law violated the EEC Treaty. Specifically, the Commission argued that the French law was contrary to the Treaty's general provisions on the free movement of labor.<sup>62</sup> In its decision the European Court of Justice confirmed the Commission's view that the general provisions of the EEC Treaty apply to all transport services, including sea transport. The Court held that while they are not subject to the specific provisions of the EEC Treaty concerning transport services,<sup>63</sup> air and sea transport services, like other transport services (i.e., road transport, railways, inland waterways), are subject to the general provisions of the EEC Treaty.<sup>64</sup> Although it did not concern air transport, the Court's decision provided an important signal for the integration of air transport within the Community.<sup>65</sup>

### B. AFTERMATH

Unfortunately, in the years following the Court's decision in the *French Seamen's* case,<sup>66</sup> the Council used its powers under article 84(2) of the EEC Treaty with a great deal of reluctance. Many of the proposals of the EC Commission concerning the establishment of a competitive air transport system amounted to nothing, or were postponed from one Council meeting to the next.<sup>67</sup> The goal of a common air transport policy was not realized due to a lack of political will on the part of a majority of Member States. According to one commentator, air transport policy developed into "a dark chapter in the history of European integration."<sup>68</sup>

The European Parliament seemed to have agreed with this view. In 1983, the Parliament took the unusual step of taking the Council to court, under article 175 of the EEC Treaty,<sup>69</sup> for its inactivity in the entire area of

62. See EEC Treaty, *supra* note 1, arts. 48-51.

63. *Id.* arts. 74-83.

64. See Commission, [1974] Sig. at 371.

65. See L. WEBER, *supra* note 16, at 89.

66. Commission, [1974] Sig. at 359.

67. Basedow, *Der europäische Verkehrsmarkt als Rechtsproblem*, 12 TRANSPORTRECHT 402, 403 (1989).

68. Schrötter, *Europäische Verkehrspolitik auf dem Prüfstand—Das Untätigkeitsurteil des EuGH vom 22. Mai 1985 aus integrations- und verkehrspolitischer Sicht*, in 2 AKTUELLE RECHTSFRAGEN—MISCELLANIA 70-72 (I. Seidl-Hohenveldern ed. 1987).

69. See EEC Treaty, *supra* note 1, art. 175 which reads as follows:

Should the Council or the Commission, in infringement of this Treaty, fail to act, the Member States and the other institutions of the Community may bring an action before the Court of Justice to have the infringement established.

The action shall be admissible only if the institution concerned has first been called upon to act. If, within two months of being so called upon, the institution concerned has not defined its position, the action may be brought within a further period of two months.

Any natural or legal person may, under the condition laid down in the preceding paragraphs, complain to the Court of Justice that an institution of the Community has failed to address to that person any act other than a recommendation or an opinion.

transport policy. The Parliament argued that the Council had failed to introduce a common transport policy, or to provide a binding framework for such a policy, and that the Council had thereby violated the EEC Treaty.<sup>70</sup>

### C. TRANSPORT POLICY DECISION

In 1985, the European Court of Justice held partly in favor of the European Parliament.<sup>71</sup> The Court opined that the EEC Treaty's provisions that generally required a common transport policy within the Community, were not sufficiently concrete to be actionable.<sup>72</sup> The Court determined that articles 75(1)(a) and (b) of the EEC Treaty were adequately clear to require the Council of Ministers to take appropriate actions to implement a policy of intra-community transportation and to regulate cabotage rights.<sup>73</sup> According to the Court, the failure of the Council to act in accordance with articles 75(1)(a) and (b) of the EEC Treaty constituted an inactivity amounting to a violation of the Treaty.<sup>74</sup> The Court set no deadline by which time the Council had to meet its obligations under these articles; rather, the Court granted the Council a "reasonable period of time" to take appropriate actions.<sup>75</sup>

At first glance, the Court's decision may appear to be of relatively little importance inasmuch as it only reiterated the principle of freedom of trade in services provided for in the EEC Treaty. The decision had, however, far-reaching political implications. Only a few months after the Court's decision, the Council of Ministers presented a Master Plan Con-

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70. The Parliament claimed that the Council's failure to act constituted a violation of EEC Treaty, *supra* note 1, art. 3(e), art. 61, art. 74, art. 75, and art. 84. Art. 61 reads, in its pertinent part, as follows:

1. Freedom to provide services in the field of transport shall be governed by the provisions of the Title relating to transport.

Article 74 reads as follows:

The objectives of this Treaty shall, in matters governed by this Title, be pursued by Member States within the framework of a common transport policy.

Article 75 reads, in its pertinent part, as follows:

1. For the purpose of implementing Art. 74, and taking into account the distinctive features of transport, the Council shall, acting unanimously until the end of the second stage and by qualified majority thereafter, lay down, on a proposal from the Commission and after consulting the Economic and Social Committee and the Assembly;

(a) common rules applicable to international transport to or from the territory of a Member State or passing across the territory of one or more Member States;

(b) the conditions under which non-resident carriers may operate transport services within a Member State.

71. *European Parliament v. Council*, Case 13/83, [1985] Sig. 1513. For a general discussion of this case, see P. DAGTOGLOU, *AIR TRANSPORT AND THE EUROPEAN COMMUNITY* 50-75 (1989).

72. *European Parliament*, [1985] Sig. at 1596-1600.

73. *Id.* at 1600-1601.

74. *Id.* at 1600.

75. *Id.*

cerning Transport Policy<sup>76</sup> that, among other areas of transport services, affected air transport. Additionally, the Council set a seven year time limit within which substantial progress in regard to the freedom of trade in services had to be accomplished.<sup>77</sup> The Council also accepted the proposals made in the EC Commission's White Paper on the Completion of the Internal Market.<sup>78</sup> The White Paper contained a detailed plan of actions for the integration of the transportation markets. At roughly the same time, the governments of the EC Member States arrived at an agreement concerning the Single European Act (the "SEA").<sup>79</sup> The SEA amended the EEC Treaty and provided the foundation for the Single European Market.

On the basis of these measures, the Council and the Commission of the EC have become very active in the field of air transportation.<sup>80</sup> With its decisions in the *French Seamen's* case<sup>81</sup> and the *Transport Policy* case,<sup>82</sup> the European Court of Justice made a significant contribution to the establishment of European Community transport policy which should not be underestimated. These decisions helped accelerate the process of European integration towards a common market.

#### IV. THE DEVELOPMENT OF THE EC AIR TRANSPORT POLICY PRIOR TO DECEMBER 1987

The first major step towards the development of a common, liberalized air transport system within the European Community was taken by the Commission in 1979 with the publication of its First Memorandum.<sup>83</sup>

##### A. THE FIRST MEMORANDUM

The First Memorandum was based upon a detailed analysis of EC air transport policies existing prior to 1979. On the basis of this analysis, the Memorandum set forth the short, intermediate, and long term objectives relating to a common air transport policy within the EC. It also proposed possible and desirable measures for effecting their implementation.<sup>84</sup>

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76. See Masterplan, BULL. EUR. COMM. 11/85 at 81 (1985).

77. See Schrötter, *supra* note 68, at 84.

78. See Commission of the European Communities, *Completing the Internal Market* (White Paper from the Commission to the European Council, Milan, June 28-29, 1985). COM (85) 310 final (June 14, 1985).

79. See SEA, *supra* at 7.

80. See, e.g., the measures concerning the First and Second Phase of air transport liberalization, *supra* notes 8-9 and accompanying text.

81. *Commission*, [1974] Sig. at 359.

82. *European Parliament*, [1985] Sig. at 1513.

83. See First Memorandum, *supra* at 3.

84. See First Memorandum, *supra* note 3, at 20-26.

Most importantly, the Memorandum underscored the need for a change to the then existing market structures.

In the following years, the First Memorandum provoked a broad discussion of the proposed measures among all concerned, including airlines, the EC Commission, the EC Council, and the EC Member States.

### B. INTER-REGIONAL AIR SERVICES DIRECTIVE

After intensive discussions, the EC Council, at the suggestion of the EC Commission, promulgated the first directive for the liberalization of air transport.<sup>85</sup> The impact of this directive however, was limited. The directive applied only to international flights within the Community by aircraft with no more than 70 seats over a distance of at least 400 kilometers.<sup>86</sup> In addition, the directive only pertained to flights into small airports (i.e., category II and III airports).<sup>87</sup> As a result, the practical importance of the Council's first step towards air transport liberalization remained modest.<sup>88</sup>

It was not until 1989, that the Inter-regional Air Services Directive was further liberalized.<sup>89</sup> As a result of the 1989 amendments to the Directive, airlines were allowed to service routes under 400 kilometers.<sup>90</sup> Furthermore, aircraft size restrictions were removed.<sup>91</sup> Regarding this rather advanced step towards the aim of a deregulated framework for regional air transport services, the Council has adopted the Commission's attitude. This attitude, developed in recent years, is that regional air service between Member States is to be strongly promoted in order to take pressure off the large congested airports within the Community.

### C. THE SECOND MEMORANDUM

In view of the world-wide crisis in civil aviation at the beginning of the 1980's and the increased competitive pressure upon both the airline and the aircraft industry, the EC Commission published a Second Memorandum on Civil Aviation.<sup>92</sup> This Memorandum reflected the United States' experience with airline deregulation, which had its roots in the Airline De-

85. See Directive (83/416/EEC) concerning the authorization of scheduled inter-regional air services for the transport of passengers, mail, and cargo between Member States. 26 O.J. EUR. COMM. (No. L 237) 19 (July 25, 1983) [hereinafter Inter-regional Air Services Directive].

86. *Id.* art. 1(a)-(c).

87. See *id.* Appendix A.

88. For details, see A. KARK, *supra* note 11, at 116.

89. See Council Directive 89/463/EEC of 18 July 1989 amending Directive 83/416/EEC concerning the authorization of scheduled inter-regional air services for the transport of passengers, mail and cargo between Member States. 32 O.J. EUR. COMM. (No. L 226) 14 (Aug. 3, 1989).

90. See *id.* art. 1.

91. *Id.*

92. See Second Memorandum, *supra* at 4.

regulation Act of 1978.<sup>93</sup> The Second Memorandum set forth the major features of a future common air transport policy for the EC.<sup>94</sup> The Commission was primarily concerned with the regulation and creation of conditions for a competitive market for scheduled air transport.<sup>95</sup> The Memorandum was aimed at a liberalization of the existing bilateral air transport agreements. The deregulation envisaged by the Second Memorandum included only the EC Member States. Air transport between EC Member States and third countries would be deregulated at a later date.<sup>96</sup>

#### D. THE NOUVELLES FRONTIÈRES CASE

The Second Memorandum of the EC Commission and the decision of the European Court of Justice in the *Transport Policy* case<sup>97</sup> increased pressure on the EC Council to take effective measures towards the liberalization of EC air transport. The discussions within the Council proved to be difficult and time consuming. It was the European Court of Justice that finally took the lead in the liberalization process. In April 1986, the Court handed down the single most important decision relating to the liberalization of EC air transport.<sup>98</sup> The case, commonly known as the *Nouvelles Frontières* case, involved the issue of whether a travel agency registered in an EC Member State has the right to sell airline tickets at fares below the tariffs agreed upon by IATA-airlines and approved by the Member States' government.

In its decision, the Court held that the Community's antitrust laws, in particular articles 85<sup>99</sup> and 86<sup>100</sup> of the EEC Treaty, are as a general rule

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93. See Airline Deregulation Act, 92 Stat. 1705. For an exposition on the Airline Deregulation Act and its consequences see, Ebke & Wittmann, *Wettbewerb im Linienluftverkehr Erfahrungen mit der Deregulierung in den USA*, 36 RIW 962 (1990); Goetz & Dempsey, *Airline Deregulation Ten Years After: Something Foul in the Air*, 54 J. AIR L. & COM. 927 (1989); E. BAILEY, D. GRAHAM & D. KAPLAN, *DEREGULATING THE AIRLINES* (1985).

94. See Second Memorandum, *supra* note 4, at 21-28.

95. See *id.* at 28-40.

96. See *id.* at 21.

97. *European Parliament*, [1985] Sig. at 1513.

98. *Ministère Public v. Asjes et al.*, Cases 209-213/84, [1986] Sig. 1425. For a general discussion of this case, see P. DAGTOGLOU, *supra* note 71, at 77-114. See also Note, *New Frontiers in EEC Air Transport Competition*, 8 Nw. J. INT'L L. & Bus. 455 (1987).

99. For the text of EEC Treaty, see *supra* note 1, art. 85. See also *supra* at 28.

100. See EEC Treaty, *supra* note 1, art. 86 that reads as follows:

Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market in so far as it may affect trade between Member States. Such abuse may, in particular, consist in:

applicable to civil aviation.<sup>101</sup> The Court, however, qualified its holding by stating that articles 85 and 86 of the EEC Treaty cannot be enforced directly by the Commission or the Member States until these provisions are implemented by secondary Community law, such as implementing regulations or directives (as required by article 87 of the EEC Treaty).<sup>102</sup> Pointing to articles 88<sup>103</sup> and 89<sup>104</sup> of the EEC Treaty, the Court suggested that the Commission and the competent authorities of the Member

(a) directly or indirectly imposing unfair purchase or selling prices or unfair trading conditions;

(b) limiting production, markets or technical development to the prejudice of consumers;

(c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(d) making the conclusion of contacts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contacts.

101. *Ministère Public v. Asjes et al.*, Cases 209-213/84, [1986] Slg. at 1463-1466.

102. *See id.* 1466-1470. EEC Treaty, *supra* note 1, art. 87 reads as follows:

1. Within three years of the entry into force of this Treaty the Council shall, acting unanimously on a proposal from the Commission and after consulting the Assembly, adopt any appropriate regulations or directives to give effect to the principles set out in Arts. 85 and 86.

If such provisions have not been adopted within the periods mentioned, they shall be laid down by the Council, acting by a qualified majority on a proposal from the Commission and after consulting the Assembly.

2. The regulations or directives referred to in paragraph 1 shall be designed, in particular:

(a) to ensure compliance with the prohibitions laid down in Art. 85(1) and in Art. 86 by making provision for fines and periodic penalty payments;

(b) to lay down detailed rules for the application of Art. 85(3), taking into account the need to ensure effective supervision on the one hand, and to simplify administration to the greatest possible extent on the other;

(c) to define, if needed be, in the various branches of the economy, the scope of the provisions of Arts. 85 and 86;

(d) to define the respective functions of the Commission and of the Court of Justice in applying the provisions laid down in this paragraph;

(e) to determine the relationship between national laws and the provisions contained in this Section or adopted pursuant to this Article.

103. EEC Treaty, *supra* note 1, art. 88 reads as follows:

Until the entry into force of the provisions adopted in pursuance of Art. 87, the authorities in Member States shall rule on the admissibility of agreements, decisions and concerted practices and on abuse of a dominant position in the common market in accordance with the law of their country and with the provisions of Art. 85, in particular paragraph 3, and of Art. 86.

104. EEC Treaty, *supra* note 1, art. 89 reads as follows:

1. Without prejudice to Art. 88, the Commission shall, as soon as it takes up its duties, ensure the application of the principles laid down in Arts. 85 and 86. On application by a Member State or on its own initiative, and in co-operation with the competent authorities in the Member States, who shall give it their assistance, the Commission shall investigate cases of suspected infringement of these principles. If it finds that there has been an infringement, it shall propose appropriate measures to bring it to an end.

2. If the infringement is not brought to an end, the Commission shall record such infringement of the principles in a reasoned decision. The Commission may published its decision and authorize Member States to take the measures, the conditions and details of which it shall determine, needed to remedy the situation.

States take appropriate measures to enforce the general principles underlying articles 85 and 86 of the EEC Treaty.<sup>105</sup> Citing its decision in the *Bosch* case,<sup>106</sup> the Court made it very clear that the enforcement procedure of articles 88 and 89 of the EEC Treaty is not capable of assuring complete compliance with articles 85 and 86 of the EEC Treaty.<sup>107</sup>

Due to the limited applicability of articles 85 and 86 of the EEC Treaty, the Court's decision provides no answer to the question of whether IATA tariff agreements are in compliance with EC law. The Court's decision is also politely silent on the issue of whether or not Member States are in breach of the EEC Treaty when they approve tariffs agreed to at IATA conferences. Despite its limited holding, the Court's decision has had an immediate impact. In view of the Court's emphasis of the Commission's responsibilities under article 89 of the EEC Treaty, the Commission proceeded against ten major European airlines for violation of article 85 of the EEC Treaty.<sup>108</sup> With the Commission's threat of a lawsuit against them looming ahead, the airlines eventually agreed, among other things, to bring their tariff, capacity, and pooling agreements into compliance with the EC antitrust laws.<sup>109</sup>

#### E. THE SINGLE EUROPEAN ACT

The decisive step towards the liberalization of scheduled air transport within the Community was finally brought about by the Single European Act, which went into effect on July 1, 1987.<sup>110</sup> The Single European Act provides for the establishment of a Single European Market for air transport.<sup>111</sup> Most importantly, decisions concerning the establishment of a single market for air transport no longer require unanimous voting by Member States; rather, measures can now be taken by a majority of votes.<sup>112</sup>

In June 1987, after intensive discussions, the Council agreed upon a package of measures for the liberalization of scheduled air transport.<sup>113</sup> The implementation of these measures was delayed by a veto of the

105. *Ministère Public v. Asjes*, [1986] Sig. at 1469.

106. *Kledingverkoopbedrijf de Gens en Uitdenbogerd v. Robert Bosch GmbH*, Case 13/61, [1962] Sig. 97.

107. *Ministères Public v. Asjes*, [1986] Sig. at 1469.

108. These airlines included Air France, Aer Lingus, Alitalia, British Airways, British Caledonian, KLM, Deutsche Lufthansa, Olympic, Sabena, and SAS.

109. See A. KARK, *supra* note 11, at 130-31; Lenz, *Die Verkehrspolitik der Europäischen Gemeinschaften im Lichte der Rechtsprechung des Gerichtshofes*. 23 *EUROPARECHT* [EuR] 158, 173 (1988).

110. See SEA, *supra* at 7.

111. See *id.* art. 13.

112. *Id.* art. 16.

113. See Dempsey, *supra* note 8, at 671-72.

Spanish government.<sup>114</sup> The Spanish government was unwilling to accept the application of the EC liberalization measures to Gibraltar airport, as Spain still contests British sovereignty over Gibraltar. The concerns of the Spanish government were overcome by the end of 1987. The Council's compromise cleared the way for the First Phase of the process of liberalizing air transport within the EC.

## V. THE FIRST PHASE

In December 1987, the Council took a number of measures toward the liberalization of air transport that are commonly referred to as the First Package of Liberalization. This Package consists of the following: a Council Directive on tariffs, a Council Decision concerning capacity sharing and market access, a Council Regulation concerning the application of the EC antitrust laws to the air transport sector, and a Council Regulation concerning exemptions from EC antitrust laws.<sup>115</sup>

The measures mentioned are applicable only to flights between EC Member States. They do not apply to domestic flights within a given Member State, nor do they apply to flights between a Member State and third countries.<sup>116</sup> Rights and obligations of Member States vis-a-vis their airlines are not subject to the First Package. The regulation of domestic air transport remains the responsibility of each Member State. The First Package affects the Member States' sovereign rights with respect to market access for intracommunity flights, capacity sharing, and tariff approval. To illustrate the significance of the First Package, we shall take a closer look at the various provisions.

### A. ANTITRUST REGULATIONS

For the first time in the history of the European Community, the Council Regulation (EEC) 3975/87<sup>117</sup> effected the application of articles 85 and 86 of the EEC Treaty to airline companies in regards to flights between EC airports.<sup>118</sup> The Regulation also grants the EC Commission power to investigate and impose sanctions on both airlines and Member States for violations of articles 85 and 86 of the EEC Treaty.<sup>119</sup>

According to Council Regulation (EEC) 3976/87,<sup>120</sup> the Commission may, by means of a further regulation, exempt from EC antitrust laws cer-

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114. *Id.* at 672.

115. *See supra* at 8.

116. *See, e.g.*, Council Regulation (EEC) 3975/87, *supra* note 8, art. 1(2).

117. *Id.*

118. *Id.* art. 1.

119. *Id.* arts. 3-6.

120. *See* Council Regulation (EEC) 3976/87, *supra* at 8.

tain categories of agreements and concerted practices of airlines.<sup>121</sup> Such group exemptions are generally permitted under article 85(3) of the EEC Treaty.<sup>122</sup> Group exemptions may be subject to certain conditions and specific requirements.<sup>123</sup> In case of a breach of an obligation that was attached by the Commission to an exemption, the exemption may be revoked.<sup>124</sup> The Commission may also impose a fine on airlines that violate a granted exemption.<sup>125</sup> The following activities between airlines may be exempt; agreements concerning slot allocation, flight schedules, the joint acquisition of computer reservation systems, the maintenance of aircraft, tariff setting, the coordination of capacities and the division of earnings from scheduled flights (i.e., pooling agreements).<sup>126</sup>

Without delay, the Commission made use of its powers pursuant to article 2 of Council Regulation (EEC) 3976/87 by promulgating three regulations.<sup>127</sup> These regulations set forth the prerequisites for group exemptions with respect to the activities mentioned above. Those exemptions granted by the Commission were far-reaching and remained effective until January 1, 1991.<sup>128</sup> For example, airlines were permitted to continue to cooperate with other airlines on the basis of the above mentioned agreements. Thus, the exemptions provided the airlines concerned with a significant amount of protection in an increasingly competitive market.

#### B. TARIFFS

Council Directive 87/601/EEC<sup>129</sup> on tariffs for scheduled flights between Member States maintains the traditional tariff approval procedure.<sup>130</sup> Hence, a tariff becomes effective only if it has been approved by the governments of both Member States.<sup>131</sup> The substantive prerequisites for the approval of a proposed tariff are set forth in article 3 of the Directive. According to this provision, a tariff proposed by an airline shall be approved by the government if they are reasonably related to long-term, fully allocated costs of the applicant carrier.<sup>132</sup> Under article 3 of the Directive, the fact that the proposed air fare is lower than that offered

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121. *Id.* art. 2.

122. EEC Treaty, *supra* note 1, art. 85(3). *See supra* note 28 for text of art. 85(3).

123. *See* Council Regulation (EEC) 3976/87, *supra* note 8, art. 2(3).

124. *Id.* art. 7.

125. *Id.* art. 7(2).

126. *Id.* art. 2(2).

127. *See* Commission Regulations (EEC) 2671/88, 2672/87 and 2673/87, *supra* at 8.

128. *See, e.g.*, Commission Regulation (EEC) 2671/88, *supra* note 8, art. 8.

129. *See* Council Directive 87/601/EEC, *supra* at 8.

130. *Id.* art. 4.

131. *Id.* art. 4.

132. *Id.* art. 3.

by another carrier, on the same route, is not a sufficient reason for withholding approval.<sup>133</sup>

Tariff proposals may be made by an airline alone or after consultations with other airlines.<sup>134</sup> In the latter case, the consultations must conform to Commission Regulation 3976/87.<sup>135</sup> Article 7 of Council Directive 87/601/EEC provides a detailed procedure of notification and the consultation and arbitration process, should a Member State withhold approval.<sup>136</sup>

The Tariff Directive introduces a new tariff approval concept that the Directive refers to as "zones of flexibility."<sup>137</sup> Proposed tariffs that are within the margins of such zones of flexibility, are to be approved automatically by the governments concerned.<sup>138</sup> The Directive creates two discount zones. In the first zone (i.e. the discount zone), the discount is 10 to 35 percent of the reference tariff.<sup>139</sup> In the second (i.e. the deep discount zone), the discount of the reference tariff may be between 35 and 55 percent.<sup>140</sup> Discount tickets are subject to considerable restrictions.<sup>141</sup> Still, member states are free to agree to more liberal discount practices than those set forth in the Tariff Directive.<sup>142</sup>

### C. MARKET ACCESS AND CAPACITY SHARING

The Council Decision 87/602/EEC liberalizes market access and capacity sharing.<sup>143</sup> Bilateral agreements have traditionally provided for an equal (50:50) sharing of passenger capacity based upon the number of passengers of one airline on a given route. The Decision aims at a liberalization of firm sharing clauses. According to the Decision, airlines may increase or decrease their capacity by 5 percent, a capacity sharing ratio of 55:45.<sup>144</sup> The country in which the airline is registered may not interfere for the benefit of its airline. Effective October 1, 1989, the ratio was changed to 60:40.<sup>145</sup>

For the first time in the history of EC air transport law, the Council Decision grants every Member State the right of multiple designations.

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133. *Id.*

134. *Id.* art. 4(1).

135. *See* Council Regulation (EEC) 3976/87, *supra* note 8.

136. *See* Council Directive 87/601/EEC, *supra* note 8, art. 7.

137. *Id.* art. 5.

138. *Id.* art. 5(2).

139. *Id.* art. 5(1).

140. *Id.*

141. *Id.* Annex II.

142. *Id.* art. 6.

143. *See* Council Decision 87/602/EEC, *supra* at 8.

144. *Id.* art. 3(1).

145. *Id.* art. 3(2).

Each Member State may appoint more than one airline to service a given bilateral route, to the extent that the route is used by a certain number of passengers.<sup>146</sup>

The Decision also permits Community carriers to establish flight connections between major airports (i.e., category I airports)<sup>147</sup> in their home country and regional airports (i.e., category II and III airports)<sup>148</sup> of another Member State, regardless of distance or aircraft size.<sup>149</sup> In addition, Community carriers are entitled to introduce scheduled air services to and from two or more points in other Member States, provided that no traffic rights are exercised between the combined points.<sup>150</sup>

Most importantly, Community carriers may also carry out scheduled flights falling within the Fifth Freedom if certain conditions are met. The flight route thus needs to include at least one regional airport and the first or final airport must be within the home country of the carrier. In addition, the flight service in question may not exceed more than 30 percent of the annual capacity of the airline on any given route.<sup>151</sup>

#### D. CRITIQUE

The First Package was a cautious and conservative step toward more competition in scheduled air transport within the Community. Radical changes to the market structure were not accomplished by the new laws. Rather, the reforms were relatively minor since they were coupled with generous exemptions for EC carriers from the EC antitrust laws. Therefore, it should not come as a surprise that the First Package had only modest effects on both airlines and passengers.<sup>152</sup> Despite a few

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146. *Id.* art. 5(2) which reads as follows:

A Member State shall also accept multiple designation on a country-pair basis by another Member State:

1. in the first year after the notification of this Decision, on routes on which more than 250,000 passenger were carried in the preceding year;
2. in the second year, on routes on which more than 200,000 passengers were carried in the preceding year or on which there are more than 1,200 return flights per annum.
3. in the third year, on routes on which more than 180,000 passengers were carried in the preceding year or on which there are more than 1,000 return flights per annum.

147. Category 1 airports are listed in Annex II to Council Decision 87/602/EEC, *supra* note 8, at 25.

148. Category II and III airports are also listed in Annex II to Council Decision 87/602/EEC, *supra* note 8, at 25.

149. *See* Council Decision 87/602/EEC, *supra* note 8, art. 6(1).

150. *See id.* art. 7(1).

151. *Id.* art. 8(1).

152. *See generally* Commission of the European Communities, Report on the first year (1988) of implementation of the aviation policy approved in December 1978, COM (89) 476 final (Oct. 2, 1989).

market entries and the establishment of many new flight routes,<sup>153</sup> the development of air fares has remained a disappointment given the Commission's high expectations. The measures did not result in noticeable tariff reductions.<sup>154</sup> Consequently, additional more far-reaching measures are necessary if the objective of competitive market structures, in the area of scheduled air transport within the EC, is to be accomplished by January 1993.

#### VI. THE AHMED SAEED CASE

In April 1989, the European Court of Justice took the opportunity, in *Ahmed Saeed Flugreisen v. Zentrale zur Bekämpfung unlauteren Wettbewerbs e.V.*,<sup>155</sup> to comment on the First Package position concerning the new legal situation in EC air transport. This case involved two travel agencies in Frankfurt, Germany, that had sold tickets at fares that were up to 60 percent less than those approved by the German government. For this purpose, the travel agencies purchased tickets outside of Germany for flights originating in the country of purchase with a destination in a third country outside the EC, but having a stopover in a German airport.

In the lawsuit brought by the Association for the Protection Against Unfair Trade Practices in Germany, the plaintiff alleged that the two travel agencies had violated German law by selling the tickets above described. It was argued that the agencies had violated the German Air Transport Statute,<sup>156</sup> which prohibits the application of air fares not approved by the German government. It was further argued that the agencies had engaged in unfair trade practices, insofar as the fares for the tickets sold undercut the approved tariff applied by their competitors. The lower courts held in favor of the Association. The *Bundesgerichtshof*, Germany's highest court in civil and commercial matters, granted the writ of *certiorari* and submitted the case to the European Court of Justice for a preliminary ruling pursuant to article 177 of the EEC Treaty.<sup>157</sup> The Euro-

153. *Id.* at 7-12.

154. *Accord* Sir Leon Brittan, EC Commissioner of Competition, in a lecture presented at the Inaugural Conference of the European Air Law Association held in London on November 2, 1989, reprinted in AIR TRANSPORT AND THE EUROPEAN COMMUNITY; RECENT DEVELOPMENTS (P. Dagtogdou ed. 1991) (forthcoming).

155. Ahmed Saeed Flugreisen et al. v. Zentrale zur Bekämpfung unlauteren Wettbewerbs e.V., Case 66/86, reprinted in 38 ZEITSCHRIFT FÜR LUFT-UND WELTRAUMRECHT [ZLW] 124 (1989) [hereinafter *Ahmed Saeed*]. For a general discussion of this case see P. DAGTOGLOU, *supra* note 71, at 133-146.

156. See Air Transport Statute, *supra* at 37.

157. See EEC Treaty, *supra* note 1, art. 177(3), which reads as follows:

The Court of Justice shall be competent to make preliminary rulings concerning:

- (a) the interpretation of this treaty;
- (b) the validity and interpretation of acts of the institutions of the Community;

pean Court of Justice concluded that tariff setting agreements between carriers constituted illegal cartels and therefore violated article 85(1) of the EEC Treaty.<sup>158</sup>

#### A. ASSUMPTIONS OF THE COURT

The holding of the Court is based upon the assumption that article 85 of the EEC Treaty was directly applicable to the case at hand. This assumption went beyond the holding in the *Nouvelles Frontières* case.<sup>159</sup> In that case, the Court held that because of the lack of implementing Community legislation, article 85 of the EEC Treaty could not be enforced directly; rather, the Commission and the competent authorities of the Member States could take measures against airlines only pursuant to articles 88 and 89 of the EEC Treaty. If article 85 of the EEC Treaty is directly applicable, the Commission no longer needs to utilize the procedures provided for in article 89 of the EEC Treaty. Rather, the Commission may proceed directly under article 85 of the EEC Treaty as implemented by Council Regulations 3975/87 and 3976/87.<sup>160</sup>

#### B. ARTICLE 85 OF THE EEC TREATY

In *Ahmed Saeed*, the European Court of Justice explicitly stated that tariff setting agreements constitute illegal cartels and violate article 85(1) of the EEC Treaty.<sup>161</sup> According to Council Regulation 3976/87, such agreements may not be subject to group exemptions.<sup>162</sup> The Court pointed out that tariff "consultations," as opposed to tariff "agreements," remain exempt.<sup>163</sup> The criteria for differentiating between permissible tariff consultations and illegal tariff agreements are set forth in article 4 of the Commission Regulation 2671/88.<sup>164</sup> Consequently, tariff agreements

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(c) the interpretation of the statutes of bodies established by an act of the Council, where such statutes so provide.

Where such a question is raised before a court or tribunal of one of the Member States, such court or tribunal may, if it considers that its judgment depends on a preliminary decision on this question, request the Court of Justice to give a ruling thereon.

Where any such question is raised in a case pending before a domestic court or tribunal from whose decisions no appeal lies under municipal law, such court or tribunal shall refer the matter to the Court of Justice.

For a discussion of the procedures under art. 177, see B. BEBR, DEVELOPMENT OF JUDICIAL CONTROL OF THE EUROPEAN COMMUNITY 366-452 (1981); T. HARTLEY, *supra* note 1, at 246-282.

158. See *Ahmed Saeed*, 38 ZLW at 127.

159. See *Ministère Public v. Asjes et al.*, Cases 209-213/84 [1986] Sig. 1425. For details, see *supra* notes 97-107 and accompanying text.

160. See Council Regulations 3975/87 and 3976/87, *supra* note 8.

161. See *Ahmed Saeed*, 38 ZLW at 127.

162. *Id.* at 127.

163. *Id.*

164. *Id.* at 128. See also Commission Regulation 2671/88, *supra* note 8, art. 4. The text of this regulation is reprinted *supra* note 30.

for intracommunity flights that did not fall within the group exemption were void *per se*, unless an objection made by the carrier concerned under article 5 of Council Regulation 3975/87 was successful.<sup>165</sup> With respect to domestic flights and flights between a Member State and a third country, the procedure pursuant to articles 88 and 89 of the EEC Treaty remains applicable.<sup>166</sup>

### C. ARTICLE 86 OF THE EEC TREATY

The statements of the European Court of Justice as to article 86 of the EEC Treaty are particularly interesting. The Court suggests that the abuse-of-market-power provisions of article 86 of the EEC Treaty apply to the entire air transport sector. That is to say that article 86 of the EEC Treaty applies to intracommunity flights, to domestic flights and flights from an EC Member State to a third country.<sup>167</sup> Consequently, tariff agreements concerning flights from an airport of an EC Member State to an airport outside of the Community fall as much within the ambit of article 86 of the EEC Treaty, as do tariff agreements concerning intracommunity and domestic flights. This is particularly true in cases where an airline company is in a position to control the market or to charge excessively high or extremely low tariffs on a given route.<sup>168</sup>

According to the Court, the fact that article 86 of the EEC Treaty has not been implemented by secondary Community law does not prevent the Commission from enforcing the provision.<sup>169</sup> Member States' courts may also enforce article 86 of the EEC Treaty, even absent secondary Community law implementing said Treaty provision.<sup>170</sup> For the *Bundesgerichtshof*, this was an important observation, as it had to decide the issue of whether a court may enforce article 86 of the EEC Treaty despite the lack of implementing Community legislation.

### D. ARTICLES 5 AND 90 OF THE EEC TREATY

Based upon its conclusions with respect to articles 85 and 86 of the EEC Treaty, the European Court of Justice stated that a Member State violates Community law (i.e., its obligations under article 5<sup>171</sup> and article

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165. See *Ahmed Saeed*, 38 ZLW at 127.

166. *Id.* at 128. For details of the procedures under arts. 88 and 89 of the EEC Treaty, see *supra* notes 99-107 and accompanying text.

167. See *Ahmed Saeed*, 38 ZLW at 129.

168. *Id.* at 130-131.

169. *Id.* at 129.

170. *Id.* at 130-131.

171. EEC Treaty, *supra* note 1, art. 5 reads as follows:

Member States shall take appropriate measures, whether general or particular, to ensure fulfillment of the obligations arising out of this Treaty or resulting from action taken by the institutions of the Community. They shall facilitate the achievement of the Com-

90(1)<sup>172</sup> of the EEC Treaty) if it approves tariffs that are contrary to article 85 or article 86 of the EEC Treaty.<sup>173</sup> As a result, the Member States' governments are required, in the approval process, to assure that the tariff consultations are in conformity with the principles laid down in articles 85 and 86 of the EEC Treaty, as well as Council Directive 87/601/EEC and Commission Regulation 2671/88.<sup>174</sup> The Court also made it perfectly clear that it expects the Member States not to enter into new bilateral agreements with third countries that, directly or indirectly, provide for illegal tariffs.<sup>175</sup>

### E. ANALYSIS

In the *Ahmed Saeed* case, there are two issues concerning the tariff setting process worth noting. By extending the application of article 86 of the EEC Treaty to flights between Member States and third countries, the Court put considerable pressure on the Member States to make sure that tariff setting and tariff approval provisions in bilateral agreements are consistent with EC antitrust laws. As a result, existing agreements that are contrary to article 86 of the EEC Treaty need to be renegotiated. Also, the applicability of article 86 to agreements concerning flights from within the Community to third countries is an extension of existing EC Laws<sup>176</sup> not only to intracommunity flights but also to both domestic flights within an EC Member State and flights to third countries.

The European Court of Justice rendered its decision in the *Ahmed Saeed* case just as the Commission was about to finish its work on the proposals for the Second Phase of Liberalization. Nevertheless, the Commission managed to include the implications of the *Ahmed Saeed* decision in its proposals for the Second Phase of liberalization.<sup>177</sup>

## VII. THE SECOND PHASE

In September 1989, the EC Commission published proposals for fur-

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munity's tasks. They shall abstain from any measure which could jeopardize the attainment of the objectives of this Treaty.

172. EEC Treaty, *supra* note 1, art. 90 reads, in its pertinent part, as follows:

1. In the case of public undertakings and undertakings to which Member States grant special or exclusive rights. Member States shall neither enact nor maintain in force any measure contrary to the rules contained in this Treaty, in particular to those rules provided for in Art. 7 and Arts. 85 through 94.

173. See *Ahmed Saeed*, 38 ZLW at 131.

174. See Council Directive 87/601/EEC and Commission Regulation (EEC) 2671/88, *supra* at 8.

175. See *Ahmed Saeed*, 38 ZLW at 131-132.

176. See Council Regulations, Directive and Decision, *supra* note 8.

177. See COM(89) 417 final (Sept. 8, 1989) at 1-5.

ther liberalization of EC scheduled air transport.<sup>178</sup> The proposals are aimed at the relaxation of tariffs, capacity sharing, and market access. On the basis of the Commission's proposals, the Council of the EC Transport Ministers, at its meeting in June 1990, agreed to a package of measures, commonly referred to as the Second Phase of the liberalization of EC air transport. These measures consist of three Council Regulations, two of which<sup>179</sup> became effective November 1, 1990.<sup>180</sup>

#### A. TARIFFS

The new Tariff Regulation is the centerpiece of the second package. This Regulation provides more flexibility in the tariff setting and approval process. While the requirement that tariffs be approved by the affected governments remains unchanged,<sup>181</sup> both the approval procedure and the range of approvable fares have changed considerably. Most importantly, the 1990 Tariff Regulation introduces, for the first time in the history of EC air transport laws, the double disapproval system.<sup>182</sup> The Regulation did not, however, go so far as to permit the double disapproval system to be applied to all tariffs, as proposed by the EC Commission.<sup>183</sup> Rather, the double disapproval system applies only to tariffs that exceed the reference tariff by at least 5 percent.<sup>184</sup>

The First Phase system of reference tariffs and flexibility zones was revised. The Tariff Regulation allows Community carriers to set the price for a "normal economy class ticket," independently,<sup>185</sup> within a margin of plus or minus 5 percent of the reference tariff.<sup>186</sup> Under the First Phase, the price for an economy class ticket was fixed at 100 percent of the reference tariff. The margins of the discount zone were changed from between 90 and 65 percent to between 94 and 80 percent. The margins of the deep discount zone were broadened from between 65 and 45 per-

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178. COM(89) 373 final and COM(89) 417 final (Sept. 8, 1989). For a detailed discussion of the Commission's proposals see Ebke & Wenglorz, *supra* note 51, at 475-477.

179. See Council Regulations 2342/90 and 2343/90, *supra* at 9.

180. See, e.g., Council Regulation 2342/90, *supra* note 9, art. 14.

181. See *id.* art. 4(1).

182. *Id.* art. 4(4).

183. See COM(89) 373 final (Sept. 8, 1989), art. 4(3).

184. See Council Regulation 2342/90, *supra* note 9, art. 4(4). The reference tariff is described in more detail *infra*, note 186.

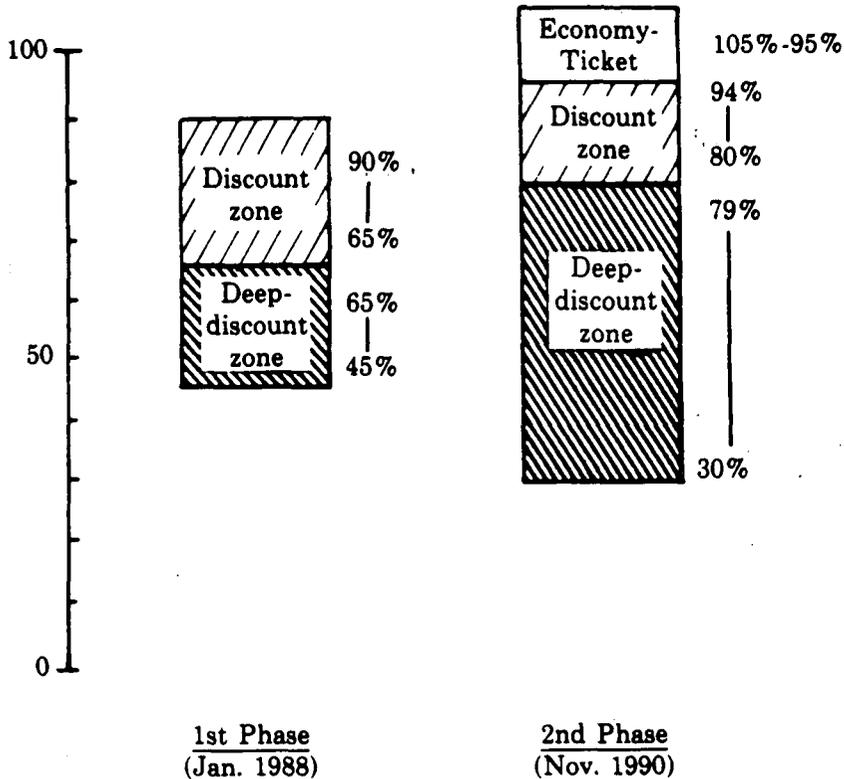
185. *Id.* art. 4(3).

186. The reference tariff is defined in Council Regulation 2342/90, *supra* note 9, art. 2(i) which reads as follows:

Reference fare means the normal one way or return, as appropriate, economy air fare charged by a third or fourth freedom air carrier on the route in question; if more than one such fare exists, the arithmetic average of all such fares shall be taken unless otherwise bilaterally agreed; where there is no normal economy fare, the lowest fully flexible fare shall be taken.

cent to between 79 and 30 percent.<sup>187</sup> The diagram in Table 1 illustrates the differences concerning the zones of flexibility between the First and Second Phase:

TABLE 1



The prerequisites for attaining a ticket within the discount zone have been eased. Prior to November 1, 1990, the journey had to include at least one Saturday night and a total of six nights, or alternatively, had to take place during off-peak times.<sup>188</sup> Under the new Tariff Regulation, these requirements, particularly detrimental to business travelers, no longer exist.<sup>189</sup> This impressive move towards more flexibility for a passenger wanting to acquire lower priced tickets is counteracted by the fact that the discount zone was reduced from 35 to 14 percent.<sup>190</sup> The reduc-

187. *Id.* art. 4(3).

188. See Council Directive 87/601/EEC, *supra* note 8, Annex II No. 1.

189. See Council Regulation 2342/90, *supra* note 9, Annex II No. 1.

190. *Id.* art. 4(3).

tion is not offset by the increase in the margins of the deep discount zone from 20 to 49 percent. For the most part, the restrictive requirements for entering the deep discount zone continue to be in effect.<sup>191</sup>

### 1. THE TARIFF APPROVAL PROCESS

According to the new Tariff Regulation, tariff approval follows from one of three procedures:

#### A. AUTOMATIC APPROVAL

If the proposed tariff of an airline lies within one of the aforementioned flexibility zones, the governments of the Member States are required to approve the tariff.<sup>192</sup> This results in a system of automatic approval, as the approval itself is merely a formality if other conditions, particularly for those set forth in article 3 of the Tariff Regulation are fulfilled.

If a tariff proposed by an airline lies above the zones mentioned in article 4(3) of the Tariff Regulation (i.e., if it is more than 5 percent above the reference tariff),<sup>193</sup> the system of Double Disapproval applies. Under this system, tariff is deemed to be approved if the Member States concerned do not, within 30 days of the airlines' application for approval, reject the requested tariff.<sup>194</sup> While it applies to a small number of tickets only, the double disapproval system enables the Member States and the EC Commission, to gain practical experience with the procedure. This is important when one takes into consideration that, beginning January 1, 1993, the double disapproval system will be applied to all tariffs.<sup>195</sup>

#### B. DOUBLE APPROVAL

A tariff proposed by an airline that is neither within one of the flexibility zones nor above the reference tariff, must be approved explicitly by both governments.<sup>196</sup> In such a case, the tariff is deemed to be approved if neither one of the governments involved rejects the tariff within 21 days upon receipt of the application.<sup>197</sup> Tariffs subject to the double approval system are most likely to be below the deep discount zone. The Member States, it seems, were not prepared to give up their strict control over these tariffs.

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191. *Id.* Annex II, No. 2.

192. *Id.* art. 4(3).

193. For a definition of the reference tariff, see *supra* at 186.

194. See Council Regulation 2342/90, *supra* note 9, art. 4(4).

195. *Id.* art. 12.

196. *Id.* art. 4(5).

197. *Id.*

## 2. INVESTIGATION AND CONSULTATION PROCEDURE

The Tariff Regulation provides control mechanisms for cases in which a Member State challenges a tariff for lack of conformity with the Tariff Regulation.

### A. ARTICLE 5 OF THE COUNCIL REGULATION

At the request of a Member State having a reasonable interest in the route in question, the Commission is obliged to inquire into the conformity of any previously approved tariff that does not lie within the flexibility zones.<sup>198</sup> The Commission is also required to inquire whether the other Member State has met its obligations under article 3(3) of the Regulation.<sup>199</sup> According to article 3(3),<sup>200</sup> the Commission must investigate whether or not an airline charges unjustifiably high tariffs that are not in the best interest of consumers. It is also obliged to investigate whether the tariffs are "dumping tariffs" aimed at the expulsion of competitors from a given route.<sup>201</sup> Within 14 days of being called upon by a Member State, the Commission must decide whether or not the tariff in question is to remain in effect during the investigation period.<sup>202</sup> The final decision on all these matters must be made within two months of the receipt of the Member State's request.<sup>203</sup> Within one month after the decision, the affected Member State may appeal to the EC Council.<sup>204</sup>

The procedure provided for by article 5 of the Tariff Regulation is an important instrument in the hands of the Member States. The provision enables the Member States to control a fare's development, especially if the tariff deviates too far in one direction or another. It should be recognized, however, that the possibility of an appeal by the concerned Member State to the EC Council of Ministers adds a political dimension to the tariff setting process which could be undesirable in light of the importance of the enforcement of EC antitrust laws.

### B. ARTICLE 6 OF THE COUNCIL REGULATION

Article 6 of the Tariff Regulation deals with cases in which tariffs that are below the flexibility zones and have to be approved by both governments,<sup>205</sup> are rejected by one government.<sup>206</sup> In those cases, article 6

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198. *Id.* art. 5(1).

199. *Id.*

200. For the text of Council Regulation 2342/90, *supra* note 9, art. 3; text of Council Regulation 2342/90 *supra*, at 193.

201. See Council Regulation 2342/90 *supra* note 9, art. 3(3).

202. *Id.* art. 5(2).

203. *Id.* art. 5(3), (4).

204. *Id.* art. 5(5).

205. See *supra* notes 197-98 and accompanying text.

provides for a detailed consultation and arbitration procedure.<sup>207</sup> If confirmed by the EC Commission, the arbitrators' decision becomes binding on both governments.<sup>208</sup>

### 3. PRICE LEADERSHIP

The new Regulation extends the possibilities for EC airlines to become price leaders (i.e., introducing lower tariffs on an existing flight route).<sup>209</sup> Prior to November 1, 1990, the possibility for increased price competition was limited to routes on which the Third and Fourth freedom rights were exercised (i.e., on intra-community non-stop connections).<sup>210</sup> According to the new Tariff Regulation, Community carriers may now become price leaders when operating on the Fifth Freedom route; provided, the tariffs proposed by the airlines remain within the flexibility zones.<sup>211</sup> Despite this limitation, the provisions are likely to considerably strengthen competition on routes on which airlines of the third, fourth, and fifth freedoms operate.

### 4. OTHER PROVISIONS

The Tariff Regulation allows Member States to enter into or maintain more flexible bilateral agreements than those mentioned in article 4 of the Tariff Regulation.<sup>212</sup> This is true, for example, of the British-German Agreement<sup>213</sup> and the British-Luxembourg Air Transport Agreement.<sup>214</sup> Furthermore, EC Member States are required to bring their bilateral agreements with third states that were granted Fifth Freedom rights for their carriers on routes within the Community, in line with the Tariff Regulation "at the first possible occasion," if the agreements are contrary to the Council Regulation.<sup>215</sup> Most importantly, the new Regulation requires that the double disapproval system be introduced by January 1, 1993.<sup>216</sup>

### 5. SCOPE OF THE TARIFF REGULATION

Contrary to the proposals of the EC Commission,<sup>217</sup> the Council did not extend the Tariff Regulation to flights from within the EC to flights from

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206. See Council Regulation 2343/90, *supra* note 9, art. 6(1).

207. *Id.* arts. 6(10)-(9).

208. *Id.* art. 6(8).

209. *Id.* art. 3(6). For the text of art. 3, see *supra* at 193.

210. See Council Directive 87/601/EEC, *supra* note 8, art. 4(5).

211. See Council Regulation 2342/90, *supra* note 9, art. 3(6).

212. *Id.* art. 7.

213. See *supra* notes 47-48 and accompanying text.

214. See Air Route Agreement, *supra* note 47.

215. *Id.* art. 11.

216. *Id.* art. 12.

217. See COM(89) 373 final (Sept. 8, 1989), Annex I, art. 1.

an EC airport to a third country. The Regulation applies only to scheduled flights on routes between Member States.<sup>218</sup> It should also be noted that the new Tariff Regulation binds Member States directly. Thus, there is no room for the Member States to exercise discretion in the transformation and application of the Regulation. This differs significantly from the old Tariff Directive of 1987<sup>219</sup> that, like all Directives, left the form and methods of implementation to the Member States.

### B. MARKET ACCESS AND CAPACITY

The Council Regulation Concerning Capacity Sharing and Market Access<sup>220</sup> may be divided into two parts:

#### 1. MARKET ACCESS

The Regulation explicitly grants the right of an EC carrier to fly an international route within the Community, as part of the Third and Fourth Freedom rights.<sup>221</sup> Consequently, EC carriers that operate under the Third and Fourth Freedom rights have free access to all EC airports.<sup>222</sup> At the same time, the Regulation requires Member States (country of destination) to allow, on the basis of reciprocity, airlines that operate internationally and are registered in another Member State (country of registration) to make use of the Third and Fourth Freedom rights on the same route.<sup>223</sup>

The reciprocity requirement is controversial as it allows a Member State to make the introduction of new routes or frequencies on an existing route conditional upon the receipt of the same number of new routes or frequencies for its airlines. The reciprocity rule can have the effect that a carrier based at a slot-tight airport (i.e., British Airways in London-Heathrow, England) may be unable to obtain new frequencies at, or routes to, less frequently used airports (e.g., Lisbon, Portugal) unless an airline of that country (e.g., TAP Air Portugal) attains route rights for London-Heathrow. While it may be detrimental to large carriers operating out of slot-tight airports, the reciprocity requirement may be beneficial to smaller carriers operating out of less frequented airports as they may use their leverage power to gain access to the slot-tight airport.

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218. See Council Regulation 2342/90, *supra* note 9, art. 1.

219. See Council Directive 87/601/EEC, *supra* at 8.

220. See Council Regulation 2343/90, *supra* at 9.

221. *Id.* arts. 4, 5(1).

222. There are a few exceptions to this general rule, see *id.* art. 1(4).

223. *Id.* arts. 5(1), (2).

#### A. MULTIPLE DESIGNATION

The new Regulation reduces the threshold for multiple designations on a country-pair basis.<sup>224</sup> Since January 1, 1991, a Member State must agree to a multiple designation by another state on a given bilateral route if there were more than 140,000 passengers travelling on the route or more than 800 return flights in the preceding year.<sup>225</sup> Effective January 1, 1992, however, the threshold will be reduced to 100,000 passengers or 600 return flights per year and route.<sup>226</sup> The Regulation opens the way for EC Member States to allow more than one airline to service a particular route. As a result, a route that has previously been limited to a single carrier per country, may in the future be served by more than one carrier.

#### B. FIFTH FREEDOM RIGHTS

In addition, the Regulation extends the possibility for airlines to exercise Fifth Freedom rights.<sup>227</sup> Under the First Phase Decision, an airline was only allowed to use 30 percent of its annual carrying capacity on a given route for Fifth Freedom service.<sup>228</sup> Under the new Regulation, it is possible to use up to 50 percent of the seating capacity per flight plan period on any given route.<sup>229</sup> The 20 percent increase constitutes modest improvement towards more competition. Unfortunately, the Council did not follow the Commission's proposal to allow carriers to make use of their rights of the Fifth Freedom in regard to third countries, if such countries agree.<sup>230</sup> Thus, there is considerable room for further liberalization in the future.

#### C. PUBLIC SERVICE OBLIGATION

Under the new Regulation, an airline may be required to service regional airports within its home country.<sup>231</sup> In order to fall within this category of airports, however, the airport must be of paramount importance to the economic development of the region concerned.<sup>232</sup>

#### D. INTER-REGIONAL AIR SERVICE

The 1990 Regulation replaces the Inter-regional Air Services Direc-

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224. *Id.* art. 6.

225. *Id.* art. 6(2).

226. *Id.*

227. *Id.* art. 8.

228. See Council Decision 87/602/EEC, *supra* note 8, art. 8(1).

229. See Council Regulation 2343/90, *supra* note 9, art. 8(1).

230. See COM(89) 373 final (Sept. 8, 1989), Annex II, art. 8 No. 2.

231. See Council Regulation 2343/90, *supra* note 9, art. 5(3).

232. *Id.* art. 5(3).

tive of 1983.<sup>233</sup> Inter-regional air transport is now subject to the new Market Access and Capacity Sharing Regulation. To a limited extent, the 1990 Regulation protects airlines that service regional airports and that have opened new routes, against carriers operating with larger aircraft.<sup>234</sup> To protect regional carriers, the reciprocity requirement is not applied for a period of two years; provided, the carrier has been granted the privilege to fly a new route between two regional airports within the Community.<sup>235</sup> The reciprocity rule comes into effect again, however, if a foreign carrier with an aircraft carrying no more than 80 passengers intends to fly the same route.<sup>236</sup>

#### E. REVERSE DISCRIMINATION AND CABOTAGE

It is important to call attention to two provisions that were part of the Commission's proposals<sup>237</sup> that the Council, however, did not include in the 1990 Tariff Regulation.

The Commission had proposed a clause according to which each Member State was required to allow more than one airline in its own territory to offer scheduled flights, if certain financial and technical criteria were met.<sup>238</sup> The Council, however, was of the opinion that the new Regulation should not interfere with the relationship between a Member State's government and carriers registered in that Member State.<sup>239</sup> Consequently, there is always a possibility that domestic carriers may be discriminated against under the laws of its country of registration. Under the new Regulation, it is still possible that an EC Member State would deny a carrier that is registered under its laws the ability to offer certain air services, only to allow a carrier registered under the laws of another Member to do so. It seems to have been impossible to obtain majority within the Council for the Commission's proposal because the adoption of the Commission's proposal would, in effect, have resulted in the loss of national sovereignty rights which the Member States were not prepared to accept at this point in time. Accordingly, the problem of reverse discrimination of domestic carriers continues to exist and there continues to be no relief under EC laws to remedy this situation.

Furthermore, the Council did not adopt the Commission's cabotage rights proposal. According to this proposal, the Member States were to

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233. For details of the Inter-regional Air Service Directive, see *supra* notes 85-88 and accompanying text.

234. See Council Regulation 2343/90, *supra* note 9, art. 5(4).

235. *Id.*

236. *Id.*

237. See COM(89) 373 final (Sept. 8, 1989), Annex II, art. 3(1), 9.

238. *Id.* art. 3(1).

239. See Council Regulation 2343/90, *supra* note 9, art. 3(1).

introduce, beginning in 1990, cabotage rights for Community airlines to a limited extent.<sup>240</sup> The Council stated, however, that it found it "desirable" to take further liberalization measures with respect to market access and capacity sharing, including the introduction of a cabotage rule by June 30, 1992.<sup>241</sup> It remains to be seen whether the Council will meet its own deadline. It should be noted that the deadline stated in the Regulation creates no legal obligation on the part of the Council to act.

## 2. CAPACITY SHARING

Starting with the 60:40 capacity sharing ratio that came into effect on October 1, 1989,<sup>242</sup> the new Regulation allows Community carriers to extend their seating capacity, beginning on November 1, 1990, by 7.5 percent per flight plan period.<sup>243</sup> At the request of a Member State, the Commission may, however, limit the growth in capacity, if the capacity increase results in substantial damage to a carrier registered in that Member State.<sup>244</sup>

It is worth noting that the new Regulation states as one of its objectives, the full dismantling of barriers regarding capacity sharing between Member States by January 1, 1993.<sup>245</sup> This has, however, already been implemented for all regional flights within the EC, effective November 1, 1990, regardless of the seating capacity of the aircraft used.<sup>246</sup> Unfortunately, the Regulation again does not go as far as the Commission's original proposal. The Commission had suggested that capacity limits also be dismantled for flights between category I airports and regional airports.<sup>247</sup> Such a measure would have benefitted international air services between regional airports and large airports. At the same time it would have relieved the pressure on major European airports that are already heavily congested.

## C. ANTITRUST PROVISIONS

The EEC Council Regulation 2344/90<sup>248</sup> which forms part of the Second Phase, should be mentioned as well. The Regulation consists of one provision only. This provision empowers the Commission to continue to

240. For details see COM(89) 373 final (Sept. 8, 1989), Annex II, art. 9.

241. See Council Regulation 2343/90, *supra* note 9, preamble.

242. See Council Decision 87/602/EEC, *supra* note 8, art. 3(2).

243. See Council Regulation 2343/90, *supra* note 9, art. 11(1). It should be noted that the summer flight plan period lasts from April 1 until October 31, the winter period from November 1 until March 31.

244. See *id.* art. 12(1).

245. *Id.* art. 11(2).

246. *Id.* art. 11(3).

247. See COM(89) 373 final (Sept. 8, 1989), Annex II, art. 12(3).

248. See Council Regulation 2344/90, *supra* note 9.

exempt, until December 31, 1992, certain airline practices and airline agreements from the EC antitrust laws.<sup>249</sup> The Council did not, however, follow the Commission's proposal concerning amendments and extensions of Council Regulations 3975/87 and 3976/87.<sup>250</sup> The Council's failure to adopt the Commission's proposal is regretful because the Council simply ignored the holding of the European Court of Justice in the *Ahmed Saeed* case<sup>251</sup> concerning the application of articles 85 and 86 of the EEC Treaty to flights to third countries and domestic flights.<sup>252</sup>

#### VIII. OTHER AIR TRAFFIC PROBLEMS

The degree of competition that may develop in air transport within the EC, depends to a large extent upon the available infrastructure, including runways, air traffic control systems, and slots. In this area a number of problems exist. With the expected growth in air traffic,<sup>253</sup> these problems are likely to become more severe. It has been said that, in Europe, chaos on the ground and in the air is no longer a myth, but nearly a reality.<sup>254</sup> Necessary changes and improvements will be extraordinarily expensive. At a number of European airports, such as Frankfurt, Madrid, and London-Heathrow, slots are no longer available during peak hours. The shortage of slots makes it very difficult, if not impossible, for new airlines to enter the market.<sup>255</sup> Also, the European air traffic control system is technically outdated and still largely based upon the traditional system of national air space control.<sup>256</sup> Internationally integrated air traffic control systems, such as Eurocontrol, are, unfortunately, still of relatively little significance.<sup>257</sup> The lack of a modern international control system within the Community is a technological and political anachronism at a time when

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249. *Id.* art. 1.

250. See COM(89) 417 final (Sept. 8, 1989).

251. See *Ahmed Saeed*, 38 ZLW at 124. See also *supra* notes 155-76 and accompanying text.

252. See *supra* notes 161-70 and accompanying text.

253. IATA expects European air traffic to grow at least 6% *per annum* in the coming years. See *Süddeutsche Zeitung*, Oct. 30, 1989, at 26.

254. According to a Stanford Research Institute study that was prepared for IATA, European air traffic is likely to collapse unless there is a radical improvement in the organization of air traffic, especially in the field of air traffic control and the capacity of larger airports. See *Frankfurter Allgemeine Zeitung*, May 3, 1990, at R13.

255. The great importance of attractive slots for new market entries could be observed in the case of the German airline newcomer "German Wings." The company went out of business less than a year after its entry, mainly because "German Wings" was unable to attain peak-hour slots. See *Die Zeit*, May 4, 1990, at 32.

256. See Bothe, Hohmann & Schmidt, *Möglichkeiten einer Reform der europäischen Flugsicherung?*, 39 ZLW 40 (1990).

257. *Id.* at 43-45.

the completion of the Single European Market is less than two years away.

The Commission has already made a number of proposals to the Council in an attempt to solve the problems mentioned.<sup>258</sup> Additional proposals have also been announced.<sup>259</sup> New initiatives regarding to airport fees,<sup>260</sup> EC-wide air traffic control, and slot allocation are being proposed.<sup>261</sup> Moreover, the Commission is presently attempting to obtain a power of attorney from the Member States to negotiate, on behalf of the EC as a whole, air transport agreements with third countries.<sup>262</sup> A comprehensive package of complementary measures will be necessary if the opportunities provided by the Second Package of liberalization are to be realized. Most importantly, one should not forget about the safety of aircraft. In the United States, this aspect of deregulation has proved to be increasingly important in an expanding and competitive market for air transport services.<sup>263</sup>

#### IX. CONCLUSIONS

The Second Phase of liberalization of EC air transport has resulted in changes to the existing system in a number of respects. In the areas of market access, tariffs and capacities it constitutes considerable progress towards the creation of more competitive and more market oriented structures. State controls have been dismantled. These are all positive achievements. However, there is still a number of important issues that need to be solved. These issues include, but are not limited to, cabotage rights and reverse discrimination of domestic carriers as well as a technically updated air traffic infrastructure. Thus, a Third Package of air transport liberalization is needed if the Single European Market in the air transport sector is to be completed by January 1, 1993.

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258. See, e.g., COM(88) 577 final (Jan. 16, 1989).

259. See COM(89) 373 final (Sept. 8, 1989) at 11.

260. See COM(90) 100 final (May 22, 1990).

261. See, e.g., COM(90) 576 final (Jan. 30, 1989).

262. See COM(90) 576 final (Jan. 30, 1991).

263. See, e.g., Oster & Zorn, *Deregulation and Commuter Airline Safety*, 49 J. AIR L. & COM. 315 (1984). See also TRANSPORTATION SAFETY IN AN AGE OF DEREGULATION (L. Moses & I. Savage eds. 1989).