THE EFFECT OF AIRLINE ALLIANCES IN CIVIL AVIATION ON FAIR COMPETITION: A LEGAL ANALYSIS

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DECLARATION

I declare that this Mini-Dissertation which is hereby submitted for the award of Legum Magister (LLM) in International Law: Air, Space and Telecommunications at Faculty of Law, University of Pretoria, is my original work and it has not been previously submitted for the award of a degree at this or any other tertiary institution.

Signed

Itumeleng Mogashoa

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This work is dedicated to my twin sons, Lesedi and Lethabo, and the memory of my beloved late mother and grandfather.

With Gratitude,
Itumeleng Mogashoa

ABSTRACT

Since the late 1990s, global network airlines have enrolled in one of the three existing global alliances (GAL) namely the Sky-Team, Star Alliance and Oneworld. By 2011, the airlines in the alliance dominated over two-thirds of all international traffic. This research seeks to examine the legal and economic analysis, and consequent interpretation of airline alliances within civil aviation and how this affects fair competition. The evolution of global airline alliances is characterised by the analysis of their size, as well as the volume of the partnership and code-share agreement between the alliances. The findings of this study indicate that the aviation international regulatory framework recognises that these principles have thus far been enacted and applied throughout the legal and/or regulatory instruments. However, with the ever-expanding commercial aviation industry, the desire for business growth and regulatory framework are not always aligned. Airline alliances have proved to be cost-effective and efficient and enabled passengers to reach their designation on schedule.

Furthermore, they have also enhanced fair competition in the airline industry with the result that the market now operates more effectively. This research recommends that airline alliances should be allowed, but that competition regulatory authorities must be empowered to scrutinise them and closely monitor the conditions imposed on the alliance to ensure the protection of the smaller players in the industry and any anti-competitive effects mitigated adequately. The regulatory competition bodies should lay out policies and procedures encouraging fair competition in the industry by seeking to eliminate unfair and procedurally flawed barriers and consideration given to the fundamental benefits to be enjoyed by the businesses and stakeholders alike in the formation and existence of these alliances.

List of Acronyms

ASAs	Air Service Agreements
AA	American Airlines
BA	British Airways
COMESA	Common Market for Eastern & Southern Africa
DOT	Department of Transport
EAC	East African Community
GAL	Global Alliances
IASTA	International Air Service Transit Agreement
IATA	International Air Transport Agreement
IB	Iberia Airlines
ICAO	International Civil Aviation Organization
O&C	Ownership and control
SAA	South African Airways
SADC	South African Development Community
TCA	Turkish Competition Authority
TFEU	Treaty on the Functioning of the European Union
UK	United Kingdom
US	United States

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Chapter 1: Introduction

1.1 Background to the Study

The aviation world has progressed quickly since the emergence of the ninth edition of air transport half a decade ago.[1] These new developments relate to the access of market patterns by air transport that include competition, new attitudes to civil aviation security as well as safety. The developments also include those considerations associated with the transparency of investigation of accidents together with the investigation of cybersecurity cases in the area of airline financial liability. For instance, there are contemporary cases in the United States (US), including insurance of product as well as liability in the United Kingdom (UK), increasing significance concerning environmental concerns, and the rights and obligations of passengers.[2]

The civil aviation industry undoubtedly operates under stiff competition. The current aviation industry does not safeguard the dilemma and needs facing the operating companies but is instead a system of recognition that enforces rigid market competition. A few firms have dominated the current aviation industry for over 40 years; thus, any talk of industry expansion is illogical if not linked to the formation of airline alliances. Creating a more efficient aviation legal system is not just a significant milestone, but also a major step towards remedying the challenges within the industry. Attempts to restore solidity to the industry's stability has yielded some results. The main impediments to this achievement are some of the existing aviation laws in international agreements and national statutes of states. The existing laws have marginalised the states which have not entered into trade agreements or are not part of trading blocs at large, and, therefore, may necessitate a review of the international civil aviation regulatory framework. This step may be a more effective way to reverse the potentially unfair competition in the civil aviation market. The different states can use their state legislative arms to amend their laws to be certain to enable the formation of trading airline alliances through trade agreements. The current aviation principles and

[1] S Taylor & K Button (2002) 'International air transport and economic development' *The Journal of Air Transport Management* (6)4: 209–222.

[2] *Ibid.*

by-laws lack the required thresholds that give different states the freedom of ownership of airline companies in foreign states.

The proposed solutions for the challenges mentioned above often involve the use of existing trade blocs, either by the agreement or formation of additional trading blocs by different states. Economic strategists and aviation professionals emphasise the need for airline alliances to meet the required economies of scale and aviation industry transition. The term aircraft is not having an international valid definition in any main source of the international law. However, under the Annexes of the Chicago Convention as well as the national level a definition of aircraft is given. Annex 7 of the Chicago Convention defines an aircraft as *any machine that is able to derive support in the atmosphere from the reaction of the air other than the reactions of the air against the surface of the Earth.* There are several types of aircraft and some of the examples include aeroplanes, airships, rotorcraft, sailplanes, rescue parachutes, powered sailplanes and unmanned aircraft among others. For purposes of this research, we will focus on commercial civil aviation.

Fair Competition

The intervention by states in the air transport sector referred to as deregulation or liberalisation has substantially promoted fair competition among firms within the industry[3] and transnational investments in the airlines have taken place against a backdrop of multi-state ownership in other service industries.[4] The increased air transport rivalry has resulted in several airline carriers adopting strategic alliances as a way of attaining economies of scope as well as scale and to react to the demands of customers for international networks.[5] The three main airline alliances, Sky-Team, Oneworld, and Star Alliance, presently represent over 60% of the international market share,[6] measured in useable seat-kilometres for total scheduled passengers. Presently, the air transport industry competition is between airline carriers and the alliances. With increased

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[3] Button, Kenneth and Samantha Taylor "International Air Transportation and Economic Development" Journal of Air Transport Management 6, No. 4 (2000): 209-222.

[4] Kenneth Button "The Impact of US-EU "Open Skies" agreement on airline market Structure and Airline Networks", *Journal of Air Transport Management* 15, No. 2 (2009): 59 – 71, page 60.

[5] Footnote 4 above, 222.

[6] *Ibid*, page 219.

competition as well as integration, there is a greater risk of anti-competitive behaviour that includes abusing the dominant position as well as oligopoly practices.[7] As a means to maintain their national competitive position in a market that has become liberalised, certain governments may be tempted to support to their national airlines in ways that may deny airlines from other states equal opportunity to compete.

Ownership and Control in the Airline Transportation Sector

Despite the developments made internationally towards a more liberal regulatory system for the global air transport industry, the rules for Ownership and Control (O&C) for airlines are typically limited.[8] Most states still uphold the rules in the International Air Service Transit Agreement (IASTA) and the International Air Transport Agreement (IATA) that state that airlines of the contracting party have to be largely owned and controlled effectively by the member states or nationals of the party to a bilateral agreement. The IASTA and IATA entrench the rights of states to impose or withhold and revoke the working right of any foreign airline which is not owned or controlled by the designating state or its citizens.[9] It is argued that the justification for the state clause is because it provides a substantive link between the airline and the member state by which parties to the bilateral agreement are able to:

- Enforce the equality of the merits rule for the airlines included;
- Prevent a non-member country via its air carrier from accessing, indirectly, a benefit which is not reciprocated; and
- Identify the state responsible for the security and safety needs.

The nationality clause was viable in those periods when most carriers were owned by the state. In the last 20 years, liberalisation, globalisation as well as privatisation has transformed the airline industry significantly. An analysis by the International Civil Aviation Organisation (ICAO)[10] as

[7] *Ibid*, page 222.

[8] *Ibid*, page 211.

[9] Article I, section 5 of the Transit Agreement and Article I, section 6 of the International Air Transport Agreement.

[10] ICAO is the organisation established in terms of the Chicago Convention and tasked with the development of principles and techniques of international air navigation and to foster the planning and development of international air transport to ensure that civil aviation is safe, amongst other things.

well as reasonable state function in the last few years has affirmed that security together with safety can be protected without relying on the standard nationality clause. To help facilitate liberalisation, ICAO has designed extensive guidelines for member states. Reasonable progress is evident in state practice in terms of leniency on the enforcement of the regulations or in agreeing to airlines with foreign ownership, regarding legal limitations on ownership as well as control of air carriers. Consequently, bilateral agreements have altered extensively. The need to enable airlines to adjust to the changing international surroundings to enable states to participate more effectively in the global air transport signals for a change in the methods of approach.[11]

Air Alliances

Airline alliances are cooperative organisations between airlines which are unique in breadth, scope as well as detail. Airlines enter into a variety of cooperation agreements that range from those with restricted cooperation such as interline agreements or marketing placements, which provide interchangeable access to standard flyer plans and lounges to forms that are highly organised like metal-neutral income and sharing the united speculations. An important merit of an airline alliance is access to traffic as this would not be possible because of the limitations found in Air Service Agreements (ASAs) given state legislation. In systematically strategising the global alliances, this usually envisions a path framework that includes paths between airlines' countries of origin and others, and many times, routes crossing that state to another nation.[12] Nevertheless, air carriers must adhere to the route regulations created for their country with the pertinent bilateral ASA, which at times forestalls them from coming between point X and Y or travelling to point Z.

1.2 Paris Convention

The Convention for the Regulation of Aerial Navigation, known as the Paris Convention, is an important treaty signed on 13 October 1919 to control global aviation and give recognition to the sovereignty of member states.[13] Sovereignty remains a fundamental and firmly entrenched principle that underscores all negotiations in the aviation industry. The Paris Convention was drawn up following the Paris Peace Conference of 1919.

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[11] Footnote 5 above, page 64.

[12] *Ibid*, page 68.

[13] Article I of the Convention.

1.2.1 Convention on International Civil Aviation

The Convention on International Civil Aviation, also referred to as the Chicago Convention, was signed by about 52 countries in 1944. By 5 March 1947, the Convention was ratified by another 26 states which still had to sign the agreement. The Convention is a significant treaty in international civil aviation, and its purpose is to provide a global uniform standard and regulatory framework for air transport. The Convention was also instrumental in bringing about governance and control in the international aviation market and governed air routes, fares and frequency. It is regarded as a 'protectionist framework' in the civil aviation industry,[14] and this is illustrated by an analysis of some of the articles of the Convention that follows below. The Convention prescribes that the ICAO is tasked with the implementation of the terms of the Convention.

Article 1 reads –

> The contracting states recognize that every State has complete and exclusive sovereignty over the airspace above its territory.

This article underscores and upholds the spirit of the Paris Convention and is considered by the international airspace community to be the founding doctrine of sovereignty in the airspace. It forms the basis for the control of airlines by states.[15]

Article 6 reads thus -

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

Historically, this article forms the basis for the negotiation of the exchange of air traffic rights and other conditions of access utilising bilateral agreements.

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[14] R Vinhais '(2018) The Star Alliance: Case Analysis – My Business Musings' Mybusinessmusings.com – http://mybusinessmusings.com/?p=129 [accessed on 3 August 2017].

[15] S Ambrose (2018) 'Chapter 3 Economic Characteristics of the Airline Industry', Docplayer.Net, http://docplayer.net/4354407-Chapter3-economic-characteristics-of-the-airline-industry.html [accessed on 5 May 2018].

Article 7 that deals with the doctrine of cabotage reads –

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

Cabotage also refers to the 8th freedom of the degrees of freedom[16] in the airspace initially excluded from the Chicago Convention. Article 17 grants aircraft the nationality of the state in which they are registered, and this fortifies the doctrine of cabotage in that, each contracting state reserves its domestic routes. Bilateral agreements are constructed in such a way that the state allocates rights to carriers that are owned and controlled by the state or its citizens.

Article 96 of the Chicago Convention defines "Air service" as *"any scheduled air service performed by aircraft for the public transport of passengers, mail or cargo"*. In the same article, "International air service" is defined as, *"an air service which passes through the air space over the territory of more than one State"*. This definition becomes important in the context airline operators servicing passengers in more than one state.

1.2.2 International Air Services Transit Agreement

This agreement, also known as the 'Two Freedoms Agreement', was adopted and implemented in 1944. It grants member states the privilege to fly into each other's territories without landing[17] and the privilege to land for non-traffic purposes, such as refuelling and repairs.[18] The agreement set a foundation for the effective cooperation of the states in the bloc.

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[16] The eighth freedom is the right to carry passengers or cargo between two or more points in one foreign country.

[17] Article I, section 1(1).

[18] Article I, section 1(2).

1.2.3 International Air Transport Agreement

Commonly known as the global agreement of the liberalisation of international air transportation or the 'Five Freedoms Agreement', this agreement was also adopted in 1944 and affords scheduled flights additional privileges to:

- Fly across the other state's territory without landing;[19]
- Land in another state's territory for a non-traffic purpose;[20]
- To deliver mail, passengers and cargo taken on in the territory of the state whose nationality the aircraft possess;[21]
- Take on passengers, mail and cargo destined for the territory of the state whose nationality the aircraft possess;[22] and
- Take on passengers, mail and cargo destined for the territory of any other contracting state and the privilege to put down passengers, mail and cargo coming from such territory.[23]

These freedoms were designed to encourage political ties among the countries within the agreement. The 'Five Freedoms Agreement' has not been ratified by many states and is insignificant in today's international civil aviation sector.

1.3 Problem Statement

The liberalisation of civil aviation is encouraged. The reduction of state control in the air transport industry has fostered competition between air carriers.[24] Consequently, many carriers have been forced to consider combining their efforts on the market with other airlines to achieve financial targets and satisfy consumer demand for global access.[25] The liberalisation and deregulation of the airline business initiated the changes in the nature of competition in civil aviation. Notwithstanding, the dominant and established airline firms within the industry enjoy control in

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[19] Article I, section 1(1).
[20] Article I, section 1 (2).
[21] Article I, section 1(3).
[22] Article I, section 1(4)
[23] Article I, section 1(5).
[24] MG Lijesen, P Nijkamp & P Rietveld, (2002) 'Measuring competition in civil aviation' *Journal of Air Transport Management* (8)3: 190.
[25] *Ibid.*

the market, and as a result of their oligopoly practices, there is an increased risk of anti-competitive behaviour, particularly with regards to new entrants in the market.[26] The competition authorities are inclined to grant the alliances anti-trust (or anti-competitive) immunity on the basis that the consumer will benefit from the alliance. However, the consolidation of airline carriers can hamper the business of new entrants to the market and other low-cost carriers who choose not to join one of the three dominating alliances, or any alliance for that matter.

Due to the stiff competition and high costs experienced in the aviation industry, reforms such formation of trading alliances should help mitigate current industry aggression. Governments have an excellent opportunity to set a precedent of introducing major aviation alliances on a global scale. Trade alliances, like any other alliances, are vital and responsible for achieving the fundamental growth of the civil aviation industry while collaborating with other states to bring efficient operations into the airline industry. Strategic alliances are continually interacting with other states and are, at times, ascribed as the primary cause of unfair competition in the airline industry. Recognition of the impact of strategic alliances allows for exploration of current aviation operations and discussions on how best to amend them. Before the promulgation of certain aviation agreements, aviation laws were recognised as significant components of a more progressive nation and appropriate for the purposes of efficient operations in the industry. Although some countries are signatories to significant treaties, some states have failed to uphold the terms of these agreements with more developed nations.

Scholars hold the prevailing view that, in as much as airline alliances offer benefits for both the alliance carriers and the consumers, they potentially have anti-competitive effects. They argue that alliances pose anti-competitive strategies which make the industry to be volatile. It is, however, unclear to what extent competition authorities are substantively addressing the anti-competitive effects because the liberalisation of the airspace must balance with the business of running an airline. It will be argued that, in granting exemptions to airline carriers to form alliances, competition authorities must monitor and regulate such alliances to guard against anti-competitive behaviour.

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[26] *Ibid.*

1.4 Research Purpose

This study aims to demonstrate that through a process of critical legal analysis and consequent interpretation, airline alliances within the civil aviation industry may have an adverse impact on fair competition. This research focuses on primary sources of international law that have been published on the topic and other academic material by scholars on the subject of air transport. A recurring and important theme in the research is that states have their own national competition laws and authorities whereas some states may not have these regulations.

The researcher aims to express the views of different authorities and/or scholars concerning the advantages and disadvantages of being part of an alliance and the impact of such on fair competition. Even though airline alliances have made travel by air more convenient, a competitive market must be available to consumers, and this study is, therefore, relevant.

1.5 Justification

Article I of the Chicago Convention expressly and unambiguously entrenches the exclusive sovereignty of member states over its airspace.[27] Unless expressly granted, no state has the freedom of traffic in another state. Hsu and Shih define an airline alliance simply as "an agreement between two or more air carriers cooperating in a commercial relationship or jointly operating activities in various fields".[28] Competition law is essentially an area of law that is designed to enable both small and big businesses to compete equally and effectively in the market and remedy the unlawfulness of any trader's anti-competitive behaviour, *vis-à-vis* the trader's competitors in the market.[29]

Anti-competitive conduct or anti-trust, as referred to in some jurisdictions, can be exempted by competition authorities if certain conditions are satisfied. Exemptions are typically granted for a

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[27] Akermark, SS, "The Meaning of Airspace Sovereignty today – A Case Study on Demilitarisation and Functional Airspace Blocks, *Nordic Journal of Air Transport Management* 14, No. 3 (2008): 123 – 129, page 123.

[28] C-I Hsu & H-H Shih (2008) 'Small-world Network Theory in the Study of Network Connectivity and Efficiency of Complementary International Airline Alliances' *Journal of Air Transport Management* (14) 3: 125.

[29] M Neuhoff (Smit) et al (2006) *A Practical guide to the South African Competition Act* (2006) Lexis Nexis Butterworths, page 15.

certain period and not indefinitely. In consideration of granting exemptions, competition authorities consider factors such as, *inter alia*, the socioeconomic impacts and promotion of trade.

This study will analyse the manner in which airline carriers operate under the bilateral agreement systems and how modern-day airline alliances function and impact on fair competition and how this affects the passenger.

1.6 Research Objectives

This study is guided by the primary objective which is the implication of airline alliances on fair competition in the global market and an industry with a service used by millions of customers on a daily basis. The specific objectives are to:

1. Analyse the existing international aviation framework to understand the subsequent deregulation and liberalisation that took place in individual states.
2. Understand the reasons for airline carriers joining an alliance or choosing to operate without association to an alliance.
3. Critically analyse and understand the impact of airline alliances on fair competition and access to the market, notwithstanding the benefit it may have for the passenger.
4. To draw general conclusions about alliances in civil aviation and propose recommendations for the future of alliances.

1.7 Research Methodology

The study entails a qualitative review of the literature, including primary sources such as treaties, bilateral agreements, policies and legislation from individual states. Secondary sources, including reports from aviation, trade and competition-related institutions, relevant documents, working papers and journal articles were considered. This study was conducted through library resources and online research.

The approach of the study was descriptive, analytical, critical and prescriptive. The explanatory aspect of the study provides an overview of the international civil aviation regulatory framework and discussions pertaining to airline alliances. The critically analytical approach is used to evaluate

the O&C rules of civil aviation and how competition authorities and courts have treated airline alliances. Recommendations make use of the prescriptive approach.

1.8 Outline of Chapters

This chapter sets out the foundation of the study by discussing the introductory elements which include the background to the study, problem statement, research questions, objectives and justification for the study and research methodology.

Chapter 2 traces the founding treaties and agreements used in international civil aviation, and bilateral agreements leading up to the liberalisation of the skies. The civil aviation regulatory framework, the policies on deregulation of civil aviation and history of bilateral aviation agreements are also discussed.

Chapter 3 critically analyses the O&C requirements that are used in civil aviation to limit access to the market or protect national carriers.

Chapter 4 provides a detailed discussion about airline alliances – the categories of cooperation agreements, and the advantages and disadvantages of airline alliances.

Chapter 5 examines the treatment of airline alliances by competition authorities in specific regions and the instruments used in consideration of antitrust applications.

Chapter 6 investigates airline alliances from a South African perspective, mainly the participation of the state carrier in one of the global alliances.

Chapter 7 provides a summary of the findings of the study, draws conclusions and makes recommendations.

Chapter 2: A Consideration of the Aviation Regulatory Framework

2.1 The International Legal Regulatory Framework of Air Transportation

This section discusses the principles and rules that are used and control international civil aviation in general. The aviation industry, due to considerations for safety and security, is highly regulated in all jurisdictions of the world irrespective of geographical location.

Several international agreements were agreed to and signed by Member States to guide their airline operations within the international airline transport industry. These agreements include the Paris Convention, Chicago Convention, International Air Service Transport Agreement (IASTA) and the International Air Transport Agreement (IATA).

2.1.1 Chicago Convention

The Chicago Convention was enacted in order to regulate as well as coordinate international air travel. The Council of ICAO assumes the measures as well as the practices recommended regarding navigation within the air, the airport infrastructure, inspection of flights, prevention of unlawful interference, as well as facilitation of cross-border processes for international civil aviation.[30] The Chicago Convention contains rules and regulations concerning the airspace, registration of aircraft as well as safety and details the rights of the signatories with respect to the air travel. Fifty-two states signed this Convention. Moreover, the Convention also provided for Five Freedoms in the initial plan and later expanded these freedoms increasing them to nine. These freedoms provide states with the autonomy to execute air transport flights, which include cargo, passenger carriage and mail, within, into or across the airspace of other countries' territory.[31]

The main objectives of the Chicago Convention can be summarised accordingly:

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[30] RJ Greene (2014) 'Effective Rewards for Strategies for Mergers, Acquisitions and Joint Ventures/Alliances' *Compensation & Benefits Review* (46)5-6: 290.

[31] H Ito & D Lee (2007) 'Domestic code sharing, alliances, and airfares in the US airline industry' *The Journal of Law and Economics* (50)2: 360.

- Enhance the development as well as planning of global air transport to make sure it is safe, as well as orderly development at both domestic and international levels;
- Enhance efficient civil aviation operations among the states in the Convention;
- Promote the aircraft art and design as well as operations for reasons of peaceful flying;
- Foster the growth of airways, airports and air facilities for navigation for worldwide civil aviation;
- Fulfil the needs of the international consumer for efficient, safe, regular and economical air transport;
- To curb unfair competition in the airline industry and sustain economies of scale;
- To ensure that the continued rights of member states;
- Fostering flight safety in the global navigation of the airspace; and
- Enhance the features of all international civil aeronautics.

The most significant aspect to note about the Chicago Convention is that it unambiguously entrenches the sovereignty of airspace above the territory of every country; therefore, it necessitates the development of the bilateral agreement system to determine the rights of states in areas such as capacity, traffic rights and frequency of services. [32]

2.2 Bilateral Agreements

In circumstances where states cannot enter into a suitable multilateral treaty governing scheduled flights, the requirements are that they enter into bilateral air transport agreements[33] for the operation of scheduled air services. These bilateral agreements can take the form of executive agreements, exchange of diplomatic notes or treaties.[34] Bilateral agreements have been in use for as long as flights have existed and until now, most scheduled flights are regulated by signed bilateral agreement among states. The ICAO does not prescribe the form for treaties or bilateral agreements but creates a framework and an environment that enables the operation of a safe commercial, civil aviation. With the advance of aviation technology, states had to find ways to

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[32] K. Bohmann (2001) 'The Ownership and Control Requirements in US and European Union Air Law and US Maritime Law- Policy; Consideration; Comparison *Journal of Air Law and Commerce*, 66: 689.
[33] Also referred to as ASAs, bilaterals or Air Transport Agreements.
[34] Footnote, 47 above.

conduct business diplomatically. Swinnen provides an example of a bilateral agreement as follows:

> ...on the route from Chicago to Frankfurt, the US carrier would fly from Germany under the Fourth Freedom. If the route, pursuant to the bilateral agreement, allows continuing service to Berlin, then the carrier flies under the Fourth Freedom and "beyond point" rights. "Beyond point" connotes an extension to a point beyond the point of entry in the same country. If the carrier can pick up additional traffic and fly to a third country, it would do so under the Fifth Freedom right. If it can pick up traffic on the inland leg, it also benefits from the limited cabotage rights. Any such right must be granted in the bilateral agreement.[35]

The earlier bilateral agreements were modelled on the Bermuda Agreement,[36] which served as the model for most countries negotiating bilateral air transport agreements. A general concept of bilateral agreements is that only designated carriers, as agreed to by the contracting party, can exercise the air traffic rights granted in the agreement. Most importantly, airlines must have a nationality to use the rights assigned to the contracting state[37] that conform to the provisions of the IASTA.[38] This is a critical consideration with regards to airline alliances as it means that a contracting party to a traditional bilateral agreement cannot alienate a majority of its shares to a foreign carrier and still qualify as a designated carrier. Furthermore, it cannot purchase the majority shares in a foreign airline and exploit the traffic rights of the acquired carrier. Bilateral agreements also detail matters of airfares, seating, frequency and capacity, all of which have a significant bearing on the issue of a competitive market in the air transportation sector. Before deregulation and liberalisation of the aviation industry, national governments typically used bilateral agreements to give advantage to their national carriers in the international market'.[39] For example, a traditional bilateral agreement clause in the ICAO Template Air Service Agreement states that:

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[35] MJB Swinnen (1997) 'Opportunity for Trans-Atlantic Civil Aviation: From Open Skies to Open *Markets'* 63 *Journal for Air Law and Commerce*, 249.

[36] *Ibid*, page 693. This was the Agreement concluded between the Governments of the United States and the United Kingdom, relating to air services between their territories.

[37] Footnote 47 above, page 693.

[38] International Air Services Transit Agreement, Dec. 7, 1944 Art. I, section 5, 84 U.N.T.S . 389, 3945, reserves the right of a contracting state to grant traffic rights if it is not satisfied that substantial ownership and control of an airline is vested in the nationals of a contracting State.

2.* On receipt of such a designation, and on application from the designated airline, in the form and manner prescribed for operating authorization [and technical permission], each Party shall grant the appropriate operating authorization with minimum procedural delay, provided that:

a) substantial ownership and effective control are vested in the Party designating the airline, nationals of that Party, or both;[40]

The bilateral system is criticised for being anti-competitive in the global operating systems of the air transport industry and often used as a 'protectionist' tool by governments for national airlines while denying emerging airlines the opportunity to access the civil aviation market. Notwithstanding this criticism, the practice of entering into bilateral agreements with the nationality and ownership clause remains in effect.[41]

2.2.1 Deregulation and 'Liberalisation'

The US enacted the Airline Deregulation Act in 1978. The purpose of this piece of legislation was to bring about regulatory reform of the domestic air transport industry by opening it up to the market and removing government control. Deregulation, also referred to as 'liberalisation', changed the aviation industry into a modern business and fostered fair competition within the aviation industry. It resulted in successful domestic deregulation, and the US approached the Netherlands and the UK to put similar agreements in place, as restrictive bilateral agreements still largely governed international aviation services. This ushered a new era of open-skies agreements. The Netherlands was the first country to enter into an Open-Skies Agreement with the US, and this prompted other Asian and European States to re-negotiate their bilateral agreements with the US.[42]

The impact of open-skies agreements pioneered by the US on international air services removed all the complex language and rules found in the typical bilateral agreements. These were replaced with plain language granting rights to the airlines of two countries to fly where and when they desired between the two states (and beyond) and fixed their fares accordingly. This change resulted in a reduction in airfares and lower barriers for entry by new market players and fostered a

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[40]ICAO Template Air Services Agreement, Appendix 5, Art. 3.

[41] Footnote 47 above, page 694.

[42] Air Service Agreement Liberalisation and Airline Alliances, International Transport Forum, OECD Report, page 14.

competitive civil aviation market. The US-Netherlands agreement was a major development for both de-regulation of the market and creation of a significant alliance agreements between airlines from different countries. This, in turn, created the link between airline alliances and bilateral air services agreements.[43]

A typical Open-Skies Agreement contains articles found in a traditional bilateral agreement.[44] Despite the success of the Open-Skies Agreement model, the US has not completely liberalised its international civil aviation and retains the foreign investment and cabotage restrictions. Admittedly, the liberalisation of bilateral agreements can be viewed as a progressive and sound development for air transportation.

2.3 Conclusion

The founding treaty for the regulation of air transport is premised on the sovereignty of the airspace and guided the development and growth of aerial navigation and all related matters. Although there are strict regulations in place, airlines are also commercial enterprises, and this necessitated entering into bilateral agreements. Liberal governments have, however, in pursuit of widening the network, moved towards the Open-Skies Agreement model to manoeuvre around the limitations of the Convention, although being mindful of the protection afforded by the regulatory framework. Domestic policies and statutes will be informed and guided by international instruments.

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[43] *Ibid*.

[44] For example, articles in Open-Skies Agreements cover aspects such as, Authorisation, Revocation of Authorisation, Application of Laws, Safety, Fair Competition, to name but a few.

Chapter 3: Ownership and Control Requirements in Air Services Agreements

3.1 Introduction

An area of critical importance for alliances and Air Services Agreements are the ownership and control requirements, often captured in the articles on Definitions, Authorisation and/or Revocation of Authorisation. The requirements of O&C have been a requirement in air transportation in order to be designated to operate and provider international services in accordance with ASAs.[45] As briefly discussed in the preceding chapter, the Chicago Convention was adopted together with the Air Transport and Transit Agreements with the purpose of regulating scheduled air services and contains restrictions on ownership and control in commercial aviation, which have prompted states and private commercial airlines to form airline alliances to foster business and growth. Bohmann explains the ownership and control rules thus -

> ...as general rule, it is impossible for an air carrier under the currently prevailing bilateral regime to sell a majority of its shares to a foreign carrier and still qualify as a designated air carrier of its state, or to buy a majority of a foreign and to exploit the traffic rights of the acquired carrier. The nationality clause establishes a link between the air carrier using international commercial rights and the state designating these rights, thereby implementing a balance of benefits and preventing a situation of non-reciprocal benefits.[46]

The requirement for substantial ownership and effective control is found in both conventional bilateral and open-skies agreements.

3.2 The Transit and Transport Agreements

Article I, section 5 of the Transit Agreement prescribes that each state within the agreement has the right to revoke and withhold a certificate issued to any enterprise where it is not satisfied that substantial ownership and control is vested with the nationals of the contracting state. The Transport Agreement also has the same provision.[47] Therefore, it follows that the nationality of an airline is relevant for the exchange of scheduled air services, which can be linked back to Article

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[45] de Borca, Hubert, Mieclecka Riga, Marta and Subocs, Anatoly, *Chapter 15 Transport*, in *The EU law of Competition*, edited by Faull and Nikpay, Oxford University Press, Oxford 2014, page 1797.

[46] Footnote 47 above, page 689.

[47] Art. I, section 6.

18 of the Convention. These clauses still form part of modern-day bilateral agreements between states. However, neither of these agreements articulate the criteria and/or manner for the determination of substantial ownership and effective control. States continue to have the discretion to determine the level of ownership they deem necessary to qualify an airline for corporate citizenship.

3.3 Justification of Substantial Ownership and the Effective Control Requirement

According to Van Fenema, these two requirements are designed for the economic protection of states and national pride.[48] In other words, states want to ensure that no foreign airlines benefit more from domestic state resources and to uphold the state flag. These requirements provide a convenient nexus between the carrier and the grantor state by which signatories to the agreement can prevent a non-party state from indirectly accessing an unreciprocated 'free rider' benefit through its airline and identifies the state to be held accountable for safety and security.[49] The argument around the 'free rider' is further underscored by the fact that ICAO has a framework of standards and inspections aimed at enforcing globally uniform and acceptable standards of safety in that these standards may not be applied in the same way in some countries, leading to 'flags of convenience'[50] in the aviation industry.[51] There have, however, been calls to liberalise the control and ownership requirement, but it has been difficult to reach a broad consensus on the matter.

Another justification for the 'substantial ownership and effective control' requirement is the consideration of national security, which is not insignificant. It can be argued that national security considerations are borne from the fear that rights granted to cooperating states may fall into the hands of enemy states, without the granting state having an opportunity to intervene.[52] Civil

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[48] HP van Fenema (1998) 'Ownership restrictions: consequences and steps to be taken' *Air & Space Law*, Vol XXIII, 2: 63.

[49] R Bartsch, J Coyne & K Gray (2016) Global Harmonization: International Civil Aviation Organization' in *Drones Society*, 70.

[50] 'Flags of convenience' refers to a situation where carriers seek out or are undercut by operators based in countries with lower regulatory standards.

[51] Civil Aviation Authority 'Ownership and Control Liberalisation', a discussion paper, CAP 769 (October 2016), Ch 4, p.2, https://publicapps.caa.co.uk/docs/33/CAP769.pdf [accessed on 6 June 2017].

[52] NM Matte (1982) 'Annals of Air and Space Law' *The American Journal of International Law*, 76(3): 707, doi: 10.2307/2200847.

aviation has gone through liberalisation, privatisation and globalisation, all of which have changed the face of the airline industry.

3.3.1 Determination of Substantial Ownership

Substantial ownership is determined by placing numerical restrictions on ownership by foreign nationals on the voting equity of airlines and looking at the prescripts of national legislation. This makes the ownership requirement relatively easy to ascertain.

Notwithstanding the call to liberalise national control and ownership regulations, most bilateral agreements still retain the principle of substantial or majority ownership in their designation clauses.[53] Bilateral agreements stipulate the ownership requirement in their designation clauses and ICAO has correctly argued that this inflexible position pays no respect to the national laws of other countries and may lead to conflicts between the national laws of the parties to the agreements.[54]

For example, the then Civil Aeronautics Board (CAB) of the US approved an agreement in the *Page Avjet*[55] matter in terms of which non-US citizens can own about nine per cent of total shares of a US carrier and exercise influence through voting.[56] In this instance, the CAB concluded that the non-voting shareholder had the right to influence several critical decisions of the company. The CAB approved the agreement on condition that it has a buy-out clause in terms of which the voting shareholders could purchase the non-voting shares back if the shareholder blocked a corporate action.[57]

The issue of substantial ownership is guided by the national laws of the designating state, and such determination is undertaken on a case-by-case basis approach. The intention behind the substantial

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[53] MG Lijesen, P Nijkamp & P Rietveld (2002) 'Measuring competition in civil aviation' *Journal of Air Transport Management* 8(3): 191.
[54] *Ibid.*
[55] Page Avjet, Citizenship, DOT Order 83-7-5, 102, C.A.B. 488.
[56] This case involved a foreign investor who purchased 100% of the non-voting shares and thus had the right to vote on matters of company mergers, acquisitions, consolidations and the liquidation of the company.
[57] Footnote 54 above, 492.

ownership rule is a matter of national pride and economic protection and to mitigate competition against a state's air carriers.

3.3.2 The Determination of Control

The determination of actual control is mostly a matter of national interpretation, as opposed to it being informed by aviation law in the strict sense. As mentioned above, it is crucial to note that while these principles of O&C exist and are entrenched in civil aviation transactions, albeit to different degrees, neither the Chicago Convention nor any other regulatory international agreements definitively articulate airline O&C. Consequently, states possess the discretion to determine the limits of foreign control.

In 1989, the US Department of Transport was asked to review the merger between Northwest Airlines and Wings Holdings, Inc.[58] Even though both companies were controlled and operated in the US, the issue of citizenship came to the fore because the merger's largest equity holder, who held 56.74 per cent of the shares, was Dutch company, KLM Inc, a foreign airline. This shareholding gave KLM substantial power with regards to decisions related to the stock of the company.[59] In its discussion of the citizenship test, the DOT referred to the *Daetwyler* decision favourably and stated that the control test 'has traditionally been a complex matter in past cases.'[60] However, it refrained from articulating specific factors to determine the existence of control and instead stated that such an analysis 'has always necessarily been on a case-by-case basis, as there a myriad potential avenues to control'.[61] In this case, the DOT identified three specific factors that made it conclude that this merger resulted in an entity that was not a US citizen which can be summarised as:

> First the equity interest in the new company held by KLM. Although a majority of KLM's interest was held in nonvoting stock, the DOT concluded that it "represent[ed] a genuine ownership interest" and therefore, significantly increased KLM's incentive to participate in Northwest's business decision. Second, the corporate

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[58] *In re of the Acquisition Northwest Airlines by Wings Holdings, Inc.*, 1989 WL 256026, *1 (D.O.T.) (1989).

[59] For example, KLM's position has an equity shareholder gave it the ability to prevent issuance for liquidation, dissolution or dividends, as well as the ability to block amendments to the certificates of incorporation that allow for changes in stock designation or the special rights of preferred stock holders.

[60] *Ibid* at 3.

[61] *Ibid.*

> structure of the new company, according to DOT, would have allowed KLM to exert influence even without voting rights. Finally, the DOT pointed to the fact that KLM was an actual competitor with Northwest in various markets and had stated an intention to become involved in the decisions of the new corporation. Taken together, these factors resulted in a finding that, as presented at the time, Wings Holdings, Inc., was not a US citizen as defined by the Federal Aviation Act.[62]

Although there is no fixed list of factors to be utilised in the determination of control, as it is a subjective enquiry, some factors that may be considered are equity ownership, control over the voting rights of stock, business and personal relationships, veto rights, competitive status, and equity/debt agreements and other corporate transactions.

3.4 The Link Between Air Services Agreements and Alliances

It is necessary to understand the importance of the O&C requirements in the context of the formation of airline alliances or how they influence their formation. Generally, bilateral agreements do not contain provisions that authorise the creation of airline alliances. States empower their designated competition authorities to review applications for airline alliances in line with their national competition laws. It is the restrictive provisions found in bilateral agreements that prompt the formation of airline alliances such as:

- The designation of a limited number of carriers to provide services on international routes;
- The restriction by states of changes in frequency and seat capacity or agreements on the airfare to be charged on international routes;
- Countries requiring that carriers providing services under a bilateral agreement are owned and controlled by nationals of the country in which the airline resides; and
- States may limit access to certain airports to certain foreign carriers.[63]

The features mentioned above pose a barrier to competitive entry to the commercial aviation market and expansion in international markets. In the review of an airline alliance, competition

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[62] TB Tatelman, 'Legal Developments in International Civil Aviation', Library of Congress Washington D.C, Report for Congress, Congressional Research Service, updated August 25, 2006-9 [https://fas.org/sgp/crs/misc/RL33255.pdf] [accessed on 15 October 2018].
[63] Footnote 42 above, page 33.

authorities will weigh the pro-competitive impact against the anti-competitive effects. In the airline market sector, the two chief barriers to entry have been constraints on rights to operate commercially as set out in bilateral agreements and limited access to the airports. The liberalised approach to international air services has since fostered increased competition in the international air services market and prompted the formation of airline alliances.

3.5 ICAO Policies in the Field of Air Transport

In addition to the relevant treaties that are applied by Contracting States in air transport, the ICAO Assembly has adopted various resolutions addressing air transport related matters, ranging from, to name but a few, economic regulation of air transport, taxation, airports and navigation services and aviation safety and security. The Assembly Resolution A39-15[64] has established a policy position on air carrier ownership and control which is considered below.

3.5.1 Air Carrier Ownership and Control

Appendix A to Statement A39-15 of the Resolution of the Assembly states puts forth the following policy position –

> *Whereas* the strict application of the criterion of substantial ownership and effective control for the authorization of an airline to exercise route and other air transport rights could deny many States a fair and equal opportunity to operate international air services and to optimize the benefits to be derived therefrom;
>
> *Whereas* airline designation and authorization for market access should be liberalized at each States's pace and discretion progressively, flexibly and with effective regulatory control in particular regarding safety and security;
>
> *Whereas* the broadening or the flexible application of the criteria for airline designation and authorization could help create an operating environment in which international air transport may develop and flourish in a stable, efficient and economical manner, and contribute to the participation objectives of States in the liberalization process, without prejudice to States' obligations for aviation safety and security;

[64] Resolutions adopted by the Assembly, ICAO Assembly-39th Session, Montreal, 27 September – 6 October 2016.

Whereas the realization of developmental objectives among states is increasingly being promoted by cooperative arrangements in the form of regional economic groupings and functional cooperation symbolic of the affinity and community of interest;[65]

The Assembly:

1. *Urges* Member States to continue to liberalize air carrier ownership and control, according to needs and circumstances, through various existing measures such as waivers of ownership and control restrictions in bilateral air services agreements or designation provisions recognizing the concept of community of interest within regional or subregional groupings, and those recommended by ICAO;

...

3. *Urges* Member States to recognize the concept of community of interest within regional or subregional economic groupings as a valid basis for the designation by one State or States of an airline of another State or States within the same regional economic grouping where such airline is substantially owned and effectively controlled by such other State or States or its or their nationals;"[66]

This ICAO Resolution takes into cognisance the O&C requirements in the expansion of air transport networks and, the impact on competition in the market and encourages liberalisation thereof, in the interest of the international aviation community but importantly, the Resolution states that aviation safety and security must not be compromised in the pursuit of this objective. This Resolution gives due regard to the fact that states and airline carriers are moving towards the model of operation of airline alliances, in pursuit of expanding carrier networks. The O&C requirements serve the noble purpose of protecting national pride but may practically inhibit the growth of airline carriers.

3.6 Conclusion

The O&C requirements demonstrate that states are wary of foreign investor control over airlines. Ultimately, and for valid reasons of national security and economic security, among others, states possess the overarching authority of sovereignty in making determinations of O&C. Due to the risks associated with the liberalisation of the O&C requirements, contracting states will determine the degree and pace of liberalisation, if they wish to do same. However, in instances where these requirements impede business growth, states may be able overcome the limitations to business expansion posed by the O&C requirements by entering into airline alliances

[65] Section II, page 55.
[66] Ibid, page 56.

Chapter 4: Airline Alliances

4.1 Introduction

This chapter is guided by the study objective which is to examine the main reason for the formation of strategic or tactical airline alliances, and prevailing trends and other ancillary issues of importance to airline alliances and to foster an understanding of this popular business practice in the civil aviation industry. Trade alliances, like any other alliances, are vital and responsible for achieving industry growth while collaborating with other states to create efficient operations in the airline industry. Strategic alliances continually interacting with other states are often ascribed as the leading cause of unfair competition in the airline industry. The current conditions in global aviation have necessitated the need to form alliances in order to survive in the industry.

4.2 General Overview of Airline Alliances

With the introduction and implementation of liberalisation of air transportation, the airline business model has been remodelled to take advantage of the benefits associated to deregulation, predicated on a 'from anywhere to anywhere' consumer proposition.[67] Airline alliances are cooperative agreements between airlines that are unique in breadth and scope as well as detail. Airlines can enter into a larger variety of cooperation agreements ranging from those with restricted cooperation like interline agreements or marketing placements that provide interchangeable access to standard flyer plans and lounges to highly-organised systems of cooperation like metal-neutral income sharing the united speculations. Significant merit derived from an alliance is the access to a broader traffic network which would not be possible because of the limitations inherent in bilateral ASAs or domestic laws that sometimes prohibit them from going between point A and B, or even to point C.[68] Therefore, the significance of an airline alliance is that it enables an airline to overcome these limitations and access other networks of air traffic. Essentially, as a result of limitations on ownership contained in ASAs which require that airlines are citizens of the contracting states, alliances are principally a response to these restrictions in ASAs.

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[67] Hacket, G.T. (1992) *Liberalisation of Air Transport in the EEC and its Implication for non-EEC European Countries*, pg 24.

[68] Oum, T.H, Park, J.H, & Zhang, A. (2000) *Globalization and Strategic Alliances: the case of the airline industry.* Amsterdam: Pergamon, pg 217.

It is prudent for the airline industry to create such alliances in order to address the diverse needs and preferences of the passengers and maximise business profits by code-sharing with other airlines. Airlines may enter into tactical or strategic alliances. Tactical alliances often involve two or more carriers and are structured in such a way to remedy specific shortcomings in individual carrier networks by providing enhanced connectivity between the networks of the carriers. However, a strategic alliance is a broader and more comprehensive form of cooperation between several carriers working to establish global joint networks.[69] Any alliance or joint venture established will be subjected to the approval of the competition authority responsible in such jurisdiction if any, and this issue of competition in airline alliances will be discussed in the chapters to follow. Currently, there are three major global alliances: Sky-Team, the Star Alliance and Oneworld.

4.2.1 The economic benefits and impact of airline carrier alliances

Typically, airlines that choose to be members entering into an alliance do so for economic and operational reasons. In such an arrangement, the pool of assets and revenue are substantial. These alliances enable airline carriers to sell more tickets on the flights of their alliance members. Also, it offers wider access for customers to different destinations and boosts the overall revenue of these firms within the alliance and tourism levels of the alliance partners. The alliance brand will enjoy more promotion and recognition than the individual brand of the alliance partner. The ability to promote the individual brand of the carrier can assist smaller alliance members with limited marketing resources.[70]

4.2.2 The benefits of airline cooperation for consumers

One of the most significant benefits of airline alliances for the passenger is lower fares, particularly for passengers travelling to international destinations. The cooperation between airline alliance partners can help improve and increase flight schedules by shortening connecting intervals.[71] The allied airlines, through the formation of alliances, can effectively manage departure and arrival times. Alliances can also boost and improve customer service as the allied partners can manage

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[69] Gilroy, B.M (1993) Networking in multinational Enterprises: The Importance of Strategic Alliances. Columbia (Critical Issues Facing the Multinational Enterprise), S.C: University of South Carolina Press, pg 220.
[70] *Ibid*, pg 231.
[71] *Ibid.*

their operation jointly. Consumers also enjoy the related benefits of ticketing and luggage checking-in that are made easier through the agreements. Alliances reduce long passenger queues as a result of the adoption of check-in facilities speeding up the check-in process at the airport. Alliances offer online booking which is a convenient way for customers to book their flight tickets without necessarily visiting the airport. Global and multilateral alliances reward loyal customers with travel benefits.

4.2 Conclusion

It can be argued that airline cooperation assists carriers in improving their competitiveness and grants them access to a wide range of networks and improves profits.[72] Airlines enter and participate in alliances for various reasons depending on their objective and targeted market. One of the critical hurdles to cross-border mergers in air transport are the restrictions found in bilateral ASAs concerning ownership.

To mitigate the economic effects of these limitations, the formation of strategic alliances encourages productive and efficient aviation industry operations. The current aviation industry is frequently evolving as a result of globalisation and the expected consequences of business development. Therefore, there is a significant need to construct and develop strategic alliances in the industry. Existing firms can enjoy economies of scale as well as extend far-reaching services to be enjoyed by the passengers as a result of the number of different firms in the market. The importance of these alliances should not be overlooked as their role is of great significance. Notwithstanding the benefits highlighted above, some critics have expressed concerns that alliances may undermine the smaller airlines that are not part of an alliance and prevent them from competing in the international aviation market and increase the risk of allied carriers engaging in predatory conduct to eliminate smaller airlines.

The existence of strategic and tactical alliances which protect the government and the consumer from being exploited by unfair competition in the airline is an excellent step towards achieving an

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[72] Belobaba, P, Odoni A.R, Barnhart, C (2015) *The Global Airline Industry* (2nd Ed), Massachusetts Institute of Technology, USA, pg. 430.

improved airline industry.[73] States should undoubtedly implement such strategic moves, as they have a vital role in achieving sustainable aviation industrial growth. Some of the strategies focus on the formation of long-term agreements between different states.

[73] Footnote 69 above, pg 235.

Chapter 5: The Impact of Global Airline Alliances on Competition

5.1 Introduction

The reduction of state control within the air transport industry has fostered competition between airline carriers and the global alliances. The three global alliances – Star Alliance, Sky-Team and Oneworld – dominate 60 per cent of the total market share. The competition in the airline industry has changed from individual airlines to global alliances, taking into consideration the accessibility to the market by smaller or new entrants. Members of global alliances do not just join an alliance but have to go through a legal process in their respective jurisdictions to be granted antitrust immunity, considering the pro-competitive and anti-competitive effects of joining an alliance. This chapter will broadly discuss the principles of competition law and its impact on fair competition *vis-à-vis* global airline alliances and non-alliance airlines or new entrants to the market and how competition authorities, through their regulatory regime, deal with these alliances.

Competition law is a law created to control and promote competition in any one market and regulates anti-competitive behaviour by entities. In general, competition law focuses on three main aspects: prevention of abuse of a dominant entity, control of anti-competitive mergers and making rulings against mergers and acquisitions.[74]

An alliance structure tends to be monopolistic, duopolistic or oligopolistic.[75] It can be argued that the airline industry can be defined as an oligopoly, meaning it is an industry with few firms that offers almost similar services or differentiated products. The typical characteristics inherent in airline alliances reflective of oligopolistic behaviour are:

- High barriers to entry;
- Few sellers in the markets;
- The firms enjoy substantial economies of scale;

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[74] D Merican: the Malaysian DJ Blogger 'Competition law and the airline industry' https://dinmerican.wordpresss.com/2011/10/31/34476 [accessed on 2016/06/13].
[75] P Oliver, (2005) 'The concept of "Abuse" of a Dominant Position Under Article 82 EC: Recent developments in Relation to Pricing' *European Competition Journal* 1(2): 315.

- The firms can grow through merger and acquisitions;
- The markets experience price rigidity and non-price competition; and
- The market is dictated by transparency and price collusion and the mutual dependence of airline firms on one another.[76]

5.2 Key Issues of Competition with Reviewing and Approving Airline Alliances

It goes without saying that the mere establishment of an airline alliance is contrary to the purpose of competition law. Competition authorities must always seriously consider the potential anti-competitive effects of an airline alliance where the allied carriers share substantial overlaps in their networks. In cooperative alliance structures where carriers jointly fix pricing, scheduling, seat capacity, among other things, this can eliminate competition between them resulting in domination in the market. If there are barriers to entry for other airlines to that market, this may result in the allied carriers abusing their dominant position and charging higher fares.[77]

Alliances may reduce competition in hub-to-hub markets and international markets, where the allied carriers are direct competitors (also referred to as 'horizontal' effects). Another concern regarding alliances in international markets is that they restrict access to domestic traffic for non-alliance carriers at hub airports dominated by alliance firms (referred to as 'vertical' effects). If alliance corporations limit or eliminate access to feeder traffic to non-allied airlines at their hubs, then the profitability of the operations of competitors on international routes from those hubs may be negatively affected.

Carriers seeking to enter into an alliance, whatever the form and extent of cooperation, will seek antitrust immunity or exemption from the competition laws as such cooperation is likely to be in contravention of the competition laws. Airlines are likely to seek antitrust immunity first before concluding on an alliance agreement because they would face challenges from competition authorities and other airlines. Competition authorities will consider the merits of each case to

[76] *Ibid*, page 339.
[77] Footnote 42 above, page 47.

determine the potential impact on competition on the market.[78] If the positive impact outweighs the negative impacts, then the alliance will be approved and exempted.

5.2.1 Typical Grounds Advanced for the Formation Alliances

Applicants need to argue to the regulatory authorities as to the desirability of approving the alliance and exempt the firm from the provisions of the competition statutes. This is not an exhaustive list on the grounds that may be put forth but are the key reasons:

Restrictive Bilateral Air Service Agreements

It has been already articulated in this research that the ownership requirement inherent in traditional bilateral ASAs is one of the primary reasons for the formation of airline alliances; carriers must be owned and controlled by the nationals of the country of origin of the airline. The Paris Convention founded the sovereignty of states over their airspace, and he Chicago Convention confirmed this principle. Most states enter into bilateral agreements to facilitate commercial air services which establish the terms and conditions for access to routes for the respective national carriers. Air Service Agreements are also, in effect, trade agreements and it is an important consideration for signatory states to safeguard their national interests. Therefore, bilateral agreements operate from a premise of reciprocity. These elements in bilateral ASAs may present barriers to entry and expansion of services:

- Designation of a limited number of carriers to the service route;
- Restrictions on frequency and seat capacity offered on the route;
- Restrictions on airfares that carriers can charge on the route; and
- Restrictions on permitted cities or permitted routes.[79]

Considerations of Efficiency

Carriers will often argue that the pooling of activities will result in cost savings and lower fares, and other efficiencies to benefit the consumer. Carriers participating in international markets argue

[78] *Ibid.*
[79] *Ibid*, page 48.

that connecting passengers enjoy significant benefits from immunised alliances.[80] Passengers are likely to derive benefits from alliances that are fully integrated and coordinated under a metal-neutral joint venture.[81] For example, in 2009, when American Airlines (AA), British Airways (BA) and Iberia (IB) applied to form a transatlantic joint venture, they argued that full integration of carrier activities would provide an incentive to carriers to code-share on all transatlantic routes including beyond segments.[82] If a fully integrated joint venture is not approved, then carriers might be inclined to exclude specific lucrative routes from the code-sharing arrangement due to the risk of traffic diversion. In deciding whether or not to grant immunity, efficiency will be determined by referring to the individual applicable competition laws of the affected states.

5.3 The Importance of Competition

In general terms, competition in the market means that merchants are striving independently for the patronage of consumers to maximise profit or other business objectives.[83] Essentially, consumers prefer purchasing products or goods at a price that maximise their actual benefits whereas a seller will sell at a price to maximise his profits.[84] Competition is therefore essential to make the service provider offer services at a lower price. Competition is the critical driver of performance and innovation in any industry and benefits everyone, both in the industry as well as the final consumer. It benefits the consumer by enabling him to choose from an array of goods and services offered by different firms at competitive prices. The competition also encourages the adoption of more innovative concepts as the major companies evolve with new and strategic ideas to meet the diverse needs and preferences of their consumers to make the company flourish in the market in which it is operating.

A competitive market fosters fair prices as well as diverse services offered by different firms in the market to the consumer. Competition is essential in making firms more accountable in offering

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[80] W Gillespie & IM Richard (2011) 'Antitrust Immunity and International Airline Alliances' US Department of Justice Economic Analysis Group, Discussion Paper, February, page 10.
[81]Metal neutrality means that the participating airlines share revenue and costs on a given route no matter which airline is doing the actual flying.
[82] Footnote 42 above, page 50.
[83] N Shah (2007) 'Competition Issues in the Civil Aviation Sector', Competition Commission of India (CCI), 30.7.07 https://docuri.com/download/comptitive-issues-in-indian-aviation_59cle268f581710b286a6b44_pdf [accessed on 2019/06/18).
[84] *Ibid.*

quality services to their consumers that are better than those offered by their competitors to survive in the market. Also, it forces firms within the aviation industry to offer quality services that are of advantage to the final consumers. Fair competition has a significant and positive impact on the economy and consumer and enhances the growth of the industry in general.

5.3.1 Monopolistic Market

A monopoly market can be defined as a market condition where the firm dictates the prices of the product. The main characteristics of a monopoly are that the firms enjoy absolutely no competition thus each firm can ignore this potential problem. In the case of airlines with a dominant market position, there are greater chances of high prices for its services. Monopoly firms dominate the market and have the liberty to dictate the prices charged to consumers. Monopoly markets are characterised by a single firm in the market with large numbers of buyers. There is no close substitute, and no close substitute goods may be sold by another different firm. Entry to the monopoly market is restricted by barriers set by the factors in the market. Monopolistic markets, are characterised by the following features: (1) a single entity selling all output in a market, (2) a unique product, (3) limitations on entry into and exit out of the industry, and sometimes (4) specialised information about production techniques unavailable to other potential producers.

5.3.2 Oligopolistic Market

An important characteristic found in oligopolies, in contrast to a monopoly market, is the 'strategic interdependence between competitors'. The oligopoly market is characterised by the following features: (1) an industry that is dominated by a small number of large firms, (2) the dominant firms sell either identical or differentiated products, and (3) the industry possesses significant barriers to entry. The airline industry can be categorised in this market. The interdependent strategic decision-making in an oligopoly structure is usually understood in terms of quantity and price competition such that the profit of one firm depends upon the overall profit of all the firms within the alliance. The rule in such arrangements is that firms choose their strategies simultaneously.

5.4 Legal and Regulatory Framework in Selected Jurisdictions for Airline Alliances

The review and approval of airline alliances are conducted by the appointed designated competition institutions concerning the relevant legal and regulatory regimes. In many states, airline alliances are adjudicated by designated competition authorities to monitor compliance with

domestic competition laws of general application. In reviewing the application, the designated authority will either refuse or challenge an airline alliance based on the applicable law, policy or jurisprudence, or approve it, subject to compliance with stated conditions. The designated competition authorities are also responsible for monitoring the compliance of alliance members with the conditions imposed to mitigate the adverse impacts presented by the cooperation of carriers on fair competition. This chapter will examine how the competition authorities in some of the prominent jurisdictions concerning airline alliances, namely, the EU, US and some African regions handle cooperation applications and the applicable competition statutes.

5.4.1 US Antitrust Regime for Alliance Review

In the US, it is the Department of Transport (DOT) that has the statutory powers to review and approve airline alliances and grant exemption from its competition legislation. This Act contains the provisions underlining the conditions for mergers and acquisitions. The Act stipulates that in order for an application for anti-trust to be granted, it must satisfy two conditions, being: (1) the agreement is for public benefit, and (2) no alternative means that are materially less anti-competitive exist to achieve the public benefit.[85]

If the DOT approves an alliance agreement, anti-trust is not automatically conferred on to such agreement. The considerations for granting anti-trust to an alliance agreement is whether parties would be able to proceed without it and if the public interest requires that anti-trust immunity be granted.[86] The public interest is a critical consideration throughout the application process, which also guides the DOT in determining how best to remedy anti-competitive effects that might occur following the approval of an alliance. The DOT is empowered to impose conditions that can serve

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[85] US Code § 41309, section 41309(b)(1)(A) and (B) states that:
(b) Approval. – The Secretary of Transportation shall approve an agreement, request, modification, or cancellation referred to in subsection (a) of this part. However, the Secretary shall disapprove-
(1) or after periodic review, end approval of, an agreement, request, modification, or cancellation, that substantially reduces or eliminates competition unless the Secretary finds that – (A) the agreement, request, modification, or cancellation is necessary to meet a serious transportation need or to achieve important public benefits (including international comity and foreign policy considerations); and (B) the transportation need not be met or those benefits cannot be achieved by reasonably available alternatives that are less anticompetitive...
[86] Report by the European Commission and the United States Department of Transport, "Transatlantic Airline Alliances: Competitive Issues and Regulatory Approaches", 16 November 2010, page 14, http...[accessed on 12 June 2017].

to preserve competition and ensure that consumers benefit from the alliance[87] and works jointly with the US Department of Justice to assess the competitive impact of international airline alliances.

5.4.2 EU Antitrust Regime for Alliance Review

The European Commission is charged with the review of international airline alliances under European Competition laws, with specific reference in this regard to Articles 101 and 102 of the Treaty on the Functioning of the European Union (TFEU).[88] Article 101(1) prohibits agreements between parties and concerted practices which may affect trade between the member states which prevent, restrict or distort competition within the internal market. Article 101(2) states that any agreements concluded that are contrary to the prescripts of sub-article (1) are automatically void. An agreement may, however, be exempted from the provisions of Article 101(1) if it –

> ...contributes to the 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 concerned 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 production in question.

Article 102 prohibits the use of a dominating position within the external or internal market or a substantial part of the market and does not provide for exceptions for anti-competitive agreements as set out in Article 101(3), whereby the conduct of a firm can only be legally accepted if this benefits the consumer. On May 2004, the EU underwent two fundamental changes; which are obtaining jurisdiction to investigate air transport services, and being given full authority to apply Article 101 of the TFEU.

[87] Anti-trust immunity is generally subject to review after 5 years.
[88] These provisions are applicable to all industries and not air transportation only.

5.4.3 Eastern and Southern Africa Competition Regulations

The eastern and southern African states have adopted and implemented *inter alia*, the Common Market for Eastern and Southern Africa Treaty (COMESA) and ancillary competition regulations. The objective of this treaty is to govern the conduct of member states to provide for fair competition in the market as well as in the entire region. The set regulations cover both the scheduled and non-scheduled air transport services operations in COMESA, EAC and in the SADC regions, including any practice, conduct or agreement which may have an anti-competitive effect within the Common Market regions of the member states.[89]

In terms of Article 8, the Joint Competition Authority, established concerning Article 9,[90] may, on application by an undertaking, exempt any practice or conduct agreement which may have been prohibited under Article 4. The exemption may also be granted on application by a member state, and the Joint Competition Authority may impose conditions aimed at mitigating any adverse effects the State may experience.[91]

The efforts of the African States to regulate competition in the air transport sector must be lauded given its economic, social and financial challenges in contrast to its European and US counterparts. The African Union has noted the challenges facing the member states in the implementation of the competition regulations such as adoption and implementation of the competition regulations by member states and funding of the Joint Competition Authority, among others. However, notwithstanding these challenges, there is a recognition by the African states to ensure that adverse impacts on competition in the air transport sector are addressed.

5.6 Conclusion

States acknowledge the impact that airline alliances may have on fair competition, and it is for that reason that in most jurisdictions, domestic competition authorities and legislation have been endorsed to deal with the practices and agreements that would ordinarily be regarded to be anti-

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[89] The provisions relating to air transport are in Article 87. Article 3 provides that the Regulations apply to all economic activities conducted by private or public bodies, or having an effect within the Common Market, except those set out in Article 4.

[90] Article 9 stipulates that the Council of Ministers of COMESA, EAC Council of Ministers and Council of Ministers of SADC shall establish a joint body to be known as 'the Joint Competition Authority'.

[91] *Ibid.*

competitive. While competition authorities grant airline alliance agreements, conditions are imposed to mitigate the negative impact on the market, and each case is determined on its own merits, taking into consideration several factors including the benefit to the consumer. Competition forces firms within the aviation industry to offer quality services which will be of advantage to the final consumers. It can, therefore, be argued that there is an impact on fair competition when two or more airlines form an alliance, but the extent of the impact can only be measured when the competition authorities interrogate such agreement.

Chapter 6: Analysis of the Findings of Competition Authorities in Airline Alliances

6.1 Introduction

It is almost inevitable that horizontal agreements and code-share agreements will be legally challenged by those affected by such arrangements, especially low-cost carriers who encounter barriers to entry to the air transport market. States have established public regulatory authorities and specialised competition courts, or commissions mandated to adjudicate on these matters and make findings on applications, disputes and referrals. Each jurisdiction has its own set of criteria for the determination of these applications, but common criteria that are a factor for consideration are the benefits that the public will derive from the approval of an airline alliance. This chapter analyses some of the seminal rulings or findings in the adjudication of airline alliances from different jurisdictions.

6.2 Air France, the Delta Airline, the Transatlantic Joint Ventures and the KLM Transatlantic Joint Ventures Exception Case[92]

In this particular case, the Turkish Competition Authority (TCA) was tasked to decide on the impact of airlines companies joining strategic alliances and joint service operations. The proposed joint venture agreement would impact on the Turkish market via Istanbul-Atlanta and Istanbul-New York. In its decision, the TCA determined that schedules and the airline frequency are basic products of the airline industry. The TCA further asserted that strategic alliances improve costs and come with more significant benefits and concluded that the joint venture agreement would foster competition in the market and accordingly granted the exemption.

6.3 American Airlines / British Airways / Iberia Lineas Areas de España case[93]

The European Commission received a complaint from Virginia Atlantic Airways concerning a joint venture agreement concluded between BA, AA and Iberia Líneas Aéreas de España (IB) in terms of which the airlines would share the revenue covering all the passengers and air transport services between Europe and North America, that is, the transatlantic routes. This agreement

[92] Decision of the Turkish Competition Authority, dated 11.6.2008 and numbered 09-27/577-137.
[93] Case COMP/39.596 – BA/AA/IB.

provided for extensive cooperation among the parties in the operation of these transatlantic routes such as revenue sharing, routes, schedule flights, pricing and capacity. Initially, the Commission suggested that the agreement between the parties contributed to anti-competitive effects especially on specific transatlantic routes[94] and expressed concerns about the compatibility of these agreements with the provisions of Article 101 of the TFEU and Article 53 of the Agreement on the European Economic Area.

6.3.1 Competition assessment

Following extensive submissions by all the parties concerned, the parties made certain commitments to affected third parties in order to remedy the anti-competitive effects of the agreements and the barriers to entry or expansion, including the allocation of slots and fare combinability.

The findings of the Commission were that the position of the airlines to the agreements was strong and caused barriers to the affected routes. Also, the commission also found out that there was a lack of peak and off-peak hours especially in the John F Kennedy airport in New York. This has resulted in limited access of frequencies advantage, connecting traffic and the advantages enjoyed by the parties relate to the frequent flyer programmes experienced by the companies in the alliances. All these factors would in terms of the agreements eliminate competition between BA, AA and IB in the view of the Commission. The extent of the cooperation between the airlines would result in the parties behaving as 'a single entity on the routes covered by the joint venture'[95] and these routes would not be able to be replicated by competitors.

In the Final Commitments, the Commission included a clause in the agreements allowing it to review the Final Commitments after five years. Although there was a clear indication that the cooperation agreement between the parties would have anti-competitive effects on third parties in the same business, the Commission allowed it on the basis that the Final Commitments, considered

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[94] The specific routes of concern were London-Dallas, London-Boston, London-Miami, London-Chicago, London-New York and Madrid-Miami.

[95] Footnote 82 above, 9.

holistically and not in individual elements, are appropriate, proportionate and necessary to address the concerns raised.[96]

6.4 Application of South Africa Airways to join Star Alliance

The South Africa Airways (SAA), was established in 1935 and it is it is the national carrier of the Republic of South Africa. SAA had, for a significant amount of time, enjoyed a monopoly on high-density routes. In 2006, SAA applied to the Competition Commission for an exemption to join the Star Alliance. In terms of South Africa's Competition Act 89 of 1998 (Competition Act), an application for exemption is allowed only if it satisfies the criteria set out therein. An application for exemption is made in terms of section 10(3)(b) of the Competition Act.

In its application, SAA sought the exemption for ten years and argued that the Star Alliance is one of the prominent global airline alliance. South African Airways advanced two of the grounds set out section 10, namely the maintenance and promotion of exports[97] and a change in productive capacity necessary to stop the decline in an industry, as a basis for their application.[98] It argued that, as a member of the Star Alliance, offering the joint products of the alliance was required for the maintenance or promotion of exports[99] and would also enable it to remain competitive in the global aviation markets while providing better services to consumers and businesses in South Africa.[100]

The Competition Commission critically considered the application from SAA and granted the exemption for an initial period of five years on the basis that it would indeed maintain or promote exports. The Commission reasoned that joining the alliance would be of economic advantage to both SAA as well as the passengers. The costs and benefits derived from the membership of the alliance are for the benefit of both the company and economy at large. In conclusion, the Commission agreed that it was prudent to allow SAA to join the Star Alliance.

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[96] Footnote 82 above, 9.
[97] Section 10(3)(b)(i) of the Competition Act.
[98] Section 10(3)(b)(ii) of the Competition Act.
[99] General Notice, Notice 1237 of 2005, No 28230, 15.
[100] *Ibid*, 4

6.5 Case COMP/AT.39595-Continental/United/Lufthansa/Air Canada

This case served before the European Commission involving Air Canada, United Airlines, Inc., and Deutsche Lufthansa concerning the A++ Agreement concluded between the three carriers in relation to a revenue-sharing joint venture for all passenger air transport. The collective routes of the parties are between Europe and North America ('transatlantic routes'). In terms of this Agreement, parties agree to cooperate extensively on pricing, capacity, sharing of revenues and scheduling coordination, which are critical aspects of air transportation. The Commission made a preliminary conclusion that these areas of cooperation between the parties raised concerns regarding the Agreement's compliance with Article 101 of the TFEU, which the parties were requested to address. Pursuant to the final commitments made by the parties, and consideration of the comments submitted by interested parties, the Commission concluded that Agreement would not infringe Article 101.[101]

6.5.1 Competition assessment

The point of departure for the Commission was the consideration of the combined aggregate market shares of the parties.[102] The relevant market would be defined as the market for scheduled passenger air transport services.[103] The Commission asserted that objective of the A++ agreement is full metal neutrality, defined in the agreement as -

> a state of events in which each Party will be incentivised to treat all flying, regardless of airline, within the scope of the provisions of the A++ agreement as flying on its own network and in which customers will also become neutral to the choice among the parties as airlines and among itineraries on any given route'.[104]

Having assessed the agreement, the Commission found that,

[101] European Commission Decision of 23.5.2013 addressed to: Air Canada, United Airlines, Inc, Deutsche Lufthansa AG, relating to proceedings under Article 101 of the Treaty on the Functioning of the European Union, Case AT.39595.
[102] *Ibid*, para 4.1(16), page 7.
[103] *Ibid*, para 4.2(17), page 7.
[104] *Ibid*, para 4.3.1.1(35), page 11.

> The parties cooperate extensively in relation to key parameters of airline competition. In particular, they develop strategic network plans including capacity requirements...pursue joint revenue management activities, combine their pricing functions and align their pricing policy...[105]
>
> Based on the above, in its preliminary assessment, the Commission took the preliminary view that the A++ Agreement by its very nature aimed at, and had the potential of, restricting competition. This is because the parties' cooperation in the joint venture completely eliminated competition between the parties on key parameters of competition, such as price and capacity...The whole concept of metal-neutrality conflicts patently with the concept inherent in the Treaty provisions relating to competition, since the parties substituted competition with full cooperation for the risk of competition that would occur due to individual airlines' different incentives.[106]

The preliminary assessment of the Commission concluded that trade between the Member States that are party to the agreement may be affected within the meaning of Article 101 of the TFEU[107] as they enjoy substantial operations and sales across the European Union. In the final, the preliminary view of the Commission was that the cooperation of the parties restricts competition in the premium marked on the Frankfurt-New York route and the competition that existed pre-cooperation between Lufthansa and United Airlines was eliminated and the parties' competitors face significant barriers to entry and expansion.[108]

Upon review of the Final Commitments made by the Parties to the Commission to address the concerns identified in the preliminary assessment, the Final Commitments were found to be sufficient.[109]

6.6 Conclusion

The discussion above reflects only but some of the case law on airline alliances that have served before competition authorities. Each matter is dealt with on its own merits, taking into consideration the applicable legislation and other economic factors at hand. It is the writer's view that decisions to grant exemptions to airlines to be participating in alliances are not taken easily.

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[105] *Ibid*, para 4.3.1.2(36), page 11
[106] *Ibid*, para 4.3.1.2(37), page 12.
[107] *Ibid*, para 4.3.1.4(53), page 15.
[108] *Ibid*, para 4.3.1.5(54), page 16.
[109] *Ibid*, para 9.2(42), page 34

Competition authorities have to consider the benefits to consumers, the economy and the impact that this transaction may have on smaller airlines or those who seek access to the air transport market, which is usually a difficult market to enter. In circumstances where an exemption can and has been granted, competition authorities may remedy the anti-competitive effects by imposing conditions, which in the researcher's view, is a fair manner in dealing with such matters.

Chapter 7: Study Conclusion and Recommendations

7.1 Conclusion

The primary objective of this study is to investigate the impact of airline alliances on fair competition, looking at the international agreements, requirements of the O&C, forms of alliances, their benefits, and views of the courts and regulatory bodies on the issue of competition. The results of the research will contribute to the body of knowledge and assist in understanding the reasons for the formation of airline alliances, benefits to passengers and how they affect smaller entrants to the market.

The Chicago Convention has rightly entrenched the sovereignty of contracting states because the airspace must always be secured for safety reasons and to benefit the economy of the contracting states. The aviation international regulatory framework recognises that principles throughout the legal and/or regulatory instruments have to date been enacted and applied. However, with the ever-expanding industry of commercial aviation, the desire for business growth and the regulatory framework are not always aligned. Airline alliances have proved to be cost-effective and efficient and allow passengers to reach their destinations on time. They have also enhanced fair competition in the airline industry hence the market now operates more effectively. The main conclusions formed by this research are stated below.

7.1.1 The Civil Aviation Regulatory Framework

Although the founding international regulatory regime for civil aviation has been criticised as rigid and hampering business growth and expansion, it must be understood in the context that state airlines supported by state governments historically controlled civil aviation. The industry has since grown globally, commercial airlines have entered the market competing for business, and it has become necessary to reconfigure the regulatory regime. Hence in some international and regional communities, states have opted to do what is referred to as 'opening up the skies' or liberalisation of the aviation industry. These initiatives are not entirely without restrictions and require that contracting states make concessions; however, they do make a marked difference to the negotiation of airline service agreements and operations.

7.1.2 The Ownership and Control Requirements in the context of Airline Alliances

It is submitted that the O&C requirements, as contained in both the Transit and Transport Agreements, strongly reinforce the principle of sovereignty unambiguously expressed in the Chicago Convention. Contracting states may grant or withhold permission for flight services over its airspace to a foreign airline if substantial O&C thereof are not vested in its nationals. In order to overcome these requirements still in force and effect, airlines have formed airline alliances enabling them to operate in various states. Most carriers are members of one of the three dominant global alliances, which can negatively affect smaller entrants to the market. The existence of airline alliances makes it appear to new and smaller airlines that the only way to succeed in the aviation sector, is to join an alliance. Nonetheless, passengers have benefitted from the alliance arrangements to date.

7.1.3 Fair Competition

The enquiry and examination into the effects of the formation of airline partnership alliance are determined on a case-by-case basis. The regulatory agencies and bodies set thresholds which stipulates that alliance partners should co-operate rather than compete. Countries also recognise the importance of alliances because of their economic importance and consumers enjoy the diverse and varied services offered as a result of the formation of alliances. Also, states recognise the importance of competition because it impacts competition in the market thereby reducing the chances of monopolies. Competition enables firms to enjoy economic freedom as well as economies of skills. The consumer will enjoy fair prices as well as diverse services offered by different firms in the market due to their competing to draw them to purchase their services. The competition also forces firms within the aviation industry to offer quality services, which is an additional advantage to final consumers. Further, fair competition allows for a free and conducive environment where all firms can compete on equal grounds and maximise the available economies of scale in the long run. Fair competition allows companies to operate effectively with limited barriers in the market, allowing for new investment and boosting the growth of the airline industry.

7.2 Recommendations

Despite the move towards 'liberalisation' of the aviation industry, sovereignty still strongly influences the bilateral agreements entered into by contracting states. There are real and valid reasons for the retention of the O&C requirements in international aviation law. Airline alliances

have proved to be a workable alternative to these limitations and must be allowed, but competition regulatory authorities must be empowered to scrutinise the conditions imposed on the alliance to ensure that the smaller players in the industry are protected and mitigate any anti-competitive effects. The regulatory competition authorities should produce carefully designed policies and procedures to encourage fair competition in the industry by the elimination of unprocedural and unfair barriers in the industry. These authorities should consider the fundamentals benefits accrued by the formation of alliances.

In conclusion, it is evident that the subject of airlines alliances and their position within international law is a sensitive topic and the subject of many discussions. In examining the limitations posed by ownership and nationality normally inherent in bilateral agreements, it appears that consequently, these alliances have developed to become an essential and convenient method of bypassing these limitations. For consumers, these have made international travel a more comfortable and efficient method of travel and have benefitted the carriers who are now able to offer their would-be passengers the choice of extended routes and services. It does remain vital that these alliances be regulated and monitored by the competition authorises to prevent abuse and not deny the smaller or new carriers the opportunity of taking part in this ever-developing market. Antitrust immunity is a privilege and not a right and, therefore, must be considered holistically. Furthermore, the regulatory competition authorities must act independently without fear or favour and be empowered and supported at all levels to achieve the effective formation of both strategic and tactical alliances in the industry.

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