Achieving Maximum Velocity: An International Perspective

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- It's wonderful to be here in Winnipeg.

- In the ten years I served as the United States' chief aviation negotiator, I spoke at a number of conferences in Canada as we worked hard and, ultimately, with success to turn our 1995 open trans-border aviation agreement into a full Open Skies agreement in 2007. It's a real honor that, even after my retirement from the U.S. Government, you asked me, a graying retiree, to be a part of an important program on securing for Canada, its communities, and its citizens the full benefits that aviation has to offer.

Background and Introduction

- I took my first international flight in 1972, setting out on a trip to Germany as an exchange student. At the time, budget travelers in the United States were confronted with the pre-deregulation oligopoly of Pan Am and TWA, which operated in a highly restricted market under the watchful eye of the IATA cartel. Students seeking a cheaper way to fly to Europe had two alternatives: flights over Iceland and flights via Canada.

    - In 1972, I ended up choosing to fly on Icelandic through Reykjavik. But the research I did at the time etched in my mind an impression of Canada as a nation committed to a free economy with a focus on the value to consumers of marketplace competition.

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[1] Served as Deputy Assistant Secretary for Transportation Affairs at the U.S. State Department from 2001 to 2010. The speaker's views are solely his own and should not be attributed to the U.S. Government or to any airline, airport, or other entity.

- That impression remains a correct one today, some forty years later.

  - Canada ranks 13th among the world's economies based on total GDP and ranks an even more impressive 9th by GDP per capita. Its 34 million citizens clearly punch above their weight in the global marketplace.

  - Likewise, in the most recent Heritage Foundation Index of Economic Freedom, Canada ranks an impressive sixth in the world, trailing only Hong Kong, Singapore, Australia, New Zealand, and Switzerland. Canada is a full four places ahead of the United States.

- And yet if there were a "freedom ranking" focused solely on air services, Canada might not fare so well.

  - According to an analysis by Professor Ambarish Chandra of the University of Toronto, the number of per-capita miles flown by Canadian residents is less than half what it is in the United States.[2] One would think that the huge size of Canada and the dispersal of its population would yield, if anything, a higher figure.

  - Where once, back when I was a student, U.S. residents crossed the border to fly from Canada, the tide has turned in Bay of Fundy proportions. One careful academic study estimated that, in 2008, over 4.7 million Canadians crossed the border to fly from U.S. airports.[3] More recently, Air Canada's CEO, Calin Rovinescu, put the figure at 5 million annually.[4] Similarly, the Senate Standing Committee report of April 2013 refers to more than 5 million.

  - And if we look at aviation practices around the world, where so many countries have endorsed aviation policies that match or even exceed the liberality of U.S. Open Skies, Canada's Blue Sky Policy is widely perceived as among the most cautious and regulation-oriented.

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[2] Testimony to the Senate Committee on Transport and Communication: Study of the Canadian Airline Industry, March 6, 2012.

[3] Omar Sherif Elwakil, Robert J. Windle, Martin E. Dresner, Transborder demand leakage and the U.S. – Canadian air passenger market, Elsevier, Transportation Research Part E: Logistics and Transportation Review.

[4] The (Montreal) Gazette, April 20, 2013 (quoting from a speech by CEO Rovinescu in January citing various reasons that "make airline tickets in Canada more expensive and now help drive 5 million Canadians a year to U.S. border airports").

- I do not intend, however, to focus on Canadian policy this morning but, instead, want to describe the U.S. experience in reaching and implementing an Open Skies policy. The contrasts between our two countries are striking.

- Admittedly, having devoted more than a decade of my professional life to the U.S. Open Skies initiative, I'm deeply biased in favor of the benefits it has delivered to American consumers, shippers, and communities. But I also think that Open Skies has been a boon to U.S. airlines and a critical element in preparing them to be effective competitors in today's global aviation marketplace. I'll talk more about that later.

- Before I turn to the U.S. experience, however, I want to emphasize that what's good policy for the United States may not be good policy for Canada. Each country must decide what its priorities are and whose interests it deems paramount—and then make decisions accordingly.

- Robert Frost wrote a famous poem that includes the following:

> *Two roads diverged in a wood, and I—*
> *I took the one less traveled by,*
> *And that has made all the difference.*

- Now, I'm certainly no poet; and it's mighty early in the conference to be citing verse; and, for sure, Robert Frost was not thinking of aviation policy when he pinned these well-known lines. My point, however, is that the decisions we make—the roads we choose to take—can indeed make all the difference.

The Path to U.S. Open Skies

- Between my first international flight in 1972 and my first experience in 1985 working on air services negotiations in the State Department, the United States, under President Jimmy Carter, had deregulated its domestic aviation industry. In addition, in 1979, the United States had adopted a policy statement on international aviation that endorsed greater reliance on vigorous airline competition. It called for "trading competitive opportunities, rather than restrictions, with … negotiating partners."[5] In emphasizing "competitive opportunities," the United States had begun to shift from an airline-centric to a consumer-centric approach. Under this new policy, fairly liberal agreements were struck with several countries, including Israel, the Netherlands, and Korea.

- Nevertheless, my recollection from negotiations in the late 1980s is that the United States still spent a lot of time fretting about the declining fortunes of Pan Am and TWA and giving their interests a top billing as we worked through one negotiating round after another.

- A critical breakthrough occurred in the Administration of the first President Bush with something called the "Cities Program."[6] This initiative, announced in 1990, was driven by U.S. airports and communities—airports and communities that were not traditional U.S. gateways but that wanted non-stop international air service. They had identified foreign airlines, such as KLM, that were ready and willing to provide it.

  - There was opposition, however, from U.S. air carriers—PanAm, for example—that possessed all the rights they wanted from the foreign countries in question and opposed giving the foreigners "something for nothing."

  - Under the Cities Program, DOT granted eligible foreign carriers "extra-bilateral authority" to serve additional U.S. communities: that is, operating authority beyond what was mandated in existing air services agreements.

- Having looked to interests beyond those of U.S. airlines, the Cities Program was quickly and logically followed in 1992 by a Department of Transportation rulemaking that looked at how to incorporate this different notion of "balance" into air services negotiations. DOT did so by defining the concept of "Open Skies" [7] and striving to create a "balance of opportunities" for airlines to compete in an open market rather than a "balance of benefits" solely for the two sides' carriers.

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[5] "International Air Transportation Negotiations, Statement of U.S. Policy for the Conduct of the Negotiations," issued Aug. 21, 1978. *Public Papers of Jimmy Carter, June 30-December 31, 1978,* at 1462.

[6] Order 90-1-62, Department of Transportation, "In the matter of Expanding International Air Service Opportunities to More U.S. Cities," 55 Fed.Reg. 4039 (Feb. 6, 1990).

[7] In the Matter of Defining "Open Skies," DOT Docket 48130, Order 92-4-53 (requesting comments) (Apr. 29, 1992), 57 Fed.Reg. 19,323 (May 5, 1992); Final Order 92-8-13 (Aug. 5, 1992), 1992 DOT Av LEXIS 568 (1992).

- In essence, Open Skies entails letting consumers and shippers have the principal voice in deciding which kinds of air service and air service providers best meet their needs. Open Skies relies much, much less on the traditional bilateral air services approach in which government regulators effectively dictate to their citizens the air services that they can, should, and will receive.

- I think that most of you know what an Open Skies agreement includes, but just in case, here's a quick list of the essentials:

  - no limits on the number of airlines of either country that can fly,
  - no limits on the airports they can serve,
  - no limits on routes for first, second, third, fourth, fifth, or sixth freedom rights,
  - no limits on aircraft types,
  - no limits on the frequency of flights,
  - no special limits on charters or cargo flights,
  - essentially no limits on airlines' freedom to price their products in the marketplace,
  - under Open Skies, there is broad authority for airlines to enter into code-sharing and other cooperative arrangements,
  - there are also strong articles to ensure aviation safety and security, as well as
  - a number of doing-business protections for airlines in areas such as the establishment of offices abroad, ticket sales, ground handling, user fees, and the right to remit earnings from abroad.

Negotiating Open Skies

- Initially, Open Skies was intended as an "initiative to negotiate … agreements with European countries,"[8] although Andrew Card, Secretary of Transportation under President Bush, expressed the hope that the effort might be expanded to other regions.

- It took a couple years to persuade the new Administration of President Bill Clinton to proceed, even in Europe. In late 1994 and early 1995, however, the United States concluded Open Skies agreements with nine smaller European

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[8] *Id.,* Final Order at 1.

countries—a group that, it was thought, might provide "critical competitive mass" to persuade larger European countries to liberalize.

- Concurrent with this effort was the negotiation of the historic Canada-U.S. open trans-border agreement, which was signed in 1995 and phased in over a three-year period.

- After the success in Europe—including an important Open Skies agreement with Germany in 1996—Open Skies negotiations followed with a group of liberal-minded Asian nations[9] and, separately, with countries in Central America.[10]

- By the end of 1997, the United States had negotiated Open Skies agreements with 25 countries. Still, there was no clarity whether Open Skies was a universal negotiating policy or one only for certain countries that could be seen as part of a "critical mass" in a region. An Open Skies agreement was concluded with Jordan in late 1996, after the State Department weighed in strongly in favor of positive treatment for this key ally in the Middle East. On the other hand, DOT insisted on carving out the London-U.S. market from a new agreement with Pakistan that otherwise had all the elements of Open Skies.

- This policy uncertainty was resolved during the tenure of Rodney Slater as President Clinton's second Secretary of Transportation from 1997 to early 2001. Intensely interested in building stronger U.S.-African relations, Secretary Slater posed a legitimate question: if the United States can have Open Skies agreements with countries from all these other regions, why not also with African countries?

- Honestly, by this time there was no good reason why not. Open Skies had won the support of U.S. airlines, airports, and airline labor as well as bipartisan support on Capitol Hill.

- Moreover, the positive results of liberalization had been documented. Perhaps the most famous U.S. study was the DOT analysis of the 1995 Canada-United States agreement.[11] The study found that in the three years following signature:

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[9] Singapore, Taiwan, New Zealand, Brunei, Malaysia, and Korea.

[10] Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and Panama.

[11] U.S. Department of Transportation, The Impact of the New US-Canada Aviation Agreement at its Third Anniversary, February 1998.

  - Total U.S.-Canada passenger traffic had increased 37.2%, versus only 4.3% in the three years prior to the agreement;

  - On average, the yearly growth rate was 11.1%, compared to 1.4% before;

  - In 1994, there were 54 nonstop markets with annual traffic of more than 50,000 passengers. In 1997, the number of markets with that level of traffic had increased to 77.

- It was with a view to results like these but with little fanfare that the United States adopted an approach to aviation negotiations by late 1998 that has remained in place for almost fifteen years: The United States will negotiate an Open Skies agreement on a "one size fits all" basis with essentially any country, bar the likes of North Korea, Iran, and Cuba.

  - Specifically, there is no effort to weigh, case-by-case, whether U.S. airlines or the partner country's airlines will derive greater commercial benefits from Open Skies.

  - Instead, Open Skies is focused on fostering vigorous airline competition, to the ultimate benefit of consumers and the national economy.

- Let's take a case study. In 2005, the United States concluded an Open Skies agreement with Ethiopia. To date, only Ethiopian Airlines has taken advantage of the right to operate scheduled service between the two countries, flying to Washington's Dulles Airport from Addis Ababa. That is not seen in the United States as a bad thing. American consumers benefit. So does the greater Washington, DC metropolitan area. Moreover, U.S. airlines retain the right to fly their aircraft to Ethiopia at any time if they decide it makes commercial sense. In the interim, they can code share to Ethiopia with foreign partners.

- Other countries have a similar "Open Skies for all" approach, including Chile, Singapore, the UAE, and New Zealand.

- On the other hand, in many countries, government regulators and negotiators continue to pick and choose the level of market opening they deem appropriate for countries on a case-by-case basis. For example, Canada's Blue Sky Policy envisions the negotiation of fully liberalized agreements with some countries but contains the express proviso that: "In other limited situations, the

Government may determine that it would not be in Canada's best interests to negotiate an Open Skies-type agreement." In other words, sometimes yes, sometimes no; it all depends.

- For example, it's my understanding that Canada agreed in 2012 to allow Ethiopian Airlines to fly to Toronto but limited the number of frequencies to two a week. Ethiopia, in short, appears to be one of those "limited exceptions" where officials in Ottawa perceive Open Skies not to be in Canada's best interests. Why Canada would not want to help this African country expand its aviation links, build cultural ties, grow tourism and exports, and foster development through a pro-competitive, fully reciprocal Open Skies agreement is hard for me to understand. Does Air Canada fear being driven into bankruptcy by Ethiopian Airlines, which is, in fact, one of its partners in the Star Alliance? Is it the fear of seeing traffic diverted from Lufthansa's flights to other points in Africa? I'm perplexed, but, of course, I come to the question with my south-of-the-border Open Skies perspective.

Assessing the Effects of U.S. Open Skies Policy

- Let's turn back to the United States, where a one-size-fits-all Open Skies policy has truly "made all the difference." (Again, with apologies to Robert Frost.)
    - ➢ As of today, the United States has negotiated Open Skies with 110 countries on every continent save Antarctica. [12]
    - ➢ U.S. airports are open for business by the airlines of those countries without restriction as are the airports in those partner countries for U.S. carriers.
    - ➢ This provides an incentive for U.S. airports and communities to make a pitch for new flights and new routes by both U.S. and foreign airlines. The door is open: with Open Skies in place, there's no need for a laborious and often contentious bilateral air services negotiation to clear the path for new service.
        - ♦ This is, I think, a very important point—a point made in one of the articles by Professors Duval and Macilree included in the materials for our conference here in Winnipeg.
    - ➢ The doors are also open for innovation—by alliances like Star, SkyTeam, and oneworld; by growing carriers from the Middle East and Bosphorus region, such as Emirates, Qatar, and Turkish Airlines; by traditional sixth-

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[12] An updated list is maintained by the State Department at: http://www.state.gov/e/eb/rls/othr/ata/114805.htm.

freedom carriers such as Singapore and KLM; and by low-cost carriers such as Volaris and Westjet.

- I recognize that opening the doors to vigorous competition entails putting a country's own airlines to the test: will they prosper or won't they?

- The verdict in the United States is clear: Open Skies has been very good news not only for consumers but also for U.S. airlines.

  - With respect to consumers, Cliff Winston, a leading U.S. aviation economist at the Brookings Institution in Washington, has done a study that found that travelers have "gained at least $5 billion annually as a result of lower international fares and additional flights generated by open skies agreements."[13]

  - With respect to U.S. passenger airlines, they have taken advantage of the "balance of opportunities" inherent in Open Skies. In the last IATA winter traffic season, U.S. carriers operated just under 60% of all the international passenger flights to and from the United States. A 60/40 market split suggests that Open Skies has been quite positive for U.S. airlines and their employees.

  - And, of course, two U.S. all-cargo carriers—UPS and FedEx—are world-leading enterprises whose ability to offer their customers express delivery service on a global basis has been boosted enormously by the rights secured in Open Skies agreements negotiated by the U.S. Government. The beneficiaries extend far beyond UPS and FedEx as corporations to:

    - the tens of thousands of men and women they employ,
    - the many communities they serve—especially, at major hubs like Louisville and Memphis, and
    - the global economy that depends on express delivery service to make "just in time" manufacturing a reality.

- Many argue that U.S. aviation policy has its imperfections, citing things such as the Fly America Act and deeply imbedded restrictions on cross-border airline ownership and control. I'm not here today to rebut these criticisms—indeed, I

[13] Clifford Winston,"A Remedy for Air Travel Woes," *New York Times,* Nov. 21, 2012.

think at least some of them are legitimate. My hope is that the United States will continue to build on Open Skies to make further improvements and remain at the cutting edge of modern aviation policy.

- The original motivation for and impetus behind the Open Skies initiative, however, was and is a noble one of focusing not on the special interests of airlines but on the interests of U.S. consumers first and foremost and of relying on competitive markets, not the predilections of government regulators, to deliver the services that the travelling public and shippers need and want.

- The title of our conference here in Winnipeg is “Maximum Velocity: Unleashing the Power of Aviation.” I think it’s hard to achieve maximum velocity when air services agreements include such roadblocks and speed bumps as frequency limits, restrictions on the number of cities that may be served, and controls on airline pricing. It’s also hard to unleash the power of aviation when one shackles airline competition in the regulatory straightjacket of traditional air services agreements—the sort of agreements that the United States jettisoned when it adopted an Open Skies policy.

- In Canada, the fear seems ever present—and I understand why—that open competition could harm the nation’s principal international carrier.

- I am the first to admit that, with only one established network airline offering extensive international service, Canada is today in a different position from the United States back in the 1990s when the U.S. endorsed an Open Skies policy. In some sense, it was perhaps easier for the United States—with a number of large international airlines—to make the jump: even if Open Skies created challenges as well as opportunities for U.S. carriers, I don’t think that anyone feared that American international aviation would drop off the face of the earth.

- But that begs the question of whether such fears are well-founded in Canada and, also, how one balances such concerns against the harm that a protectionist policy does to Canadian consumers, cities, and economic growth. Put a bit aggressively, is a fear-based policy a good policy in the long run?

- My personal belief is that it’s well-nigh impossible, in the long run, to protect an airline to competitive strength. Witness the tragic efforts to do so in Brazil: years of protectionism failed to cure the ills of its airline industry. One after the other, Vaspe, Transbrasil, and Varig slid into oblivion, as Brazil clung to restrictive air services accords. Today, Brazil's policy is far more liberal, and its airlines are far more successful.

- Just as in hockey, soccer, baseball, football, or any other competitive endeavor, one cannot build a championship team by playing in the minor leagues only, by skating or running only at half-speed, or by banning fastballs in practice in order to protect the oh-so-vulnerable hamstrings and elbows of the players. In a world of global airline competition, protectionism—in my view—seems a recipe for ultimate decline. And, in the meantime, it deprives a nation's citizens and communities of the power of aviation to deliver jobs and economic prosperity.

- Likewise, a strange argument is sometimes advanced that rights granted to airlines should be limited so as to reflect the relative number of passengers originating or ending journeys in their home countries. Small countries do poorly under this concept. This view of aviation—one that gives priority to third- and fourth-freedom rights and frowns on fifth and sixth freedom operations—does have antecedents dating back to the antiquated U.S.-UK Bermuda 1 agreement of 1946.

  - But the world moved on a long time ago—witness the success (and the huge benefits to consumers, globally) of the sixth-freedom services that KLM and Singapore have been providing for decades.

  - It's particularly strange to see such arguments advanced in Canada, where Air Canada has publicly announced its intention to use sixth-freedom rights to tap the potential of the huge U.S. market to Canadian advantage. To my thinking, these plans are wonderful: great for competition, great for consumers, great for students looking for new and better alternatives for their first trips abroad.

- What about the future of international aviation? I'd be a much richer man if I had an accurate crystal ball—I might own a mansion in Bermuda where I could celebrate on a daily basis the demise of my country's Bermuda 1 and 2 agreements with the United Kingdom.

- Seriously, it's hard for me to imagine any long-term trajectory for international civil aviation that isn't directed toward greater liberalization, increased market access, and enhanced competition. That was certainly the consensus view at the

ICAO Air Transport Conference that took place in Montreal just two months ago.[14]

- And I think, as well, that we will see an expansion of what I'd call "cross-border airline ventures." Already, we have three huge airline alliances—Star, SkyTeam, and oneworld—which function in part as a work-around of many countries' limits on foreign ownership and control of air carriers. But we're also seeing outright cross-border airline mergers—for example, in Europe with Air France/KLM, Lufthansa/Swiss/Austrian, BA/Iberia and in Latin America with Avianca/TACA and Lan Chile/TAM (to create LATAM). Moreover, other experiments such as the expansion of the Air Asia family of low-cost carriers are chipping away at the walls of national ownership and control requirements in much the way that tourists demolished the Berlin Wall. North America—the United States, Canada, and Mexico—are not part of this movement at present. One has to wonder whether North America is on right side of history.

- Summing up, with the benefit of hindsight, it's clear to me that the United States made the right choice—the right choice for the United States—when it opted in the 1990s to pursue an Open Skies policy and, after some back and forth, to apply that policy universally. More airlines, more destinations, more city-pairs, more frequencies, more price and service competition—these are fundamentally good things.

- The origins of Open Skies, as I mentioned, lay in the Cities Program, an initiative spurred by U.S. airports and communities outside the traditional gateways such as New York and Los Angeles.

- Perhaps a similar initiative in Canada—focused on addressing the needs of Canadian cities outside the traditional hubs such as Toronto—would be a good initial step forward, whether or not it leads to a broader Open Skies approach.

- In any event, I applaud and salute Winnipeg for hosting this important conference and hope that your efforts to "make a difference" will meet with similar success.

- Thank you so much for inviting me to join you. I look forward to a great two days. If there is time, I would be glad to respond to any comments or questions.

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[14] Documentation at: http://www.icao.int/meetings/atconf6/Pages/default.aspx .