A Transaction Cost Analysis of Scheduled international Air Transport of Passengers

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Citation for published version (APA):

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Chapter IV - The Community structure

4.1 - Introduction
The previous chapter described the Bilateral structure which traditionally governs the exchange of air transport rights. The Bilateral governance structure no longer applies to that transaction when the Member States are involved, having been gradually replaced by a specific European structure. This Community structure is the subject of the current chapter. First, some general remarks are made about the views of the European states on air transport. Sections 4.2 and 4.3 look at the development of the Community structure, while Section 4.4 describes the structure in its present form. Section 4.5 discusses the parties to the transaction, namely the Community institutions as well as more traditional parties. Section 4.6 describes the transaction, and Section 4.7 the various phases in the transaction process. Section 4.8 then characterises the Community structure and Section 4.9 concludes with some comments about the future development of the structure.

The air transport industry in Western Europe and the Community structure cannot be analysed without looking at European integration within the framework of the European Community. For a long time, the Bilateral structure governed the exchange of air transport rights between Western European states, who were party to the Chicago Convention and entered into bilateral treaties. Not until recently (1997) was a specific Community structure implemented. Cooperation was, however, already a common feature. Motivated by the growing co-operation between some Western European states, the Council of Europe was established in 1949. In 1957, the Treaty of Rome was concluded by six Western European states, with the objective of integrating the economies of the participating member states (hereafter: ‘Member States’). This objective was pursued for political as well as for economic reasons. They included the desire of the Member States to end the threat of renewed hostility between France and Germany, the demise of the colonial empires, and the dramatic change in the balance of powers whilst the states still aimed for an influential role in the world (among others: Jansen, De Vree, 1985). Each state had its own reasons to join the Community and this applies equally to the states that joined later. In many cases, these different interests, concerns and circumstances are still of relevance today and influence the conduct of Member States in their European policy-

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1 Recall that in this thesis ‘Community structure’ refers to the structure governing the exchange of air transport rights between Member States. The Community structure comprises the rules of the EC Treaty, secondary legislation and all other rules and institutions governing such exchange.
2 The Community structure applies to the member states of the European Economic Area, which means that, in addition to the EC member states, it covers Norway, Iceland and Liechtenstein. Infra, p. 96.
3 The Treaty of Rome was opened for signature on 27 March 1957. It forms the basis of the EEC Treaty, which was renamed ‘EC Treaty’ following the Maastricht Treaty mentioned on p. 1.
making.

Chapter III observed that views on air transport differed between European states, on the one hand, and countries such as the United States on the other. The reasons are both political and geographical. Historically, air transport in the United States was essentially domestic. The policy focus was on competition with the railways, which, unlike those in Europe, had not been damaged by the first world war. Not until Charles Lindbergh had completed his international flight in 1927 did air transport become more internationally oriented. Like the European states, the United States government needed to provide financial aid because of the sector’s marginal profitability. It intervened in the industry primarily by awarding contracts for the transport of mail and regulating these services. In Europe, the industry was very much influenced by the small size of individual states and relationships with the (former) colonies. The European geography gave the industry an international orientation from the outset as it generated a large volume of international flights, which in turn raised questions of sovereignty. Furthermore, each state had a flag carrier which made hub-and-spoke systems a natural development (among others, Williams, 1993: 85, Nero, 1995: 137). The relatively short flying distances also resulted in high operational costs and led to financial aid from the state. The means employed tended to be more direct than in the United States. They included subsidies and even nationalisation. These intercontinental differences are not to deny some wide differences within Europe. The French, for example, subsidised the sector from the outset, whilst the English were very reluctant to provide financial aid (Sampson, 1985: 31). Generally speaking, however, European states had a stronger tradition of air transport regulation than the United States (Button et al., 1998: 27).

The international orientation of the European states and close relations between them strengthened initiatives for co-operation in air transport at an early stage. This included state initiatives, such as the creation of ECAC in 1955, which offered a forum for exchanging views and agreeing on common policies. ECAC further constituted an instrument for negotiating as a group, thus enabling the states to exercise more influence. There were private actions as well, such as the establishment of a research institute, ‘ITA’, and the Air Union project. Traditionally, European carriers were party to pool agreements and participated in each other’s capital (Williams: 1993, 118). The states accepted these participating interests, mainly for financial reasons. Any shareholdings were, however, tied to a maximum to be able to comply

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4 As was stated in Section 3.1, the British attitude was completely different after the second world war. This illustrates the extent to which the relative value of objectives can affect behaviour.

5 The ITA was established in 1954 by KLM, together with the six largest European carriers. The Air Union project was started in 1957 by Lufthansa together with Air France, and joined by Sabena and Alitalia. It entailed the establishment of a pool agreement, whereby flights would be operated under a common flight schedule. Abbatı (1987: §7.2.11) points out the link between this initiative and state actions on air transport cooperation.
with the requirements of substantial ownership and effective control. None of the initiatives succeeded, primarily because states did not want to give up their sovereign rights.

The next section will take a closer look at European integration and at the role of air transport in the EC Treaty.

4.2 – European integration, EC Treaty and air transport

An analysis of the Community as a governance structure requires an understanding of the features characterising that structure and the relationships between Member States, which are responsible for concluding air services agreements. This, in turn, requires some information on the general objectives of the EC Treaty and elements specific to the international co-operation between Member States. Given the important role assigned to case law in the formation of the Community structure, this section also discusses some court cases. The developments will be discussed in chronological order.

The European Community (formerly the European Economic Community) was created by the Treaty of Rome. The treaty’s goal can be described as the economic integration of Member States and, more specifically, as the promotion of a harmonious development of economic activities, an increase in stability, and an accelerated rise in the standard of living. One of the means to realise these objectives is a ‘common market’. A common market is characterised by the free movement of goods, persons, services and capital, a common competition policy and harmonisation of national laws, in so far as differences would inhibit the formation of such a market (Mathijsen, 1990: 124). The establishment of a common market can be pursued by way of positive as well as negative integration (Hellingman, Mortelmans, 1983: 121-123). ‘Positive integration’ means the creation of equal conditions across various sectors of the economy. This is done through ‘harmonisation’, which is the creation of a new rule at the Community level or harmonisation of existing national rules. ‘Negative integration’ entails the elimination of obstacles to the free movement noted above and is also referred to as ‘liberalisation’. Whilst liberalisation has the potential to create more freedom, harmonisation requires that domestic powers be limited or even transferred to a higher (supranational) level. This makes harmonisation more difficult to accomplish than liberalisation (Corbey, 1993: 100-101). Indeed, harmonisation is not usually a feature of co-operation between states. In view of the

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6 An extensive overview can be found in Kapteyn, VerLoren van Themaat (1998).
7 In the EC the term ‘liberalisation’ is used mostly to denote a freeing up of the market. The term ‘deregulation’ is avoided to appease political sentiments. See Havel (1997: 92) for a discussion of the difference between liberalisation and deregulation. He opines that liberalisation (like regulatory reform) is a conceptual staging post on the journey to full deregulation. On the other hand, ‘liberalisation’ was defined in Chapter III as ‘making free’. One way of making free is deregulation.
broad treaty objectives, however, harmonisation forms an integral part of the EC. Apart from harmonisation, there are more elements differentiating European integration from traditional inter-governmental co-operation between states. In inter-governmentalism, there is no separation of powers and the participating states act independently of other institutions and either consensually or not at all. The EC Treaty creates a binding force that goes far beyond such co-operation in limiting the powers of Member States. Limitations include the direct applicability of Community law, and in cases before the European Court of Justice it has been established that this law holds primacy over national law. The EC is provided with its own institutions and has legal personality. It is vested with real powers arising from a limitation of competence or a delegation of certain powers from states to the Community (Kapteyn, VerLoren van Themaat, 1998: 78). In some cases, Community institutions enjoy primacy over national governments because qualified majority voting as laid down in the EC Treaty gives them the necessary legal powers. The objectives of the treaty encompass every policy field and the transfer of Community measures to domestic legal systems is substantial. Although the Member States in practice can still stop decisions, policies or agreements from being reached, they have found it all but impossible to go back on decisions and policies previously introduced. In other words, Member States have become constrained in their policy-making and are no longer sovereign in the traditional sense. Notwithstanding these limitations, the EC structure generally leaves Member States a relatively high degree of flexibility to implement the policies or rules that have been agreed. The structure contains a large number of minimum norms, optional clauses, exceptions and opportunities sometimes enabling a state to go beyond the provisions of the EC Treaty or secondary legislation. Furthermore, some provisions require legislative action by Member States. As an example, Regulation 1617/93, concerning slot co-ordination makes the operation of the rules dependent on the declaration by a Member State that an airport is slot co-ordinated. Fennes (1997: 242) compares the EC Treaty to a framework treaty, which essentially sets out general principles and objectives. Community institutions have to provide more detailed rules through secondary legislation, comprising Regulations, Directives, Decisions, Recommendations and Opinions. These features create

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8 From a transaction cost perspective liberalisation has an advantage over policy harmonisation in that accepting proposals demanding inactivity is often easier than agreeing on policies that are to be pursued actively (Corbey, 1993: 100-104). However, harmonised policies save on information and search costs, which is especially important in the internationally oriented air transport sector.
11 Note that these instruments differ in their applicability. A Regulation, for example, is binding in its entirety and directly applicable in the Member States, whilst a Directive is binding as to the results to be achieved but leaves the choice of form and method to Member States’ authorities. Decisions are binding upon those to whom they are addressed. Recommendations and Opinions are not binding.
flexibility and enable Member States to cope with varying circumstances and to accommodate - to a certain extent - domestic sentiments. By thus increasing the chance of state co-operation in the process of policy making and implementation, a layered structure can facilitate the integration process. However, there are also disadvantages, such as a greater risk that regimes will diverge, as well as the difficulty of knowing all the rules applicable at any one time. Donner et al. (1998: 124-125) cite the Dutch practice of dynamic referral, whereby - in the case of Directives containing a provision delegating power to the Commission - an implementing law contains a reference to the original Directive (or certain provisions or annexes) without amending or clarifying the text. Future amendments are transposed automatically. Although the procedure increases the speed of implementation and eliminates the risk of incorrect implementation, future changes in any rules are likely to remain obscure.

The EC Treaty contains various provisions that elaborate the EC’s objectives and serve to implement them. An important part of the treaty deals with the realisation and operation of the common market. It also contains various provisions on relations with third countries as well as on the powers of Community institutions. The transport sector is given separate attention\(^\text{12}\). The draftsmen justified their decision of not dealing with transport in the section on services in terms of the distinctive features of the transport sector, drawing, in part, on the controversy over whether transport is to be seen as an instrument of economic policy or as a sector important in its own right. In the final analysis, they considered transport a means of realising the common overall purpose of the EC Treaty rather than an end in itself (among others Abbati, 1987: 18-19, Kapteyn, VerLoren van Themaat, 1998: 1172-1173, Button, forthcoming)\(^\text{13}\). The relevant treaty articles reflect this by emphasising intervention and harmonisation rather than liberalisation. Article 3 para 1 (f) EC is a good example as it formulates an obligation to adopt a common policy on transport. Button (forthcoming), in the context of the Common Transport Policy, also points to the early focus on harmonisation as a way of creating a level playing field. It may thus seem surprising that negative integration has been common in air transport, as will be seen in this chapter. Within the special transport regime, the draftsmen created an even stronger exception for air and sea transport. Article 80 para 2 EC states that the EC Council of Ministers determines whether, to what extent, and by what procedure, appropriate provisions (for air transport) may be adopted. The treaty’s section on transport further envisages the elimination of various barriers to the free movement of

\(^{12}\) Title V in the second part of the EC Treaty, Articles 70-80 EC (previously 74-84 EC). Even though transport is a service, the freedom to provide transport services is not part of the Treaty’s chapter on services. Article 51 EC states that such freedom will be governed by the transport title.

\(^{13}\) Transport was seen as vital to the establishment of a common market. Moreover, the transport sector was highly regulated in all the founding Member States and contained some special features such as the crucial role of infrastructure and associated problem of cost allocation as well as the inability to stockpile transport services, implying a capacity adapted to peak demands.
services in the transport sector, as it does for ever other sector in the economy.

The general integration process proceeded very well during the first years of the treaty’s existence and action was taken on various issues. A far more cautious approach was chosen for the transport sector. In practice, the Council of Ministers as well as the other European institutions delayed taking action towards establishing a Common Transport Policy until a fairly late stage. This was partly because the relevant treaty provisions did not contain a time frame for the adoption of measures and partly because political and financial interests had to be protected. Ultimately, the European Parliament objected to the inactivity of the Council of Ministers and lodged a complaint against it in 1983. To be sure, the above is not to imply a lack of pressure on states to relax their policies on air transport regulation. Although states were used to dealing with air transport relations on a country-by-country basis and to a system which gave national flag carriers substantial protection against competition, the European Court of Justice ruled the general provisions of the treaty to be applicable to sea and air transport as early as the 1974 French Seamen case. In addition, over the years, charter airlines in particular became adept at devising measures circumventing regulations, thereby effectively liberalising the industry (Williams, 1993: 69).

In the second half of the 1980s the situation changed and legislative action was taken as part of the Community’s internal market programme. This programme was issued in 1985 in response to a deterioration of the Community’s competitive position, an increasingly pressing need to integrate and a strengthening of nationalism within the Community. The Commission’s ‘White paper on the completion of the internal market’ (‘White Paper’) set the date of completion at 31 December 1992 and listed the barriers still in place and preventing the establishment of the internal market, the measures that would be required to eliminate those barriers, as well as a time path. Air transport was explicitly mentioned as a sector where the internal market was to be realised. The 1986 Single European Act (hereafter: ‘SEA’) facilitated the

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15 Case 13/83, Obligations of the Council, 1985 ECR 1513.


17 Have1 (1997: 418) notes that the development of the charter industry was to some extent an outgrowth of the insistence on managed trade for scheduled airlines. The traditional understanding was that consumer interests could be served by low fare charter operations, while ‘national’ interests (commerce, services to peripheral and underserved regions) would be performed through scheduled services.

18 Commission: ‘Completing the Internal Market’. Com (85) 310.

adoption of various measures aimed at establishing the internal market by changing the decision-making rule of unanimity into qualified majority.

Shortly before the White Paper was published, the Commission issued a second memorandum on air transport\textsuperscript{20}. An important impulse was the decision of the European Court of Justice in the ‘Nouvelles Frontières’ case, which dealt with tariff agreements between airlines\textsuperscript{21}. The 1974 French Seamen case mentioned above had already clarified that air transport is subject to the general rules of the Treaty, which included the competition provisions. However, the effective operation of these provisions, Articles 81 (prohibition of anti-competitive agreements, decisions and concerted practices which eliminate, reduce or distort competition, unless specific exemptions have been granted\textsuperscript{22}) and 82 EC (abuse of a dominant position)\textsuperscript{23} requires an implementing Regulation. Such a Regulation was created in 1962 (Regulation 17/62), but in the same year a second Regulation (Regulation 141/62) excluded transport from its applicability\textsuperscript{24}. In the Nouvelles Frontières case the European Court of Justice had to clarify how the competition provisions could be applied in the absence of secondary legislation. In doing so, the court noted that article 84 EC imposes on authorities in the Member States, pending implementing rules under Article 83 EC, the obligation to apply Articles 81 and 82 EC. With respect to Article 85 EC, on the powers of the Commission, the court noted that the Commission may investigate cases of suspected infringement. Although the decision itself neither declared any specific illegalities nor imposed upon national authorities or the Commission a legal obligation to act, the court did allow national as well as Commission action against tariff agreements (including their governmental approval). The Commission sensed an opportunity to use its court-validated competence under Article 85 EC. The Member States for their part preferred a say in any final proposals over and above Commission infringement procedures. The decision of the European Court of Justice thus stimulated both the Commission and the Member States to take action (Haanappel, 1989: 74-75, Havel, 1997: 296-297, Button et al, 1998: 41).

In the second memorandum, the Commission analysed the status of the industry and formulated objectives with regard to its future development. It concluded that measures were needed to increase the efficiency and profitability of the sector, as well as improve the quality and

\textsuperscript{20} Air Transport, Com (84) 72, ‘Progress towards the development of a Community Air Transport Policy’. Also referred to as ‘Second Memorandum’.

\textsuperscript{21} Case 209-213/84, 1986 ECR 1425.

\textsuperscript{22} Article 81 para 3 EC notes that the prohibition of Article 81 para 1 may be declared inapplicable, either individually or generally.

\textsuperscript{23} Previously Articles 85 and 86 EC.

lower the prices of its services. Competition policy was assigned an important role. The memorandum did not address services to third countries. In its analysis the Commission drew on experience gained in the United States, where the domestic air transport market had been deregulated in 1978 and where a radical restructuring of the industry had occurred\(^{25}\). Although the initial situation in the United States differed substantially from that in Western Europe, in formulating its proposals, the Commission was aware that certain sensitivities made it important to avoid any repetition of the US experience in Europe (Second Memorandum, 1984: at 42-43, Button, 1996: 276). It thus decided upon a different course. The strategy adopted was a phase-wise liberalisation which would be accompanied by a common policy. The Commission thus preferred a 'learning by doing approach' to a 'Big-Bang approach', as had been chosen in the United States (differently, Havel, 1997: 140-141). The EC programme comprised three main packages of measures, each independent of the other two and not fully planned. They were aimed at liberalising the sector in three phases: 1987-1990, 1990-1992 and 1993 onwards. Emphasis was thereby placed on the process, with a gradual implementation of measures enabling an analysis of their effects and a tailored amendment of rules in each successive phase. This allowed Member States at least partially to accommodate domestic sentiments and to create a structure considered fair by each of the parties. It also lowered uncertainty, which was further reduced by explicit goals and phases that were part of the White Paper. Some uncertainty remained due to the vagueness inherent in the internal market concept\(^{26}\). In addition, the programme was not entirely clear about the regime that should ultimately prevail in the market, nor about the level of intervention that would still be allowed in order to protect the public. Finally, an 'internal market' disregards the global character of air transport.

Apart from actions taken at the Community level and actions taken by charter airlines, liberalisation occurred through changes in existing Bilaterals. The first was the 1978 protocol amending the 1957 Bilateral between the United States and the Netherlands, which had a spillover effect on other European states (Schreurs, 1983: 91, Havel, 1997: 157-159). In 1984, the United Kingdom and the Netherlands agreed on a Bilateral that basically freed the market between the two countries (Doganis, 1991: 64, 79). It was soon replaced by an even more liberal agreement.

In 1987, the ECAC member states concluded an agreement whereby they could share capacity up to a maximum range of 45%-55%. A trial period of two years was agreed. Another element was the introduction of tariff zones, whereby tariffs within a zone would automatically

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\(^{25}\) Supra, p. 85.

be approved (recall that governments could require approval of tariffs agreed through IATA procedures). This had a limited deregulatory effect and facilitated the introduction of Community measures.

4.3 - European air transport packages

The first regulatory package was agreed in December 1987\textsuperscript{27}. The package contained the measures from the ECAC agreement mentioned above and included legislation on fares, market access and capacity determination. In addition, Regulation 3975/87 implemented the competition provisions by setting out the customary procedural provisions in the air transport sector relating to obtaining individual exemptions, with an opposition procedure, the Commission’s powers of investigation and its powers to impose fines (Kapteyn, VerLoren van Themaat, 1998: 1205)\textsuperscript{28}. Since some of the customary industry agreements had a positive effect on transport and could potentially benefit the public, a second Regulation, namely Regulation 3976/87, empowered the Commission to grant block exemptions\textsuperscript{29}. The block exemptions that were issued applied, among other things, to capacity and pooling agreements, computerised reservation systems and ground handling agreements\textsuperscript{30}. The first package was limited in territorial applicability to traffic between Member States, and its effect was small. The greatest effects were seen in those states that were already prepared for a freer market, such as the United Kingdom. France, by contrast, declared that it would keep its national market closed and maintain a policy of single designation (Dempsey, 1987: 97, Doganis, 1991: 81). A small number of new carriers entered the market and a few regional carriers expanded their activities, while some carriers made use of larger fifth freedom opportunities.

The second package, issued in July 1990, elaborated on the measures from the first package\textsuperscript{31}. The effect of this phase was equally small, mainly because the prevalent economic situation did not stimulate firms to start up new activities but rather provided an incentive for consolidation.

Also in 1990, an initiative of the EFTA countries\textsuperscript{32} led the Commission to start negotiations.
with these countries. Its objective was to enter into a multilateral agreement, based on the provisions from the first package. When agreement was reached in 1992, the territorial scope of the Community measures had been expanded to all of Western Europe, with the exception of Switzerland.

The third package entered into force on 1 January 1993. As of 1994, it has also been fully applicable to the countries constituting the European Economic Area (hereafter: ‘EEA’), namely the Member States, Iceland, Norway and Liechtenstein (Havel, 1997: § 4.2.5.2.2, Kapteyn, VerLoren van Themaat, 1998: 1202). Again, Switzerland is not a member, notwithstanding its long negotiations with the Community. A liberal trade agreement, also covering air transport, was signed with Switzerland at the end of 1998 but, at present ratification is still pending.

4.4 – Current Community structure

This section describes the main features of the current Community structure. Loosely speaking, the structure is built around six items, namely price approval (tariffs and charges), market access (including routes), capacity, competition policy, harmonising measures and measures aimed at airports. These items will be addressed in turn.

The airlines may freely determine tariffs without governmental approval. As a way of protecting the public, Member States may require tariffs for scheduled services to be filed in advance and to be made public. Further, a safeguard clause allows Member States or the Commission to intervene when an extremely high or low tariff is issued in a market in which there is already an opposite trend. A proposal for the regulation of airport charges is pending at the Community level.

As to market access, Bilateral agreements among the Member States and the EEA states no longer apply. The agreements no longer have practical relevance, apart from incidental provisions that extend beyond what Community rules provide or provisions that cover a different area. Bilaterals with third countries have remained in force. A carrier with an air

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33 Regulation 2407/92 on licensing of air carriers, Regulation 2408/92 on access for Community air carriers to intra-Community air routes, Regulation 2409/92 on fares and rates for air services, Regulation 2410/92 amending Regulation 3975/87 and Regulation 2411/92 amending Regulation 3976/87. OJ 1992 L 240.
36 An example of a provision that (until April 1997) extended beyond Community provisions was cabotage. The Bilateral between the Netherlands and the United Kingdom initially also outpaced the gradational establishment of the new order (Havel, 1997: 303). An example of a provision that covers a different area is a Bilateral provision dealing with fifth freedom traffic to a third country (e.g. KLM via Germany to Bangkok). Differently, Kapteyn, VerLoren van Themaat (1998: 1203, footnote 421), stating that such behaviour is no longer allowed on the basis of the ERTA doctrine. Section 4.5.6.1 will look at the remaining powers of the Member States.
operator’s certificate\textsuperscript{37} can obtain an operating licence, which has to be issued if the carrier has the financial means to adhere to the rules that apply to service provision during the first two years of its existence, is willing to comply with those rules and is able to do so (‘fit, willing and able’). The carrier has to maintain its principal place of business in the state that issues the licence. The provisions of the EC Treaty have also influenced the traditional Bilateral nationality requirement. A fundamental feature of the EC Treaty is the right of establishment and free movement of goods, services, persons and capital, which implies that every Community airline has a right of establishment in any Member State. As a result, the nationality requirement no longer applies at the domestic level but at the Community level. ‘Community carrier’, both chartered and scheduled, have unlimited market access. This is not to say that they are allowed to start operating a service, because access is subject to a route authority for scheduled services or a charter permission and may include an authorisation procedure. Regulation 2408/92, however, implies that access cannot be withheld without an objective reason\textsuperscript{38}.

Capacity may be freely determined and the equal opportunity requirement is interpreted as an equal starting position.

The relaxation of ex ante rules has increased the role of competition policy. Section 4.3 noted that Articles 81 and 82 EC have been implemented by Regulation 3975/87, while Regulation 3976/87 has empowered the Commission to grant block exemptions. The Regulations have been amended over time, as have the block exemptions. At present the only block exemption that is still valid is Regulation 1617/93 dealing with slot co-ordination. Article 86 EC\textsuperscript{39} also needs to be mentioned here. Firms in the air transport industry often have a special position in the economies of Member States, which may affect the application of treaty rules\textsuperscript{40}. Member States may, for instance, give domestic firms a preferential treatment, or firms may claim that the special tasks with which they are entrusted exempts them from some of the treaty provisions. Article 86 para 1 EC confirms that the treaty provisions are applicable to the actions of Member States in relation ‘to public undertakings and undertakings to which Member States grant special or exclusive rights’, while Article 86 para 2 EC provides for a

\textsuperscript{37} The certificate certifies that the carrier possesses the professional skill and organisation needed for the safe operation of air transport activities listed in the certificate.

\textsuperscript{38} Supra, p. 63.

\textsuperscript{39} OJ L 373 of 16 December 1991. Article 3 para 2 Regulation 2407/92 states that the licence does not in itself confer any access to specific routes or markets. See Case no. VII/AMA/I/93, OJ 1993 L 140 (Viva Air), mentioning an automatic authorisation to exercise traffic rights except where a specific provision states otherwise. The list of exceptions includes public service requirements, rules on safety, congestion and environmental protection, as well as restrictions due to slot co-ordination. Authorisation has to be issued within a short time frame (Havel, 1997: 320, footnote 517).

\textsuperscript{40} Previously, Article 90 EC.

\textsuperscript{41} Note that state ownership in itself does not determine whether the article is applicable to a firm.
very limited exemption from treaty rules in respect of 'undertakings that are entrusted with the operation of services of general economic interest (…)' Kapteyn, VerLoren van Themaat (1998: 933) mention the transport obligations for non-viable routes as an example\textsuperscript{41}. Article 86 para 3 EC gives the Commission the powers to issue appropriate Directives or Decisions to Member States in order to ensure compliance with the first two paragraphs. These Directives or Decisions may, for instance, target discriminatory treatment or unacceptable price setting. Finally, competition may be distorted via the provision of financial aid, and the treaty provisions dealing with state aid Articles 87-89 EC are an important element of the structure. Among other things, they prescribe the notification of aid prior to its distribution and give the Commission surveillance authority to review and approve aid proposals and to require their withdrawal or modification.

Harmonising measures include the technical aspects of carrier licensing and the licensing of personnel. The first category is the responsibility of the JAA\textsuperscript{42}. Some JAA regulations, or ‘Joint Aviation Requirements’ (‘JARs’), are implemented through Regulation 3922/91 on the harmonisation of technical requirements and administrative procedures\textsuperscript{43}. Domestic requirements will apply until European rules enter into force.

Of specific relevance to airports is the 1985 Schengen agreement. Although at first not part of EC legislation and not specifically aimed at air transport, the agreement abolished border controls on persons travelling between its member states\textsuperscript{44}. This had serious implications for airport layout and traffic flows. At the time of writing all Member States were party to the agreement, except for Denmark, Ireland, the United Kingdom, Sweden, Austria and Finland. The Treaty of Amsterdam incorporated the ‘Schengen acquis’ into the EC structure. A final development of some relevance has been the introduction, via the Maastricht treaty, of an initiative to facilitate trans-European infrastructural projects (‘Trans-European Network’ or ‘TENs’))\textsuperscript{45}. Transport is one of the areas where these networks are to be established. They are to create better, safer and cheaper transport via the removal of legal obstacles and the selection of certain high priority Community projects (Kapteyn, VerLoren van Themaat, 1998: Chapter XI, § 7.4). Fourteen priority projects have been selected, including one airport project. Finally,

\textsuperscript{41} The existence of a formal procedure by which these obligations are imposed and the derogation from the general regime of Regulation 2408/92 may seem to have reduced the scope for airlines to resort to Article 86 para 2 EC. Similarly, in the airport sector the Commission has more than once rejected an appeal on this provision (see Slot, Skudder (2000: 1-9)). However, the actual operation of Article 86 para 2 EC calls for an investigation into the treaty provision that is being infringed and the operation of the service that requires an exemption. This is essentially a case-by-case approach. Firms may thus still invoke the provision, for instance, to justify differential tariffs or a discriminatory treatment.

\textsuperscript{42} Supra, p. 62.

\textsuperscript{43} Regulation 3922/91, OJ 1991 L 373.

\textsuperscript{44} Agreement of 14 June 1985 between the governments of the BENELUX countries, Germany and France.

\textsuperscript{45} Council Decision 1692/96, OJ 1996 L 228.
the ground handling markets at Community airports will gradually be opened up until 2001\textsuperscript{46}.

More recently, the Commission has issued proposals dealing, among other things, with the implementation of the competition provisions on external air transport and external air transport relations generally (Balfour, 1995: 29, 168, Kapteyn, VerLoren van Themaat, 1998: 1205)\textsuperscript{47}, but in this area no real progress has been made. Some progress has been achieved in decision-making, however. The 1992 Treaty of Maastricht introduced the co-operation procedure into decision-making in air transport, while the 1995 Treaty of Amsterdam replaced co-operation by co-decision.

The air transport packages and accompanying measures described in this section aim to provide an all-encompassing regime. The Community structure is unique in the sense that no other group of countries has integrated their air transport markets to such an extent. Nonetheless, air transport is a global activity and the Community is not a self-contained market. Many carriers from third countries are active on the internal market. In 1999, for example, passenger throughput at Schiphol airport was 36,425,113, of whom 20,168,638 travelled to and from the 15 EC Member States (Amsterdam Airport Schiphol, 2000), which means that approximately 44\% of total passenger traffic was governed by structures other than the Community. The activities of third country carriers within the internal market and remaining Bilaterals with third countries continue to affect the Community structure.

The next section describes the most important participants in the exchange of air transport rights. Some of these parties also appear in the Bilateral structure (see Section 3.3) while others are specific to the Community. The differences between the Bilateral and Community players identified here will help explain the differences between the Bilateral and Community structures identified in Chapter V\textsuperscript{48}.

4.5 – Parties to the transaction

4.5.1 - EC Commission
The Commission is a non-partisan body comprised of representatives of the Member States. As at 1 January 1997, following the accession of Sweden, Austria and Finland, the number of members stood at 20. Members are appointed by the Member States, in principle by common accord of their governments. In practice, however, each government announces its choice

\textsuperscript{46} Directive 96/67, OJ 1996 L 272.
\textsuperscript{47} Com (97) 218.
\textsuperscript{48} For a general overview and elaborate discussion of the Community institutions see, for instance, Kapteyn, VerLoren van Themaat (1998), Chapter IV, specifically, sections 1-7 and 10.
unilaterally. The appointment is for five years and is renewable. In performing their duties, Commissioners are required to be independent and neither to seek nor take instructions from any quarter. The Commission meets weekly and in principle decisions are taken by a simple majority. Although it acts in close co-ordination with the Council of Ministers, the Commission, unlike the Council of Ministers, enjoys some measure of autonomy from the influence of member governments. One reason is that the Commission acts as a whole. As a result, members can only be sent home collectively and not individually. The Commission has several tasks. For instance, it can render Opinions and issue Recommendations to the Council of Ministers on issues related to the EC Treaty as well as execute policies which have been decided. It may also represent the Community and sometimes negotiates on behalf of the Community, examples being the EEA negotiations (see Section 4.3) and the GATS negotiations in the early 1990s. Furthermore, the Commission is responsible for proposing new legislation and revising existing legislation. Finally, the Commission has a duty to oversee EC developments and to ensure that business transactions are conducted in conformity with the relevant provisions of the EC Treaty. This supervisory function includes the power to investigate alleged infringements of competition law and has been important to the development of the Community structure.

Despite appearances, the actual power exercised by the Commission is limited. A few factors play a role. To begin with, although the Commission has powers of its own, information asymmetry may in effect make the Commission dependent on co-operation of Member States in reporting violations of competition law and in effectively eliminating these violations. From an institutional point of view, the co-operation of the Member States is needed in the adoption of legislation and realisation of their intended effect. Finally, the Community institutions only have those rights that are explicitly conferred on them.

4.5.2 – EC Council of Ministers

The Council of Ministers (hereafter: ‘Council’) is the governing body of the EC, as well as a negotiation and executive body, ultimately responsible for realising the objectives of the EC Treaty. The Council is not the same body as the European Council, which consists of the heads of state and government of the Member States meeting with the President of the Commission and assisted by Ministers of Foreign Affairs and other Commission members. The Council is the institution in which Member States are represented as such and through which they participate in the political and legal activities of the EC (Kapteyn, VerLoren van Themaat, 1998: 187). The Council is made up of representatives of the Member States who act in accordance with instructions given to them by their respective governments and who are authorised to bind their governments. In performing their tasks, members of the Council
always have to take into account the instructions from and their relationship with the home country, where the proposal has to be defended and approved. In this respect the Council differs from the Commission, whose members are independent. In some Member States relationships between the delegates and the state are essentially formalised. Denmark, for example, uses a system whereby a delegate operates under an explicit mandate from its national parliament, the Folketing (Westlake, 1995: 59, 346-348). On the one hand, such a mandate could form an obstacle to efficient decision-making as it limits the opportunity for making compromises. On the other hand, the mandate provides guidance to the representative and helps the state to control the representative’s behaviour. Furthermore it increases the chance that an agreement - when concluded in accordance with the mandate - will be upheld domestically and so generates lower implementation costs.

The composition of the Council depends on the policy field. For instance, there is a Council of Ministers of Finance, of Industry and of Transport. Each of these sectoral Councils develops its own distinctive character and practices. In part this follows from treaty provisions on voting requirements and decision-making procedures as well as from the nature of the subject matter. It can also result from the status of ministers. The members of any given Council often develop a sense of familiarity especially if their Council meets frequently. This in turn can lead to an ‘esprit de corps’ and a strong sense of corporate identity, particularly vis-à-vis other sectoral Councils and institutions and even vis-à-vis domestic institutions (Westlake, 1995: 60). The frequency of Council meetings varies. The General Affairs Council, for instance, meets once a month whereas the Transport Council only meets about four times a year. In the intervals between meetings, there is frequent contact and proposals for decision-making are processed by both administrative and political auxiliary bodies of the Community, such as the Committee of Permanent Representatives (Van Schendelen, 1996: 533). The Presidency of the Council rotates among the Member States and the President has become increasingly important for resolving matters, for instance through brokerage. In addition, the Presidency may try to influence legislation through setting the agenda and issuing a legislative programme at the start of its 6-month term. During its Presidency in the first half of 1997, the Netherlands, for example, tried to get an agreement on the introduction of a tax on emissions in air transport as well as a Commission proposal on ‘non-addition’ of noisy aircraft belonging to the ‘Chapter III’ category (Ministry of Transport, 1998). The Council is the only Community institution with decision-making power, except where and to the extent that power has been entrusted to other organs or institutions. An example of such delegation is the Commission’s competence in competition policy. Even though the EC structure is relatively open, Council meetings are

49 A different view of the relationship between the representative and domestic constituency is formulated by Corbey (1993: 170-172), who points out that the EC provides the opportunity of taking unpopular decisions
secret. Public discussions, it is believed, could frustrate an agreement.

The Council is aided by the Committee of Permanent Representatives, or ‘COREPER’. COREPER is formed by representatives of the Member States, seconded to Brussels. It prepares Council meetings and performs certain executive tasks. The preparation of meetings entails the process of agreeing on and formulating material to be submitted to the Council. This function in effect exerts a powerful influence on decision-making, and some studies estimate that about 90% of Council decisions are actually taken at this level (Westlake, 1995: 291, 294-295, 370). Furthermore, COREPER constitutes the exclusive communication channel between the Commission and Member States, thus performing important information gathering and processing tasks. In practice, COREPER members tend to adopt a frame of reference broader than their own countries’ needs or at least understand the requirement of satisfying the national interests of individual Member States and the additional interest of the Community (Kirchner, 1992: 76). The Committee thus serves as a harmonising force.

4.5.3 - EC Parliament

The political system in Europe requires democracy at every level. Accordingly, the Community’s institutional structure needs to be subject to democratic control (Nicol and Salmon, 1994: 226-228), which is the role of the European parliament (hereafter: ‘Parliament’). Parliament consists of directly elected representatives of the citizens of the Member States. It serves to advise the Council on matters pertaining to the development of the Community and holds certain decision-making powers.

The repeated criticism that the Community’s law-making process is too far removed from the people and is not subject to a democratic control mechanism has over the years led to an increase in Parliament’s powers. For example, a procedure has been introduced whereby the Commission and Parliament agree on a legislative programme annually. Parliament’s influence has also increased as a result of the practice of the Presidency presenting its legislative programme at the beginning of its term and reporting back on its achievements at the end (Westlake, 1995: 342). Specific to air transport has been the introduction of the co-decision procedure in air transport which has made Parliament a legislative partner completely equal to the Council.

4.5.4 - EC Courts

The EC Courts are the European Court of Justice and the Court of First Instance, established in 1988. The Court of Justice holds adjudicative powers vis-à-vis Member States, institutions without risking the alienation or frustration of the domestic electoral base.
and individual persons, including firms which are located in the Community\textsuperscript{30}. The Court of First Instance handles disputes between individual persons, but is not competent in disputes between Member States, or between Member States and Community institutions. Individuals can bring an action against a Member State in a national court for infringement of any directly effective provision of Community law, whether or not it has been incorporated into national law. Member States and Community institutions may also ask the Court of Justice to establish an infringement of the EC Treaty by the Council, the Commission or Parliament for failing to act, having been called on to do so. Note that the European Courts operate alongside domestic courts, which are required to apply Community law. It may be argued that the national courts should adjudicate every dispute because of their superior local information. However, in the matter of air transport the argument loses force in the light of the international nature of these activities. Moreover, the adjudication of international cases by domestic courts may lead to difficult questions of competence and uncertainty.

The existence of international courts, capable of issuing binding verdicts and imposing sanctions is a fundamental feature of the Community governance structure. Apart from adjudicating specific cases, the EC Courts play a harmonising role through their case law. This enables and sometimes obliges domestic courts to ask for an interpretation of a provision via a preliminary ruling\textsuperscript{31}.

Section 4.7.4 will look at some specific aspects of the Community's dispute resolution mechanisms in air transport.

Two final parties need to be mentioned, namely ECOSOC and the Committee of the regions. ECOSOC represents employers, workers and independent persons. Numerous articles of the EC Treaty - including those on air transport - require the committee to be consulted by the Council and the latter also consults the committee optionally. The committee's opinions are not binding on the Council. The Committee of the Regions consists of representatives of regional and local bodies. It has advisory functions and must be consulted where the EC Treaty so provides. The Treaty of Amsterdam requires that the committee be consulted on matters relating to air transport. Given their consultative roles, the influence of these committees is greatest at working group level during the contact and contract phases.

\textsuperscript{30} In some cases even third country firms, see Commission Decision 202/85 and Cases 89, 104, 114, 116, 117, 125/129/85, 1988 ECR 5193 (Wood Pulp). Although this case is not specifically related to air transport, there are some implications as it deals with the imposition of fines on third country firms that were involved in price co-ordination activities. These activities had the object and effect of restricting competition within the common market (Haanappel, 1989: 78).

\textsuperscript{31} This opportunity was used in the French Seamen case (supra, p. 92). The European Courts can also initiate new policies and legislation. An example is the 1983 case of Parliament against Commission (supra, p. 92), which motivated the Commission to become more active in developing the Community's transport policy.
4.5.5 - Objectives of the EC institutions

The overriding objective of the EC Treaty has already been identified as the economic integration of the Member States. An efficient transport sector can help to realise this objective and the treaty requires a Common Transport Policy. According to Jarzembowski (1998: 15) the goal of this policy is to ‘further integration in the transport sector so as to create a functional European transport market, and in addition ‘to create “long-term stable mobility”, combining the business’ and citizens’ desire for mobility with the citizens’ desire for protection of the environment’. The key term is ‘sustainable mobility’. On air transport, Balfour (1995: 268-269, 271) opines that the Community’s objective is to try and realise the benefits of the internal market by eliminating barriers to the free movement of services and by developing a common policy. The Second Memorandum (1984) notes that such a common policy would be directed at raising the efficiency and profitability of the sector, as well as lowering prices and improving the quality of its services. The memorandum includes some social objectives, such as those concerning the mutual conditions of licences and employee working conditions. These objectives are limited, however, given that Member States do not hold a common view on the question of whether social Europe is an integral part or merely a by-product of economic Europe (Molle, 1990: 420, Kirchner, 1992: 102-103). The above description illustrates that the European Community is a collection of different Member States and institutions each with their own objectives, making it difficult to formulate a ‘Community objective’. More recently, environmental protection has been introduced into policy documents and it is now acknowledged that air transport has serious consequences for the environment (Jarzembowski, 1998: 16). The greater attention to environmental protection may also be inferred from the Treaty of Amsterdam, which inserts into the EC’s institutional structure the obligation to integrate environmental policy with other policies. At the same time, the integration requirement does not mean that environmental interests are given preference, nor that the Community will be able to ensure an adequate level of protection.

Turning to the individual European institutions (Second Memorandum, 1984: 3-5), various proposals and memoranda show that the Commission has been the most vocal proponent of amending the traditional structure. This is only natural, given the Commission’s role as

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52 The objective of sustainable development is also inserted in Article 6 EC and embraces the preservation, protection and improvement of the quality of the environment as well as the prudent and rational utilisation of natural resources (Kapteyn, VerLoren van Themaat, 1998: 1356). See also the Communication from the Commission, ‘Air Transport and the Environment, Towards meeting the Challenges of Sustainable Development’, Com (99) 640.

53 In many instances the competitive position of the air transport industry is at stake and there is a preference for developing proposals at a global level (in ICAO) (For instance, Kinnock, 1999). Section 5.8 will further discuss the effectiveness of the Community structure in pursuing the goal of environmental protection.
guardian of the treaty and EC development. Parliament has been of the opinion that the performance of the air transport industry both can and must be improved, but has favoured a 'go-slow approach', pointing to the extremely complex nature of the industry. The opinion of ECOSOC has been even more conservative and has concerned safety and the interests of airline employees. The Committee has suggested that action should be considered on several of these social issues. The opinion of the Council has varied depending on the proposal being decided, and the economic conditions, traditions and air transport policies in the Member States. The position of the Member States that make up the Council will be detailed further in Section 4.5.6.

It should be noted that the objectives described in this section only concern internal policy. In its proposals on an external air transport policy (supra, Section 4.4), the Commission has already stated in general terms the objectives of such a policy. Broadly speaking, it should enable all Community carriers to take advantage in the international context of benefits created by the internal market and thus to relax bilateral constraints, while at the same time ensuring reciprocity of opportunities. The policy should further the interests of users, who are generally served by a removal of regulatory and competitive constraints on carriers and not by national protectionism, and the interests of regions, by facilitating access to regional airports (Balfour, 1995: 278).

4.5.6 - Member States

4.5.6.1 - General remarks
The position of the states has changed as a result of their participation as Member States in the development of the Community and a gradual implementation of the various air transport packages. The exchange of air transport rights still takes place between states, but the nature of the exchange has changed from an intergovernmental treaty to EC legislation, which is a type of semi-specific governance structure. The sovereign position of the states has been restricted by their status as EC Member States. Community co-operation has meant state interdependence and a reduction in domestic powers. The greater powers at the Community level have increased the need for co-ordination between domestic and European positions. To facilitate such co-ordination, each Member State has set up a European secretariat in Brussels, where the ministries' views and interests can be reconciled into a co-ordinated position. These inter-ministerial forums are responsible for preparing and commissioning messages to the Brussels, or permanent, representatives of the states (Dinan, 1998: 297-301). As at December 1999, the permanent representation of the Netherlands had a staff of 48, with diplomatic status as well as support services (Interinstitutioneel Jaarboek, 1999). The staff are either members of
the diplomatic service or seconded to it from the home country (Nicoll, Salmon, 1994: 69). Every ministry has its representatives in the permanent representation and hence a direct representation of its own interests as well as a ‘barometer’ of its specific policy areas. Contact can be established more directly and efficiently than via formal co-ordination channels. At the same time, each representative is also in frequent contact with his home country. As is true for a Council representative, a permanent representative needs to have the confidence of the party he represents in order to be effective.

Section 4.3 made clear that the current regulatory package does not exclude the ability for Member States to pursue a domestic air transport policy (also, Balfour, 1995: 275). Yet, this ability has been reduced in the following ways.

First, Bilaterals are no longer used as an instrument in air transport by and between Member States. The domestic market of each Member State has been opened up to carriers for whom the requirements of effective ownership and substantial control apply at a Community level. There is the requirement of a route authority and there may be some entry barriers in the form of slot co-ordination or public service requirements. However, these instruments can only be justified on the basis of objective criteria, such as infrastructural constraints. Member States are further constrained by the central principle of Community membership, namely Community loyalty (or: solidarity), as laid down in Article 10 EC. This provision binds all national institutions that hold public authority, requiring them to take all the steps needed to comply with the obligations imposed by the EC Treaty and to facilitate the tasks of the Community. It also obliges them to refrain from any action that impedes the realisation of the treaty’s objectives. In addition, Article 10 EC touches upon the Member States’ powers to conclude Bilaterals with third countries or to determine their content. Some provisions are more expressly directed at these powers. An example is Decision 80/50, requiring Member States to consult each other on air transport matters being handled in international organisations. The Decision also requires Member States to provide information to the Commission and other Member States on developments in their air transport relations with third countries (Balfour, 1995: 265). The ‘ERTA doctrine’ is another direct constraint. According to this doctrine, whenever the Community lays down rules with a view to implementing a common policy envisaged by the EC Treaty, Member States acting individually or even collectively lose the right to contract toward third countries obligations affecting that policy. The doctrine has been

54 A public service requirement is defined as an activity exercised by either a publicly or a privately owned enterprise which is generally in the public interest and carried out under governmental supervision and regulation (Second Memorandum, 1994: annex IV, p. 16). By 1996 more than 100 intra-Community routes had been opened under the new Regulation (Commission, 1996: 7).
55 Supra, p. 92.
56 Case 22/70, 1971 ECR 263.
expanded in Opinion 1/76\textsuperscript{37}, which has found that the Community also has exclusive competence if internal measures can only be adopted after an arrangement with third countries has been concluded, provided that such an arrangement is also necessary to achieve an internal Community objective (Kapteyn, VerLoren van Themaat, 1998: 1178-1179). The Commission tried to obtain more clarity on the division of powers between the Community and the Member States at the time when the GATS agreement was concluded (1993). In a request to the European Court of Justice it wanted to find out whether the Community had exclusive competence to conclude the agreement or whether both the Community and the Member States should become signatories. One of the arguments was that international trade in services formed part of the commercial policy (implying an exclusive Commission competence on the basis of Article 109 EC\textsuperscript{58}) (ibid. 1278, Mahler, 1995). This view was rejected by the Court of Justice. With respect to transport services, which were an element of GATS, the court noted explicit provisions in the transport title covering these services foreclosing the subsumption of transport services within the common commercial policy. The Court of Justice further rejected the attribution of competence based on the mere establishment of common internal rules in transport, particularly when not all transport matters were already covered by common rules. Exclusive Community competence would have ‘to be established on the basis of the ERTA doctrine or on the basis of specific clauses in EC legislation ... dealing with negotiations with third countries’ (Kapteyn, VerLoren van Themaat, 1998: 1279, 1348)\textsuperscript{59}.

The situation has become more complicated as, in 1996, the Council granted the Commission a ‘split mandate’, namely to open multilateral aviation talks with the United States, but to conduct negotiations in two discrete, mutually dependent cycles. The current mandate covers only soft rights. Furthermore, the Commission has started infringement proceedings (based on Article 226 EC) against various Member States that have concluded Open Skies Bilaterals, claiming that these actions may distort the operation of the common air transport policy\textsuperscript{60}. The Netherlands is one of the Member States targeted, notwithstanding that its Open Skies agreement with the United States was concluded long before the Community structure had been implemented\textsuperscript{61}. At present, it is unclear how and when the Commission’s competence will be fully implemented as the ERTA doctrine requires a case-by-case approach (Balfour, 1995: 288-290). As a result, Member States face an increasingly complex

\textsuperscript{37} European Laying up Agreement for Inland Waterway Vessels, 1977 ECR 741.
\textsuperscript{38} Previously Article 113 EC.
\textsuperscript{39} Advisory Opinion 1/94 of 15 November 1994, CRS I-5267.
\textsuperscript{40} Article 226 EC (previously Article 169 EC) Cases C-466/98 Commission against United Kingdom, C-467/98, Commission against Denmark, C-468/98 Commission against Sweden, C/469/98 Commission against Finland, C-471/98 Commission against Belgium, C-472/98 Commission against Luxembourg, C-475/98 Commission against Austria, C-467/98 Commission against Germany (Kapteyn, VerLoren van Themaat, forthcoming).
environment in which they are uncertain as to the exact division of powers.

Finally, competition law imposes an important constraint, both within and outside the Community. Article 86 EC and the provisions on state aid, in particular, prevent Member States from frustrating competition through preferential treatment of the domestic air transport industry and similar measures.

Notwithstanding any loss of domestic powers, the Community's framework structure makes states the key to realising the treaty's objectives (also, Schout, 1999: 21). Various provisions make the states responsible for giving effect to these objectives. To illustrate, states must provide for the implementation of Directives, and the actual operation of provisions in Regulations may depend on domestic action. Regulation 2407/92, for instance, allows Member States to issue licences and to attach conditions to these licences. This position may in some instances hinder integration as Member States are ambivalent about the overall benefits of integration. While they acknowledge that there are benefits, they are reluctant to accept proposals in individual cases (Jansen, De Vree, 1985: 374). Moreover, they differ in their policies and attitudes towards the Community and in their ways, methods and opinions (Wallace et al., 1983: 7). Smaller states, for example, traditionally fear domination by France and Germany. Ironically, these two states joined, if not formed, the European Community to end the recurring hostilities between them and to tie Germany to Europe (Jansen, De Vree, 1985: 99). The difference in views on European co-operation can also be witnessed in the transport sector (Dinan, 1998: 297-301). Generally speaking, larger economies, or those in which airline operations are small relative to the size of the market and commercially weak, have less incentive to support a more open system (OECD, 1997: 95), whereas countries that are small in terms of population and area have a stronger interest in a more open regulatory system. The Dutch preference for liberalisation (see Section 3.3.1.3) supports the claim. Their preference for liberalisation is in line with the Community's objective of integration, but does not imply a complete harmonisation of interests. The element of environmental protection, for example, which has been identified as an important Dutch air transport goal, has led to stricter requirements than the equivalent obligations at the Community level. In addition, the rights to third country traffic in any future development of Community policy form a potential source of conflict for the Dutch because larger Member States are likely to claim a large part of those transport rights. Disputes over the allocation of transport rights earlier prevented any substantial co-operation among European states. Such controversies may hinder the operation of the Community structure.

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4.5.6.2 - Implementation of the air transport goal in the Community structure

The above discussion shows that Member States face legal and practical limitations both in formulating and realising domestic policy goals. At the same time Member States are essential to the EC development and there are many instances where there are opportunities to influence the course of that development. These factors raise the risk of opportunism but also increase the need to be well-prepared in interstate negotiations and to maintain well-designed state-industry relationships. Before turning to these relationships, this section addresses the implementation of the Dutch air transport goal within the Community structure. The requirements that capture the selective network goal and the instruments that have been created to realise the goal fall into the following categories (see also Section 3.3.1.4):

1. the volume of traffic,
2. the composition of the fleet of aircraft that use Schiphol airport and
3. market behaviour.

4.5.6.2.1 - Traffic volume

Section 3.3.1.4.1 listed the requirements imposed on the industry, namely a cap on the volume of traffic, restrictions on night flights and capacity clauses dictating a specific capacity. Instruments available to force the industry to meet these requirements are the airport designation, slot co-ordination and access policy (i.e. authorisation of ad hoc flights or charters). The Community structure, which is based on free market access, has complicated the imposition of some requirements.

4.5.6.2.2 - Fleet composition

The requirements targeting fleet composition include certain Bilateral clauses and the delegation of responsibility to develop the ‘Marshall plan’ to airlines. States may agree on phasing out noisy aircraft. This instrument is addressed at the Community level by Directive 92/14, which aims to phase out ‘Chapter II’ aircraft by 1 April 200263 and has also been introduced at the domestic level. For Dutch airlines, it implies restrictions on the use of aircraft belonging to the noisiest types within the ‘Chapter III’ category. The ‘Marshall plan’ addresses states with whom Bilateral relations are maintained rather than the Member States themselves. It will therefore not be discussed further in this chapter.

4.5.6.2.3 - Market behaviour

62 Cases include Sabena, OJ L 216 and ANA (Slot, Skudder, 2000). A private firm may abuse its dominant position. Such abuse may, however, be the result of government regulation.
The airport is required to implement a charges policy that differentiates between aircraft and a system of bonuses or fines to silent or noisy aircraft. The state aims to be selective in the choice of countries with whom Bilaterals will be concluded and the frequencies to be agreed. There are also several measures aimed at stimulating other forms of transport such as high speed trains as well as fiscal measures.

4.5.6.3 - Interstate relations

The Community structure restricts both the imposition of requirements and the use of certain mechanisms and instruments at the interstate level. The many parties involved in the transaction reduce the ability to make secret arrangements. Some instruments, such as the selective choice of a Member State as a trading partner, are not allowed, while the use of other instruments is problematic. For instance, Bilateral clauses between Member States, while not prohibited as such, may be interpreted as a contravention of the ERTA doctrine and lead to legal claims. They are not used as a result. Likewise, any cap on volume conflicts with an important element of the Community structure, namely free market access. At the same time, the right to market access is not identical to the ability to exercise that right. Moreover, the Community structure may allow an implementation that is consistent with domestic interests. Not all Dutch instruments are therefore ruled out by the Community structure. Slot co-ordination, for example, has been permitted at Schiphol airport to protect the environment even though the Community officially allows slot co-ordination only when capacity problems dictate its use. The system in practice serves as a volume cap. A Member State can also pursue policies that encourage substitution towards other forms of transport, notably (high speed) railways. The TEN initiative, for instance, targets the development of train infrastructure. Similarly, the Community structure partly allows a policy directed at fleet composition. Finally, the option of tariff differentiation is permitted.

To avoid the risk that measures going beyond EC rules will be considered in breach of the Community’s market access or non-discrimination agreements, the state could adopt the alternative strategy of pursuing issues at the Community level. With respect to the important social goal of environmental protection, Section 4.5.5 noted that some EC policy documents (for instance, Commission, 1996: v) suggest introducing into the Community structure a larger role for environmental protection. The phasing out of noisy aircraft and taxation of aircraft fuel are being discussed both at the Community and at a global level. On the one hand, a Community approach may increase the likelihood that a state’s policy goals will be realised. This may be especially relevant to a small country like the Netherlands. On the other hand, a state must realise that its domestic influence is limited by the Commission’s right of initiative, the multi-party nature of agreements and the fact that the veto is not part of the Community’s
way of decision-making.

Given that air transport is a global industry, not limited to the territory of the Member States, and that Bilaterals still govern relations with third states, some mention of third countries is in order. Third country traffic is especially important for the Netherlands because of a small captive market and a significant transfer operation at Schiphol airport. Section 4.5.6.1 showed that Member States no longer fully control the content nor conclusion of Bilateral agreements. As an example, a Bilateral usually provides that domestic rules apply, which - given the incorporation of Community law - means that the operation of traffic rights by third country carriers is subject to Community rules. Further, the ERTA doctrine prohibits agreements on Community traffic between domestic powers and third countries. To secure a favourable position before new Community legislation prevents this, Member States and third countries have tried to revise existing Bilaterals. The Open Skies Bilateral in particular has been used as an instrument to secure access to the Community market, in exchange for Member State access to foreign markets, which they would otherwise not be able to acquire. Thus, there is an Open Skies Bilateral between the United States and the Netherlands. More recent initiatives are the Open Skies Bilaterals between France and the United States and between the United States and Italy, concluded in 1998. However, Section 4.5.6.1 noted the infringement procedures initiated by the Commission and the ongoing process of policy formation is creating an increasingly complex situation regarding the competence of Member States. New Community legislation is an additional source of uncertainty and it is not clear how third countries will respond to further restrictions on their Bilateral rights. Apart from the Open Skies strategy, third countries can try to form alliances at the carrier level. This route was initially chosen by Switzerland. Its national carrier, Swissair, secured access to the Community market via a shareholding in the Belgian carrier Sabena and participation in ‘Qualiflyer’. A special category of third countries consists of states that are candidates for EC membership. Currently, negotiations are taking place between the Community and ten European states (Commission, 1999: 16). Prior to their accession, these states will become bound by the corpus of Community legislation and commitments, the ‘acquis communautaire’, in force at the time. ECAC acts as an important facilitator in this process.

To summarise, a smaller influence at the interstate level and a wish to improve environmental protection have led the Netherlands to go beyond Community rules. The strategy of expanding domestic legislation, liberalisation at the Community level and spill-over

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64 Recall from Section 4.3 that the EC and Switzerland have concluded a trade agreement also covering air transport, in 1998.
65 According to Havel (1997: 249, note 89) acquis communautaire literally means ‘Community patrimony’ - ‘The provisions of the constitutive treaties and the secondary legislation adopted thereunder, as well as, self-referentially, the judicial and quasi-judicial decisions of the various EU institutions including the European
effects from third country traffic are altering interstate relations and the competitive position of
the Dutch air transport industry. The state has chosen to tighten its regulation of the industry
and this has increased the state’s reliance on the industry. Yet, without appropriate incentives,
the industry is unlikely to pursue the state’s goals. As an example, the KE PD requirement that
the airport should encourage passengers to use public rather than private transport is being
pursued in an opportunistic way: the airport seems to be taking advantage of the requirement
by raising its parking fees and hence its revenues. Rather than improving the airport’s
accessibility to the public, it has turned its attention to real estate activities and the attraction of
firms to the airport area. Although there has been an increased use of public transport, on the
whole, accessibility has deteriorated. There is a more general problem with tighter domestic
regulation and greater freedom at the Community level. As the industry is confronted with
stricter regulation than what applies to its Community competitors, there is a growing risk that
the industry’s competitive position will be harmed, that the Netherlands will infringe their
treaty obligations and that existing agency problems will be exacerbated. The next two sections
look at the relationships between the state and the airline and airport, respectively, and
elaborate on some of the problems identified above.

4.5.7 - Community carriers
The Community carriers were divided on the issue of liberalisation. The carriers represented in
the Association of European Airlines (AEA) did not support it, contending that their high
operational costs justified safeguards. The weak financial status of some airlines provided an
additional argument and, in part, accounted for the gradual approach that was chosen to amend
the governance structure. Note that during the formation of the Community structure most
carriers took a seemingly hypocritical position, opposing changes in the regulatory regime,
while at the same time actively infringing price regulations by supplying tickets below agreed
rates to non-licence d agents (Williams, 1993: 73-74). The Dutch airlines favoured liberalisation. This was especially true for KLM (Van den Polder, 1993). It had built up a large
network through sixth freedom traffic and was aiming to be one of the few surviving global
carriers. It had a small captive market, yet wanted to obtain a large market share. It was
constrained in its efforts because its competitive strength made many European states unwilling
to enter into liberal Bilaterals with the Netherlands. Liberalisation was seen as an opportunity.

Integration and market access for Community carriers, once certain pre-defined criteria
have been met, have loosened the relationship between the airline and the state. Instead of a
permit and a designation, airlines now require a certificate, a licence and a route authority.
Although a licence in itself does not confer any right of access to a route, access can only be
withheld on the basis of an explicit provision in Community legislation. Some examples are the existence of restrictions at slot co-ordinated airports and routes where public service requirements apply. The certificate and licence are issued on the basis of more or less harmonised rules. The new licensing procedure involves submission of a business plan backing the statement that the relevant criteria have been met. An operating licence can only be granted, and is only valid, if the operator also holds an air operator’s certificate, certifying its operational fitness. If there is a change in the material supporting a licence, the airline is obliged to inform the Ministry of Transport. It may then be required to submit a new business plan. The Ministry of Transport may formulate conditions when issuing licences, provided that they are compatible with Regulation 2407/92. Compared to the Bilateral licensing procedure, the procedure and the information that the airline needs to submit are more elaborate. On the other hand, the information requirements have been standardised. Moreover, standardisation of the procedure and restrictions on conditions have made the grant of a route authority easier than an evaluation of a designation request. The procedure does not differentiate between KLM and other carriers. As in Bilateralism, the ministry may rescind the licence when the licensee has not fulfilled the given conditions.

The freedom to provide services offers airlines more scope to realise their continuity objective. It has led to new airline alliances and has made airlines less dependent on the state. The licence conditions are a weaker instrument than Bilateral designation. The already weak link between the airlines’ performance and pay-off has weakened further, as has the state’s monitoring ability. Slot allocation and the prescription of the types of aircraft allowed have become the main regulatory instruments but, in their current form, do not give appropriate incentives as slot transfers and differentiation across aircraft types are prohibited. In addition, the increased formation of international airline alliances limits the effectiveness of any instruments even further as it reduces the bond between the home carrier and home state.

The airline’s co-operation may continue to be elicited through interest harmonisation and this is partly stimulated by the institutional structure. The Dutch carriers operate both Community and Bilateral services, which provides an incentive to take into account the effect of any opportunistic behaviour on their relationship with the state. An example of such harmonisation can be found in an unpublished memo on the selective network goal (Ministry of Transport, March 1998) where it is stated that, outside the Community, preference is given to those routes that strengthen the international network. This means that scheduled services and a large network are valued. Because KLM is a scheduled carrier and the main operator of the

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66 Balfour (1995: Chapter X), Fennes (1997: 282, note 168), Havel (1997: 392 note 885) and Daalder et al. (1998: 144) all note that Regulation 2407/92 gives Member States some freedom in granting a licence, thereby influencing market competition. As an example, the airline needs to prove that it is able to comply with various requirements and that it needs to do so to the ‘satisfaction of the state’. See also Ministry of Transport (1994).
current network, while its open permit facilitates designation, KLM is generally preferred. Its strong position continues to provide the airline with incentives to co-operate. To strengthen its position in the Dutch air transport system, KLM has increased its shareholding in Martinair (Dierikx, 1999: 352). Thus, smaller domestic airlines (except for Air Holland) are also induced to co-operate with KLM and so indirectly with the state. The state could choose to harmonise interests through financial dependence. Intensified competition and rapid change in a liberalised environment generate some opportunities, because stronger pressure on profits may bring some carriers into financial difficulties. By supplying aid, tying it to certain conditions, and developing adequate monitoring instruments, the state can continue to exert influence. This option has been anticipated at the Community level, however, and in recent years the provision of state aid has been scrutinised more closely, among other things, through the obligation to inform the Commission of any proposed aid prior to its distribution. Furthermore, while Member States are creative in circumventing rules, control through financial dependence is not a long-term solution. Competition law and a supranational compliance mechanism are influencing the state-industry relationship. The states’ ability to give preferential treatment to their own carriers, for instance, by restricting access to certain airports or routes, is subject to Commission scrutiny and corrective action. Within the Community, the competition rules are fully operative. The absence of secondary legislation implementing the competition provisions in respect of air transport between Member States and third countries limits their effectiveness to some extent, but by no means entirely given the powers of Member States and the Commission described in Section 4.2.

In brief, the Community has eliminated some of the instruments available to the state to structure its relationship with the airline and has imposed restrictions on other instruments that may lead to a preferential treatment of and a closer relationship with the airline. At the same time, the state increasingly relies on the industry, including airlines, to realise its transport goal. This reliance has primarily taken the form of new regulations, but the state has failed to create

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67 Dierikx (ibid. 307-308) notes that this has been a general trend in Europe. Note, however, that Section 3.3.2 mentioned the dissolution of KLM’s agreement to buy the remaining shares in Martinair because of the conditions the Commission would have attached to its approval.

68 NRC, 19 January 1999 ‘Staatssteun krijgt steeds nieuwe vermomming’. In a communication on the results of liberalisation, the Commission clearly states that it authorised state aid as a one-off measure to help national carriers adjust to the liberalised single market during transition, and that this transition phase is over (1999: 3).


70 Kapteyn, VerLoren van Themaat (1998: 1200, footnote 400 and 1205, footnote 437) notes that this transport is subject to the ‘Asjes Saeed regime’, i.e. the combined effect of the verdicts in the Nouvelles Frontières and the Saeed Flueggesen cases. In brief, Article 81 EC is not directly effective and can only be applied through Articles 84 and 85 EC. Article 82 EC is directly effective. However, the Commission does not possess the normal powers of investigation, of imposing fines or periodic penalties, or of granting individual exemptions.
appropriate incentives, nor has it adapted its instruments to the new environment. A looser relationship and continued absence of performance incentives have reduced the airline’s incentive to contribute to the state’s selective network goal, while the greater freedom within the Community has made it more difficult for the state to monitor airline behaviour. Similarly, increased regulation contrasts with greater freedom at the Community level and has led to a growing tension between the interests of the state and airline. Although institutional factors may harmonise interests to some extent, they do not compensate for a reduced dependence on the state. Potential agency problems have become more apparent as a result.

4.5.8 - Community airports

The Community airports generally welcomed liberalisation, which they viewed as an opportunity to loosen their ties with the state and to start operating as commercial undertakings rather than mere infrastructure providers and being seen as such. But, despite favourable passenger growth rates and greater marketing opportunities, the airports have failed to take full advantage of their new environment. This can be attributed to a number of reasons.

To begin with, the increased use of hub-and-spoke systems, due in part to liberalisation, has led to strong traffic growth at some airports\(^7\). These airports have become more dependent on their home carriers. In contrast, other airports, primarily servicing feeder-carriers, have experienced a fall in traffic because of a re-routing of traffic flows. This has made the development of airport operations less predictable and has created uncertainty. There has also been a downward pressure on average aircraft size as network carriers increasingly compete in terms of frequency. Airports experiencing growth have run into capacity problems, while hub operations feature wave-type patterns which require tremendous capacity during peaks. These developments have generated significant investment needs. The 1985 Schengen Treaty (see Section 4.4) has contributed to the need to invest. Airports using a single terminal concept, such as Schiphol airport, have needed substantial alteration. Long lead times and in some cases a lack of funds have resulted in widespread congestion. In Europe, it is estimated that US$65-US$80 billion will have to be spent on airports and related infrastructure over the next ten to fifteen years (Arthur Andersen, 1999). Since governments are often unable or unwilling to meet these needs, more airports are now developing new financing strategies involving the private sector. This has contributed to a demand for more industry freedom and has strengthened privatisation trends in the industry\(^7\). Schiphol airport, for example, aims to be privatised in

\(^7\) Data from 33 major European airports indicate an increase in passenger throughput of 6.4% and an increase in aircraft movements of 5.4% in 1998. This follows increases of 7.8% in passengers and 6.4% in aircraft movements in 1997 (ACI, 1997).

\(^7\) See, for example, the 1999 Aer Rianta report. ‘Privatisation’ refers to the transfer of government corporate assets to full or partial private ownership.
the near future. Section 3.3.3 observed that the presumption that air transport harms the environment has resulted in a more critical approach towards the sector and has limited opportunities for expansion. Finally, the introduction of new regulations at the domestic level and the absence of liberalisation at the Community level has contributed to the airports' inability to take advantage of the new environment.

One of the reasons behind airport regulation is that the airlines take a critical stance towards the development of airports as commercial undertakings and have tried to counter this development. The Comité des Sages (1994: 37), for example, considers airports part of the overall public infrastructure providing services to airlines. The committee's report further states that, because of their central position, airports are required to make available the capacities necessary for current and future air traffic loads, regardless initially of any economic considerations, and to provide take-off and landing facilities for all licensed aircraft on a non-discriminatory basis. The Commission also supports airport regulation on the grounds that airports are often entrusted with special or exclusive rights and should be prevented from abusing their privileged position. Domestically, the feasibility of behaviour control in the state-airport relationship has led to an expansion of the use of regulatory instruments. Regulations include slot co-ordination and the liberalisation of ground handling activities.

Chapter III showed that the state's air transport goal is broader than the objective of the airport. The airport's fixed infrastructure makes it dependent on local conditions, including its relationship with the state, but a growing divergence of interests resulting from new marketing opportunities, the growing volume of legislation and a changing view of its own position have increased the likelihood of agency problems. As an example, whereas the state mentions a tariff policy to promote the use of certain types of aircraft, Schiphol airport mentions tariff setting as an instrument to improve its competitive position (Amsterdam Airport Schiphol, 2000: 28). The Community has witnessed stronger capacity and environmental concerns and greater industry freedom. The single terminal concept, which has traditionally been a factor

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73 See Section 3.3.3 for some other reasons.
74 The 'Comité des Sages' was formed by a group of experts in the air transport sector. They investigated the status of the air transport sector and made suggestions for new policy objectives on behalf of the Commission.
75 A dissenting opinion in the report addresses airports as independent commercial enterprises. See also Monopolies and Mergers Commission (1996: 220) in a reference to the UK Department of Transport's opinion on airport policy. The UK DOT opined that airports should operate on a commercial basis, and government aimed to keep its intervention in airport development and management to the minimum necessary to secure its objectives for the environment, safety and security and economic regulation.
76 The regulation of airports has largely been left to the Member States, whose actions have been closely scrutinized by Community institutions (Slot, Skudder, 2000). The Community structure has not liberalised the airport sector.
77 Directive 96/67, supra, p. 99. The Directive has reduced the airport's ability to organise its facilities optimally, however, because it requires the airport to provide access to those areas that are sensitive for capacity and security reasons. Only in extreme cases may an exception be granted.
contributing to the success of Schiphol airport, has reached its physical limits. Although some instruments designed to elicit desired behaviour may still be used (e.g. the Operations plan and agreements on a noise preferential use of runways), the airport’s reward structure has not been adapted to the new environment. At the same time, the airport faces greater uncertainty, as a result of liberalisation and hub-and-spoke type transport operations, which has made it more reluctant to invest. The Community showed some sensitivity to the problem of uncertainty when it initiated the Trans-European Network initiative (see Section 4.4). However, at present only a small number of airport projects are included in the TEN scheme, and these are mainly studies and pilot projects. Italy’s Malpensa airport is the only air transport infrastructure project among the TEN’s 14 priority projects. A wish to reduce uncertainty has given the airport an incentive to formalise its relationships with other industry players, which is in line with the state’s proposed instrument of concluding covenants with the sector. These covenants also allow the industry to influence the content of future legislation. The PASO covenant and the ‘Uitvoeringsmemorandum’ of 1998 are examples. Airports, in general, have also worked on improving their co-operation with airlines, in part through an ACI-AEA project involving the establishment of model use agreements. The Optimisation strategy is another development stimulating co-operation. Since 1998 the main home carriers, Dutch Air Traffic Control and Schiphol airport have been meeting frequently to co-ordinate their actions and try to devise a new system of environmental norms and compliance that enables them to optimise their operations (known as the ‘Schiphol Optimisation Project’). At the same time, EC competition law places limits on such co-operation.

To reduce its dependence on the home carriers and increase its financial revenues, Schiphol further seeks to conclude co-operative agreements with other airports and to diversify its activities. It has, for instance, shifted its focus towards retail and real estate. The abolition of tax and duty free sales on Community flights in July 1999 and the wish to be privatised have given these initiatives an extra impulse. The strategy of diversification carries with it a new risk for the users of the airport. For example, investments may be delayed because of an expansion of retail facilities.

The discussion has shown that, in the Dutch situation, a diminishing ability to realise domestic objectives at the interstate level has led to tighter domestic regulation. Many requirements are

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78 The ‘Uitvoeringsmemorandum’ is mentioned in a letter dated 16 February 1998 from the Minister of Transport to parliament (Kamerstuk 25 466, no 9).
79 Some cases involve discounts based on a certain volume of flights, or discounts on domestic flights. For example, Commission Decision 198/99, OJ 1999 L 69, prohibited the discounts on domestic flights given by the Finnish airport operator Finnairlautakat. Also, Section 4.7.4.
aimed at Schiphol airport, making close co-operation between the state and the airport crucial. The Community structure has influenced the Member States’ ability to regulate. Although some traditional domestic instruments may still be used, there is a general lack of performance incentives, a growing divergence of interests, and hence a greater risk of moral hazard. One consequence is that there is frequent recourse to mechanisms that control the airport, resulting in many court cases between the state and airport. Similarly, airlines operating at Schiphol airport are increasingly involved in court cases concerning operations at the airport. Finally, uncertainty and greater marketing opportunities available to airports have led to a formalisation of state-airport and industry relations.

4.5.9 - International organisations
Section 3.3.4 discussed the role of the main international organisations in air transport, namely ICAO, IATA and ECAC. The discussion now turns to the effect of the Community structure on these organisations.

ICAO was established by the Chicago Convention, which is the basic document governing international air transport. The global nature of the organisation has meant that the creation of the Community structure has not had much effect. The Convention makes clear that only a state can be a member of the Chicago Convention and thus of ICAO. Each Member State is a party to ICAO, whereas the European Community only holds an observer status.

Member States, but again not the Community, are also party to ECAC. The role of ECAC seems to have decreased because of growing interdependencies and the ERTA doctrine, limiting the right of Member States to discuss a proposal in any other forum once the proposal is being discussed in a Community context. Nevertheless, the organisation plays a very important role. Its conferences keep other European states, who may be candidates for EC membership, informed about relevant Community policies. Any legislation can be introduced gradually and in a non-threatening way because of separate ratification requirements. ECAC co-operation can also be used strategically by Member States in the sense that they can form coalitions on subjects to be discussed in a Community context.

Chapter III observed that the liberalisation of the airline industry has reduced the role of IATA. Section 3.3.4 discussed this trend and shed further light on IATA’s current position. The Commission is an official IATA observer (Havel, 1997: 122).

Finally, liberalisation has stimulated co-operation among airports and has led to a bigger role for ACI EUROPE, the European division of the world-wide airport institution, ACI

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118 Some of these cases concern actual or potential restrictions on aircraft operations at Schiphol airport, imposed because the limits of the annual Operations Plan had been reached. Carriers are often unable to amend
(Bouwens, Dierikx, 1996: 353).

The absence of Community membership in these organisations and potential information problems have made it more important to exchange information and co-ordinate positions that Member States should take in negotiations. Commission Decision 80/50, which requires consultation and the provision of information, only partly meets the need for such activities.

4.6 - The object of the exchange and property rights

Chapter III defined the transaction as the barter exchange between states of air transport rights. These rights comprise the right 1) to enter a foreign air transport market, 2) to use the airspace to transport people to and from that market and 3) to capture the benefits from such use. Restrictions placed on the operation of these rights may vary depending on the policies of the states involved, but in every exchange reciprocity and a balance between rights and obligations are paramount. In the Community structure, separate Bilaterals no longer govern the provision of market access by and between Member States. Instead, market access is covered by a regulatory package, created by the Member States. Whereas Bilateralism is based on a categorisation of the rights to use the airspace (freedom rights), the Community structure ultimately eliminated that categorisation when it introduced full cabotage rights in 1997. There is one exception, namely the public service requirement. The fair and equal opportunity requirement has been reinterpreted as a requirement that starting positions should be equal.

The centre piece of the Community structure is the creation of market access, comprising each of the freedom rights, for Community carriers meeting certain predefined, objective criteria. The rights to use the airspace have been largely delegated to the carriers but they are not allowed to exchange any air transport rights. Nor can the airlines formally alter those rights because only Member States can change Community legislation. However, the way in which airlines operate their rights (e.g. route combinations or alliances) enables them to alter them in practice.

In Bilateral relations with third countries, the traditional categorisation of the rights to use the airspace is still intact and, apart from the limitation of the powers of Member States, the same applies to the categorisation of property rights to airspace. The discussion in Section 3.4 will not be repeated here.

In line with the description of the Bilateral structure, the following section looks at the Community's transaction process. The contact, the contract and the execution phases are considered in turn, while a separate section looks at compliance.

their flight schedules at short notice.

82 Recall from Section 2.2 that these are the rights to use an asset, to capture the benefits from that use, to alter
4.7 - The transaction process

4.7.1 - Contact phase

The contact phase has been defined as the phase during which potential transaction partners search for an opportunity to transact, and try to identify and evaluate other potential partners. The Community's transaction process does not include a search for transaction partners in the traditional sense because the ultimate parties are known. If a Member State wants to form a coalition it may need to search for those Member States that are willing to join. The identification of a transaction involves launching new ideas and creating support for proposed policy initiatives. Even though the Commission has the exclusive right to issue proposals, new policies or innovations also depend on new ideas and developments in Member States and on the ability of states to push these ideas through at Community level (Schout, 1999: 21). In addition, a Member State that holds the Presidency formulates its legislative priorities and tries to get these accepted. Prior to the formal initiation of a negotiation, there may be frequent contacts between representatives trying to get a feel for the position of Member States on a proposal. The initial phase is particularly important for small Member States since their influence is generally limited at the time when decisions are taken within the Council (ibid.: 10, 55). Sometimes, in order to start a discussion or to get a feel for the views of relevant stakeholders, the Commission issues a 'green paper', in which items for discussion are set out. This is followed by expert meetings and leads to a 'white paper'. The procedure was followed for the internal market objective as well as for the air transport packages.

4.7.2 - Contract phase

The contract phase formally starts with a proposal drafted by one of the directorates of the Commission, namely DG VII in the case of air transport and DG IV in the case of competition policy. The legal basis of a proposal determines the procedure and the majority needed to pass the proposal. The regulation of air transport matters is based on Article 80 para 2 EC and is subject to the co-decision procedure. Although the influence of Parliament and the Member States in this procedure is considerable, it is the Commission that holds the monopoly of legislative initiative. Preparatory work on legislation begins in working groups composed of Commission representatives, Member State officials, some of them experts, representatives from industry, permanent representatives and civil servants. The Dutch consider activities during this phase to be informal. 'Instructions for issuing regulations' have been formulated,

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the asset and to transfer all or some of these rights.

83 This section is partly based on Nicoll, Salmon (1994: 69-70).
which bind each Dutch representative working under ministerial responsibility but these are too general to exert a major influence. Specific instructions will not be formulated until the Council phase. The working group meets under the serving President. This group sets out to prepare a report which will show what can be agreed and what remains disputed at this level. Estimates show that almost 80% of any differences of opinion are resolved at this stage. The chairman, Commission representatives and individual delegates may also seek to devise compromises or act as brokers between different viewpoints. This includes negotiations outside the conference room and negotiations between delegations and the Commission. The General Secretariat of the Council provides assistance in the search for a compromise. This search occurs at all levels, but everything done below the level of the Council is informal. At this stage Dutch civil servants are generally regarded as independent experts and any co-ordination will be informal and bilateral. Nevertheless, the experts' opinions will be taken more seriously if they can present an overall picture of the view of their national government, which provides an incentive to co-ordinate (Schout, 1999: 187)

After agreement is reached at working group level, the Commission will receive a draft proposal. The proposal is accompanied by various explanatory memoranda, including a statement on subsidiarity. Each proposal must also be accompanied by a budgetary statement of its costs to the Community and a statement, in the name of deregulation, of its effects on small and medium-sized firms (Nicoll, Salmon, 1994: 63). These statements are not comparable to the explanatory memorandum that accompanies a legislative proposal in the Netherlands. This 'memorie van toelichting' is far more elaborate (Bracke, 1996: 80). Nonetheless, the amount of information provided by these documents is far greater than what is generally the case in transactions between states. If the Commission agrees to the text, it will be submitted to the Council. The Council phase consists of three levels: negotiations between officials in working groups, negotiations between ambassadors in COREPER and the political decision in the Council of Ministers. In contrast to the contact phase, officials in working parties formally represent their respective Member States and therefore have to present co-ordinated negotiating positions. The Council will start treatment of the proposal by consulting Parliament and ECOSOC as soon as the proposal has been translated into each of the official languages. Their reports are sent to the various working groups established by COREPER and consisting of civil servants who then deal with the proposal. The conclusions reached by officials are passed on to COREPER for formal approval. Proposals on which working groups have not

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84 The 'Aanwijzingen voor de regelgeving', Ministry of Justice, 1992, The Hague. The instructions are not confined to Community legislation, although they contain a separate chapter on it.

85 According to the Subsidiarity doctrine, which is based on the social teaching of the Vatican, set out in the encyclical Quadragesimo Anno of 1931, people should be closely involved in decisions that affect them, while
been able to reach agreement are also sent to this committee for further discussion. In principle, there is no time limit for consideration by COREPER but the Presidency may try to influence the period needed for discussion, for example, if the proposal forms part of its legislative priorities (Westlake, 1995: 378). During this phase and until the Council takes a common position, the Commission may modify the proposal. The way in which the Commission uses its prerogatives influences and is influenced by the attitude of other delegates. A change to accommodate one delegate, for example, will not always please other delegates. In addition to satisfying the Member States, the Commission has to be sensitive to the attitudes of Parliament and ECOSOC. A permanent representative in turn will have to act fast in order to respond to proposals the Commission might be inclined to accept. The President might further try to influence the negotiation outcome through his responsibility for the organisation and course of Community affairs (De Zwaan, 1993: 290-291, Westlake, 1995: 43).86

Given the reduced powers of the state, the various state interdependencies and the decision-making procedure of co-decision and qualified majority, a thorough preparation is crucial to realising a favourable negotiation outcome. Through careful co-ordination (i.e. ‘a set of actions aimed at the adoption by all the members of a group .. of mutually consistent decisions’, Schout, 1999: 6) states can process information, ensure a common national line, and become more adept at managing the environment (Westlake, 1995: 368). Their tasks include discussing negotiation strategy (identifying possible trade-offs), interpreting multiple goals, centralising authoritative guidance on Community issues as well as ‘line clearing’. Individual ministries may know exactly what they require to negotiate a piece of legislation, but they may wish to ensure that other ministries have been informed and have sorted out any issues important from their own perspective. Some states find the task of co-ordination easier than others. The German Basic Law, for instance, is relatively clear about the competencies of the different layers of government (Kreis, Land and Bund), which facilitates adding a European layer (Westlake, 1995, more generally: Schout, 1999). The Netherlands face more difficulties as may be illustrated by the following description of the current Dutch procedure (De Zwaan, 1993: 50,

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86 The Commission may, but is not obliged to, decide to modify its proposal on the basis of the discussions. When a modification is substantial, Parliament will have to be consulted for a second time, which constitutes a new ‘first reading’. The Council takes a ‘common position’ by qualified majority, or by unanimity if it amends the (possibly revised) Commission proposal. Parliament then examines and votes on the common position, needing a qualified majority or at least half its members to propose amendments (the ‘second reading’). The Council considers Parliament’s readings within three months, which is extendible to four months and the Commission has one month to express an opinion on the Council’s common position. If at the end of the period the Council has not decided, the proposal is dead.
As soon as a proposal is submitted to the Council, it is sent by the Dutch permanent representative to the Ministry of Foreign Affairs. The proposal is discussed in the interdepartmental Working Group for the assessment of new Commission Proposals (‘Werkgroep Beoordeling nieuwe Commissievoorstellen’ or ‘BNC’). Each ministry is represented and the group’s essential task is to establish whether the new proposal affects other national or Community legislation, to assess its financial implications, and to define responsibilities for negotiations in the Council (Schout, 1999: 192). It is not until this time that the formal co-ordination process starts with the formulation of specific instructions (ibid., De Zwaan, 1993: 289-300). These might relate to the subject under consideration, the content of the proposal and negotiation tactics. Member States should make sure that these instructions are clear and leave room for manoeuvre, especially when a proposal has already been discussed for some time. At the BNC meeting a filing card (‘fiche’) is prepared by the ministry with prime responsibility for the proposal, in this case the Ministry of Transport, which provides relevant information (Van der Flier, Van den Oosterkamp, 1994: 745). The ministry is also responsible for an implementation plan (ibid.: 733) which entails verifying if there is any need to consult the relevant national advisory bodies and representative organs.

The Dutch permanent representative attends weekly instruction meetings in The Hague. The meetings are chaired by the Ministry of Foreign Affairs and are used to exchange information and to prepare the position that the Netherlands will take in COREPER and the Council. Another meeting that is used for this purpose is the inter-ministerial Co-ordination Committee for European Integration and Association Problems (‘Coördinatie Commissie Europese integratie en associatievraagstukken’ or ‘CoCo’), chaired by the State secretary for Foreign Affairs. CoCo prepares Cabinet decisions concerning national positions and Council meetings. The positions which ministers present in Council meetings are officially agreed in Cabinet. The wish to rationalise the process of preparing national EU policy has led to the creation of a senior-level co-ordination committee, namely the High Level Co-ordination Committee (‘Coördinatie comité op hoog niveau’ or ‘COCOHAN’), which consists of representatives at the level just below the minister. It meets on matters of a more strategic nature and provides civil servants with guidelines on major policies. The conclusions of both committees are submitted to the Council for European and International Affairs (‘Raad voor Europese en Internationale Aangelegenheden’ or ‘REIA’), which is a sub-council of as well as to the Dutch Cabinet. The Securitel Decision has led to some changes to improve the exchange of information. It has led

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87 The problems were also illustrated by the Securitel decision (Case C-194/94, CIA Security International, Jur 1996, I-2201). In this case, it was found that in many instances the Netherlands had failed to comply with various notification requirements relating to technical conformity, which were laid down in EC legislation. The breach meant that any domestic regulations based on these rules were invalid.
to a greater role for REIA and the establishment of a new group, namely the Interdepartmental Subcommittee on European law ('Interdepartementale subcommissie Europees recht' or 'ICER'), divided into a working group on matters of preparation (ICER-V) and one on matters of execution (ICER-U). The procedures aim at a fast approval and at minimising the need for advice and consultation during the execution phase, which explains the frequent information exchange among the various groups. It also means that parliament is more closely involved in Community procedures than is generally the case in international affairs. Information to parliament is provided on a quarterly basis and parliament receives the annotated agenda of the Council. Further, ‘fiches’ are sent to parliament if the Ministry of Transport opines that the proposal has substantial consequences for domestic law, which is the case if a formal law is necessary to implement the proposal. Nevertheless, some problems remain. There is a lack of clarity on ultimate responsibilities as well as a split between those responsible for preparing and those responsible for executing (i.e. implementing) new legislation (De Zwaan, 1998: 364). In addition, specific instructions are only formulated at a very late stage, while the short time frame between formulating a national position and the Council meeting where the proposal is discussed limits the opportunity to exert any significant influence (Schout, 1999: 213). Furthermore, the low administrative level of representatives at domestic co-ordination meetings makes these meetings rather ineffective. Finally, the equality principle (i.e. equal rank of the ministries) implies that ministries may contribute to the content of policies in earlier phases (such as in expert meetings) and thus makes the ultimate responsibility of the Ministry of Foreign Affairs to co-ordinate Council decisions redundant. It also means that all items on the agenda are given equal weight and no priorities are set, making it impossible to concentrate lobbying and negotiating in Brussels on a few items of special importance (ibid.: 28, 30, 208, 212).

The conclusion of the transaction entails acceptance of the Commission proposal by the Member States acting through the Council. When COREPER reaches a common understanding, the proposal is sent to the Council as an ‘A point’, which means that delegations have found that there is agreement, or the necessary majority can be obtained. These A points are formally approved in Council meetings. Decisions on the other - ‘B’ - points are seldom taken, unless the item is a B point because a delegate or Commission representative wants to give an

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88 Parliament, however, is far less attentive to Community than domestic policy management. Schout (1999: 29, 193) partly ascribes this to a generally favourable attitude towards European integration.

89 The COREPER instruction meeting takes place approximately ten days before a Council meeting. Schout (ibid.: 209) notes that a position should be ready about three weeks before the meeting, i.e. when the informal agenda of the Council meeting is available, Member States are lobbying and coalitions start taking shape.

90 For items belonging to the common foreign and security policy, the responsibility for co-ordination lies mostly with the Ministry of Justice. Furthermore, the Ministry of Justice is responsible for implementation (De Zwaan, 1998: 364-365).
explanation of or make a statement on his position. The division into A and B points enables the President to structure the meeting and makes meetings more efficient. There is also a written procedure (De Zwaan, 1993: 200-205, Westlake, 1995: 85) for cases of extreme urgency as well as for simple administrative matters, such as the accreditation of third country representatives to the Community. Leaving aside this last category, a survey by De Zwaan (1993: 204) shows that the written procedure is followed in approximately 30 cases per annum.

When comparing the above description of the contract phase with the corresponding phase in Bilateralism, the elaborate procedures, extensive availability of information and large number of parties involved stand out. The existence of deadlines that serve to structure negotiations also differentiates the Community from the Bilateral structure. The broader scope of Community negotiations has led to new opportunities for trade-offs. At both the domestic and Community levels, a ministry has to search for coalitions, identify compromises and show greater sensitivity to the opinions of other states and institutions. In all cases, the negotiation process runs more smoothly if representatives in the Council have similar rank or political clout (Westlake, 1995: 58-59). Yet, representatives frequently differ in power because of such factors as seniority or in the position of the home country with respect to the issue. The relative size and economic strength of a Member State are also important, as are domestic events, such as elections. Furthermore, states are no longer equal in their decision-making power. Of course traditional formal equality need not imply actual equality. The economic and thus often the bargaining power of a large Member State is generally greater than that of a small state, such as the Netherlands, although a monopoly or superior information in a policy field could alter the balance. But, whereas equality is a central feature of Bilateralism, the EC Treaty has formalised differences in power through a system of weighted voting, whereby each Member State has been allocated a number of votes. In qualified majority decision-making, which is applicable to air transport, the Netherlands are entitled to five votes in the Council. Decisions are taken if 62 out of the 87 votes are in favour, which means a vote in favour by eight Member States. In addition to enhancing the need for a careful preparation, these factors have also increased the solidarity among Member States. Member States empathise with each other and try very hard to accommodate individual requests. Furthermore, although the 'Luxembourg compromise' no longer seems part of the Member States’ mentality in the

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91 There are some remaining cases that do rely on unanimous decision-making.
92 The resolution of the Edinburgh European Council of 1992, amended in 1995, following accession of Finland, Austria and Sweden, introduced a quorum requirement of eight states out of fifteen.
93 The ‘Luxembourg compromise’ was arrived at after a marathon session in February 1996 (Bulletin EEC no.3-1966, page 5 onwards) and contains the rule that a Member State - in a situation where it believes that fundamental interests are at stake - can block decision-making in the Council through a veto. This has led, among other things, to a preference for reaching consensus. Since the SEA entered into force there has only
Council, a situation is conceivable in which a Member State, whilst not formally invoking the compromise, makes clear that it feels a fundamental issue is at stake. Given the Council’s consensual instincts, it is equally conceivable that the other Member States will not force an issue under such circumstances, especially if they recognise the strength of the Member State’s case. The Member States are aware that they might be in the same position one day. Such conduct might be termed a ‘de facto veto’. Apart from these sensitivities, domestic factors are important. Domestic objectives, mandates and political views influence the conduct of the representatives. If a proposal is placed on the Council agenda as a B point and a discussion is necessary, these factors can lead to package deals or marathon sessions. From the point of view of a Member State or its constituents, it matters whether a representative silently acquiesces in or votes in favour of a measure. In the event of a vote, a Member State’s representative might even choose to be outvoted in order to demonstrate to a domestic audience his inability to secure a particular outcome (Kirchner, 1992: 107. Differently, Corbey, 1993: 103). As a result the Council’s decision-making process can be characterised by a strong accent on politics, co-ordination and consensus with the Council seldom taking a vote94.

4.7.3 - Execution phase

The Community rules apply after publication in the Official Journal. A Regulation applies directly and requires no separate domestic approval. A Member State may not even incorporate the provisions of a Regulation into domestic law, except when implementing measures are necessary. With respect to a Directive, implementation is needed and the text will stipulate the period in which this has to occur. A Member State that has failed to take the necessary measures at the expiration of this period is in breach of its treaty obligations. When the text of the Directive is clear and unambiguous, some provisions might be directly applicable even without implementation and it might be possible to invoke these provisions against the state95. Community legislation must be issued in every official language of the Community, and every version has the same status. Translation is carried out by the legal linguistic division within the translation group of the Community. This constitutes a high cost in the decision-making process, but can be traced to a sensitivity about equality among the Member States. In addition, it is crucial that all Member States should be fully aware of the contents of the Community rules.

As stated earlier, the Community’s layered structure requires the continuous co-operation

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94 The President can initiate a vote. Voting is also required on the initiative of the Council or the Commission, provided that a majority of the members so decide. If no vote is held, the President simply notes that the required majority (or unanimity) exists (Westlake, 1995: 148-151).
of Member States if the Community is to realise its goals. In the case of Directives, this need is exemplified by the responsibility of the Member States to provide for implementation. Domestic structures may complicate the process. The Dutch system, for example, adheres to the principle that rules can only be changed by rules of at least the same order. When a formal law is involved, as is often the case, the period needed to amend this law usually outruns the official implementation period. Although Schout (1999: 217) describes the Dutch implementation record as average, the Netherlands face the risk of breaching their obligations under the EC Treaty. This has motivated the use of dynamic referral, which is applied whenever possible. For example, it is incorporated in Article 16a of the Air Transport Act.

To speed up the implementation process, the Dutch AWB contains a chapter aimed at facilitating the implementation of Community legislation. Articles 1 para 7 and 1 para 8 AWB, respectively, provide that in the case of decisions serving to implement Community law, the general procedure of advice and consultation can be disregarded, unless exceptions apply. Information on implementing rules can be found in a domestic register of Directives. There is no equivalent register for Regulations, but some Regulations oblige Member States to inform the Commission of the legislation brought into force to comply with the relevant provisions. An example is Article 17 of Regulation 2407/92. Finally, the Securitel Affair prompted some changes in co-ordination procedures to improve the implementation of Community legislation.

On the basis of the above procedures, the Air Transport Act was amended in 1993 to comply with the various regulatory packages. The amendments covered the licensing procedures and implementation of the JARs mentioned in Section 4.4. The new licensing procedures entered into force in mid-1993 and, because of the direct applicability of the Regulation, had a retroactive effect. Under the new procedure, any Community carrier that has its principal place of business in the Netherlands can apply for an air operator’s certificate and a licence in the Netherlands. It can start to operate scheduled services after obtaining these and a route authority. Slot co-ordination and the ground handling Directive were introduced in the Netherlands in 1997 and 1999 respectively. New operations generate additional income for the airline. Section 4.5.7 explained that the elimination of designation has weakened the already limited direct link between the airline’s pay-off (e.g. designation or additional rights under a Bilateral) and performance. There is just one exception, namely the operation of a route based on a public service requirement, but this opportunity has not been exploited in the Netherlands. The investments that the carrier needs to make to support a new operation are generally the same

95 Cases C-6/0 en C-9/90, 1991 ECR, I-5357 (‘Francovich et al. vs. Italy).
96 Supra, p. 91.
97 An example is a Directive that Member States can implement with substantial policy freedom (Van der Flier, Van den Oosterkamp, 1994: 729).
as in the Bilateral structure. Start-up costs may be lower since the harmonisation of rules and more abundant information make it easier to gather and process information on local conditions. The Community structure has not had much effect on the pay-off of the airport, which is largely independent of the airport’s agreement with the state. The remarks made in Section 3.5.3 also apply to the Community structure. Recall, however, that the Community structure has meant new airport legislation and the liberalisation of ground handling activities, and that liberalisation more generally has expanded the airport’s marketing opportunities, thus raising the possibility of clashes between the airport on the one hand and the state and airline on the other. This has made it harder for the state to realise its objectives through the airport.

4.7.4 - Compliance and enforcement

Section 3.5.4 explained that compliance in the Bilateral structure is influenced by the sovereign nature of states and by the general absence of an external compliance mechanism. In addition, international law and various domestic legislations apply simultaneously, creating uncertainty about the applicable rules, which is reinforced by a lack of uniformity in domestic compliance procedures. The adverse effects of uncertainty and opportunism are likely to be even more serious at the Community than at the global level because of a greater risk of trade diversion within the Community. However, the long and close relationships between Member States have made the environment more conducive to self-enforcement at the state level. The Community structure also contains an enforcement system that allows the adjudication of disputes between states. Community institutions (e.g. the European Courts and, in competition cases, the Commission) may adjudicate and sanction Member States in case of a breach of treaty obligations. This includes cases where a state fails to implement a Directive within the allotted period.

The use of legal enforcement mechanisms has gained importance in practice. Regulations place a greater emphasis on legal wording, which facilitates legal enforcement. Moreover, the distribution of power has changed and states as well as industry players seem to be less afraid of any adverse effects on their relationships that might result from invoking legal remedies. The Commission is not susceptible to such concerns because of its independent position, which also contributes to a more frequent use of legal enforcement. Earlier sections noted the important effect of the Commission’s supervisory function in matters of competition law. In the light of increased competition and a loss of powers at the interstate level, Member States may try to resort to special arrangements with domestic firms to compensate for a loss in other fields. States may thereby distort competition. Familiar cases are those on the provision of state aid,
such as the Sabena100, Aer Lingus101 and Air France102 cases. These cases show that domestic measures providing state aid to the industry are being carefully scrutinised and that the approval of state aid may be tied to strict conditions. Legal enforcement is also used by the Commission in its action against several Member States, including the Netherlands, contesting the conclusion of Open Skies Bilaterals (supra, Section 4.5.6.1). Another example concerns the privatisation of the two Rome airports, Fiumicino and Leonardo da Vinci. Italy has limited the maximum shareholding of foreign state entities in its Rome airports to 2%. This is being contested by Schiphol airport on the grounds that it discriminates against foreign investors. The Commission is looking into this matter to determine if it inhibits the free movement of capital. The existence of EC Courts and the obligation of domestic courts to apply Community law have strengthened the incentive to abide by the rules.

In relations with third countries, the Bilateral dispute resolution mechanisms still apply.

The greater delegation of air transport rights to industry players in the Community structure implies a more important role for the legal remedies that can be used against these parties. One area where they are particularly important is the ex post monitoring of behaviour through competition law. To give some examples, industry players may contest competitors’ agreements and the Commission may investigate infringements, such as the abuse of dominant positions by refusing access to ground handling activities103 or the discounts on domestic flights mentioned in Section 4.5.8. Competition provisions 81 and 82 EC have been implemented via specific air transport Regulations, while Regulation 17/62 applies where air transport is not involved104. In addition, air transport on non-Community routes is subject to the interim regime of Articles 84 and 85 EC105. The existence of multiple rules, each with its own compliance procedures, is an element of concern, as it creates a complex situation. There are, for instance, differences in the notification requirements for proposed co-operation agreements. On the other hand, every Regulation allows any party to an agreement to ask the Commission to certify that the agreement does not infringe the competition rules. Further, there are no exceptions to the general corrective measures, which include the power of the

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99 The method of consultation is not ruled out. In addition to being the traditional way of maintaining interstate relations, Article 6, para 4 of Regulation 2409/92, mentions consultations among Member States to review a situation where a Member State has intervened in price setting by an airline.

100 Decision 91/555 OJ 1991, L 300.
104 For example, this Regulation applies to ground handling services. See Commission Decision 121/85, OJ 1985 L 46 (Olympic Airways) on the interplay between Regulations 17/62 and 141/62.
105 Supra, p. 93.
Commission to issue fines when it finds an infringement, suspend a transaction, take interim measures as well as adopt a Decision requiring termination of an illegal act.

In the domestic state-industry relationships, the distribution of power influences the preferred form of enforcement. In this regard, the Community resembles Bilateralism. However, the weaker interdependencies, the wider differences between state and industry objectives and the greater marketing opportunities in the industry have weakened state-industry relationships, altered the distribution of power and increased the likelihood that the parties will use legal enforcement to resolve conflicts.

4.8 - Characterisation of the Community structure

In terms of the categorisation of governance structures outlined in Chapter II, the Community structure of formal rules, and informal norms and values can be seen as a hybrid of a transaction-specific structure and the semi-specific structure of regulation. The complicated nature of state relationships is a feature of relational contracting and a transaction-specific structure. The same is true of the framework character of the EC Treaty and its secondary legislation. While the latter features make it less of a semi-specific regulatory structure, the air transport packages are examples of regulation based on the EC Treaty. The regulated parties are the Member States, as well as, indirectly, airlines and airports. The autonomy of the regulator derives from its right of initiative, decision-making rules involving qualified majority and broadly worded policy memoranda. Yet, there are some features that are more consistent with a non-specific structure. These include the importance of legal wording, detailed law-making procedures and independent courts.

Notwithstanding extensive powers to regulate in order to realise the objectives of the EC Treaty, the Community institutions face limitations on these powers. One feature of the Community is that its institutions only have those powers that have been explicitly conferred on them. Moreover, the Community’s framework structure implies that the treaty’s objectives cannot be attained without co-operation on the part of Member States. Any secondary legislation must be essential and effective, as well as proportional to the other goals of the Member States. This general rule was strengthened by the 1992 Subsidiarity doctrine, according to which the Community should only act if and when it is in the best position to do so. A procedure was created for the application of the principle, with pre-proposal consultation by the Commission as one of its requirements (Nicoll, Salmon, 1994: 299, Bekkers et al., 1995: 30). This principle has in practice come to mean that many actions are

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106 Supra, p. 121.
107 Bekkers (ibid.) describes two alternative tests created to evaluate whether a decision is taken at the right level. These are a value added test, which aims to judge whether action by the EC might have added value because of its ability to take into account international effects, and a comparative efficiency test, which looks at efficiency.
generally taken by national powers rather than the Community, but in air transport its influence is limited due to the global nature of the industry. Finally, formal rules governing the transaction process constrain Community institutions. The emphasis on procedures contrasts with the traditional process governing the creation of international rights and obligations (Bracke, 1996: 76-87). Chapter III explained that the traditional process is rather informal, characterised by rules of diplomacy, fundamental equality and sovereignty.

The relationships between the state and the airlines and airports are further examples of regulation.

4.9 - Further developments

This chapter has provided a description of the Community governance structure. On the one hand, the structure seems simpler than Bilateralism, because of the abolition of separate air transport agreements between Member States, the introduction of clearer rules, and the existence of enforcement mechanisms. On the other hand, differences between domestic and Community objectives, the existence of Bilaterals with third countries and various airline agreements with third country carriers have resulted in gaps and overlap and have made the structure more complex. It is the task of the next chapter to analyse and compare the effectiveness and transaction cost efficiency of the Bilateral and Community structures. Before turning to that analysis, some remarks on the future development of the Community structure are in order.

It has already been observed that air transport is a global activity. The relationships with third countries are of great economic and political relevance for the functioning of the internal market. This factor as well as the broad scope of the EC Treaty make it almost imperative that the development of the governance structure should focus on external relations. It is generally easier to reach agreement on external than on internal issues (Wallace et al., 1983: 75), but this has not been the case in air transport. Although at present there is no disagreement on the notion that air transport policy is part of the Community’s institutional structure, a consensus on the future development of this policy is still lacking, and the Community is limited in its powers vis-à-vis international organisations and third countries. From time to time, the Commission has issued proposals dealing with precisely this aspect but the Council has tended to reject these. The Commission has also used the option of going to court to pursue the policy further. The case initiated when GATS was concluded is one example, as are the infringement proceedings against Member States (see Sections 4.5.6.1). It is not yet clear when the Community structure will be completed and what form it will ultimately take. Given the

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the resources of the Member State. The efficiency test implies that the Community should only take action when competition between Member States is not producing an efficient outcome.
sensitive nature of air transport services and their link with foreign policy issues, some commentators (including the current author) assume that further progress will not result from any spill-over. Chapter VI will look into some elements surrounding further development of the Community structure.