# Open Skies Agreements

By: Marsha W. Johnston

Few corporate travel executives consider new Open Skies agreements between countries as a way to improve the services they buy. However Marc Hebert, executive vice president of Fremont, California-based Sierra Atlantic, thinks of little else. The new Open Skies agreement, signed between India and the United States in April, promises to make business travel infinitely easier for Sierra Atlantic, which has an offshore software development center in Hyderabad, India.

Sierra Atlantic buys approximately $1 million worth of travel per year, 80% of that between India and the U.S. As the new agreement removes current flight availability constraints and the airlines establish more routes between U.S. and Indian cities, the company's most frequented route of San Francisco-Hyderabad should ease considerably.

Getting to Hyderabad, which is not an Indian hub city, could not have been more complicated, says Hebert, often requiring passengers to stop over in Singapore, travel to Chennai in India, and take a domestic flight to Hyderabad. "For a while, the Singapore-to-Hyderabad flight ran only a couple of times a week, so if you didn't fly on the right day, you had to fly into Chennai and often stay overnight, when you'd already been traveling nearly 30 hours. By the time you got there, you'd been traveling nearly 2 days!" he said.

Open Skies agreements, he says, "open the gates to get more supply into some of these lesser-served cities". Already, since the agreement was signed, Delta Air Lines announced new daily service between New York and Chennai while Northwest Airlines plans new flights between Minneapolis and Bangalore. With a sufficient increase in frequency, fares could come down by 20 percent, Hebert adds.

Across the board, Open Skies agreements are seen as the best means to bring international aviation up to speed with the already-globalized industries it serves. Stephen D. Van Beek, executive vice president for policy at Airports Council International (ACI)-North America, in Washington says. "Aviation lives under a 50-year-old legal framework and Open Skies is the attempt to bring it into the 21st century." Barry Humphreys, director of external affairs and route development for Virgin Atlantic Airways in London adds, "We have one of the most global of businesses, but not a single global business, due to archaic ownership and control rules, whose philosophy goes back to the mercantilism of the 19th century, not merely the 20th!"

Changing those ownership and control rules remains the biggest single obstacle to removing the proverbial elephant under the rug that is the lack of an Open Skies agreement between the 25-member European Union and the U.S.

Currently, the airlines of each of the U.S.'s 15 EU bilateral Open Skies partners are allowed to fly to and from any point in their country to any point in the U.S., but all those flights must funnel in and out of their individual home countries due to the famous "nationality clause". The clause stipulates that to operate services under an Open Skies agreement, an airline must be owned and controlled by citizens of one of the two contracting parties. The result of the existing series of bilateral agreements with EU member states is that a British airline cannot fly from Milan to Washington, for example, says Frederic Camus, VP of industry relations EMEA for Carlson Wagonlit Travel. "But if we had an agreement between the two blocks tomorrow, it would be possible," he said.

In fact, in late 2002, the European Court of Justice ruled that the nationality clause was inconsistent with a unified Europe set up by the Treaty of Rome and that member states should get it out of their treaties. Since then, the U.S. and the EU have been trying to get a comprehensive agreement.

In negotiations last year, the U.S. agreed to accept an "EU carrier" principle, which would have opened up every EU-U.S. city pair market, heretofore limited to one or two EU national carriers by the operation of the nationality clause, to all EU carriers. The U.S. would not, however, agree to allow EU airlines to fly point-to-point in the U.S., as U.S. airlines can do in Europe, or to allow airlines with a majority foreign-owned voting share to establish themselves on U.S. territory. The EU rejected the agreement.

Says Virgin Atlantic's Humphreys, "The U.S. is being quite difficult on certain points…for ownership and control, under U.S. rules you can only own 25% of voting shares, but there are an additional large number of restrictions on control of the airline, such as that the chairman and board of directors have to be U.S. citizens." He acknowledges that the Bush Administration asked Congress to change the rule from 25% to 49%, but added, "it doesn't really change anything, as you still don't have control." Camus, of Carlson Wagonlit Travel, noted: "It's an old demand for Europeans, to change the ownership rules, to get access to the capital of US airlines. It would be an opportunity for US airlines, who are going bust or are at minimum unwell, to get a bailout. For US Airways, America West, United Airlines, it could be one solution, if Lufthansa, or Air France or British Airways, could put in some money and help them survive."

Indeed, certain high-powered voices in the U.S. have begun to call for a change. In a late April speech to the Chicago Council on Foreign Relations, United Airlines CEO Glenn Tilton called on the U.S. government to "repeal the 1938 federal law that bars foreign ownership of more than one-quarter of a U.S. air carrier. This restriction has emerged as one of the most significant barriers to this industry becoming more global." Undersecretary of Transportation Jeffrey Shane made similar remarks in a speech at the Aviation Symposium 2005 in Phoenix, Arizona. "It does not seem radical today to suggest that it is time to reconsider the justification for a law that restricts U.S. airlines' access to the global capital marketplace."

Nonetheless, as ACI's Van Beek notes, getting rid of the ownership and control rule in commercial aviation is still a radical view for the majority, as it will entail inevitable airline consolidation and, quite probably, job losses. "[Open Skies agreements] present risks for current employees, but presents opportunities in growth markets. When countries such as China and India open, for example, those high-revenue flights would be good for airlines like United," he says. Adds Virgin's Humphreys, "When the change does happen, there will be massive upheaval and consolidation and we will get global airlines."

Consequently, as Shane acknowledged in an interview with the ACTE Global Business Journal, the DOT has not made any decision to push Congress again to change the ownership rule. "It's been around a long time. It's tough culturally and politically, but not economically. But we've been trying to persuade our European friends that there are an awful lot of good things we can do, even if we can't immediately change the ownership rule."

In a positive sign, Shane noted, when EU Transport Commissioner Jacques Barrot met with U.S. Transportation Minister Norman Mineta a few weeks ago, Barrot seemed to understand entirely that having another failure like last year's "would not be in the best interests of either Europe or the US." So, he said, the two parties are conducting informal conversations to see if the ingredients are there to get something that might fly this time.

An Open Skies agreement between the U.S and the EU, which account for between 60%-70% of global airline traffic, could open the door to international service from low-cost airlines, as well as negatively impact today's airline alliances.

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Says John Hume, director of policy for ACI-Europe: "People are saying that with an [EU-US] Open Skies agreement, we will get lots of transatlantic low-cost carriers, but the truth is that we'll never know unless we do it. And, if you look at what they have done in Europe, they created a whole new market!" Clifford Winston, a senior fellow at Brookings Institution and co-author of a recent study on competition in the U.S. airline industry, adds: "Not only would there be more competition and flexibility with the existing dinosaurs, but it would also bring in low-cost carriers. When you see what they did for the domestic industry, just imagine what they would do internationally!" Indeed, wonders Sierra Atlantic's Hebert, "If someone like JetBlue were to start doing European flights, what would it look like?"

Existing airline alliances, say both Hume and Winston, will not survive greater international deregulation, as they simply mask inefficiencies and represent the best means to get around airlines' inability to merge. Nanci Cheberenchick, regional director of America sales and market development for the Star Alliance in Chicago, objects, saying that alliances don't mask inefficiencies any more than do mergers; yet provide 75-80% of a merger benefit without the headaches. Furthermore, she adds, "even if you eliminate everything, that you can fly anywhere, anytime, you still have the issues of resource availability. No one carrier has the resources to expand infinitely."

With an ailing U.S. industry and new planes that can fly up to 17,000 nautical miles without stopping, Open Skies agreements are inevitably the way of the future and corporate travel executives have every reason to be glad. Just ask Marc Hebert. ■