

## WORLDWIDE AIR TRANSPORT CONFERENCE: CHALLENGES AND OPPORTUNITIES OF LIBERALIZATION

Montreal, 24 to 29 March 2003

### Agenda Item 1: Preview

#### 1.1: Background to and experience of liberalization

### BACKGROUND OF LIBERALIZATION AND EXPERIENCES IN THE LATIN AMERICAN REGION

(Presented by Argentina, Aruba, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cuba, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay and Venezuela)<sup>2</sup>

#### SUMMARY

The main objective of this paper is to present to the international aeronautical community an overview of the situation of air transport liberalization in Latin America.

Action by the Conference is in paragraph 3.1.

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## 1. INTRODUCTION

1.1 Economic globalization, commercial integration, sub-regional development of integration processes and the possibility of regional free trade agreements have led to the holding of regional fora for coordinating and harmonizing positions in order to move in an orderly and efficient manner towards a more flexible air transport.

1.2 In terms of trade and integration it can be observed that, with respect to our region, various initiatives are being developed, and that the economic and structural differences of our countries must be given great consideration during the conformation of these integration processes.

1.3 At the same time, in terms of air transport, the traffic integration and flexibilization initiatives continue to move forward, fostered by aeronautical and trade authorities, as is the case of the Fortaleza Agreement, the Andean Community of Nations (CAN) decisions, and the work of the Association of Caribbean States (ACS). All these initiatives are aimed at harmonizing policies in order to make the granting of traffic rights and market access more flexible and air transport more fluid.

1.4 The Latin American Civil Aviation Commission (LACAC) fosters this type of processes by promoting harmonization and coordination, permitting the amalgamation of policies and the development of air transport, in such a way that it will not only respond to the interests of developed countries but mainly to those of less developed nations.

1.5 It should be noted that, within the framework of modernization of the political and economic management of governments, new actors have emerged in the aeronautical market during the last decade, following the implementation of more open economic policies by the States in the region. Consequently, not only aeronautical authorities and airlines, but also private airport operators and regulatory bodies have had to be considered as referential elements of this activity in the new scenario.

1.6 The work carried out by LACAC in this area has been intense. The steps taken to strengthen regional air transport and coordination among the different actors in this new scenario have been fruitful. LACAC, as a body specialized in civil aviation, has focussed on the strengthening of the link between economic policies and technical aspects, fostering political decisions that serve the interests of consumers and that seek the safety of this means of transportation.

1.7 As a result of its work, it has issued several resolutions, including one that contains air transportation policy criteria and guidelines, which is regularly assessed to match changes in the market, and which seeks a more flexible air transport at all levels and throughout the region. Among its whereases, it states that “such policy should seek to liberalize the provision of commercial air transport services in the region,...applying the principle of healthy competition, supported on a safe, orderly and efficient system”.

## 2. LIBERALIZATION AND EXPERIENCES IN THE LATIN AMERICAN REGION

2.1 Flexibilization, as an irreversible trend in Latin American air transport, probably began with the elimination of State-owned airlines and the centralized economies on which many of them were supported. The aeronautical authority became more flexible. This brought about the need to apply more liberal airline nationality criteria.

2.2 Authorities started to negotiate traffic rights in a different framework; they no longer did it for the sake of State-owned companies, but rather for private companies, which, in some cases, included foreign capital. It was at that time that new elements were introduced for the determination of airline nationality, such as headquarters, place of business, actual and effective headquarters, base of operations of aircraft in the national territory, and other strong links with the country, criteria which have largely replaced the traditional requirement of a majority, both in terms of capital and airline management, to determine nationality.

2.3 Driven by a global trend, several States started to deregulate aspects which previously had rigid structures, such as supply and the fare system, which started to depend on market forces. All this occurred slowly at first and was then supported by a more decisive political position.

2.4 The rate at which this process has developed in the countries of the region has varied. For some aeronautical authorities, the liberalization of air transport markets still entails the risk of ruinous competition, and prefers the traditional system of regulating supply and setting prices. Others are convinced that regulation and restrictions hinder growth, while free competition encourages carriers to improve services and create new markets. There are also other authorities that have chosen to introduce flexibility into their policies in a progressive way, gradually adjusting to the new scenarios.

2.5 The process of flexibilization has not been easy in the region. It has required an environment that offered better conditions and some tools. One of these tools is the adoption of more liberal safeguard clauses in bilateral agreements, aimed at avoiding unlawful competition practices. These clauses should be aimed at providing safeguards against unlawful and anti-competitive behaviours by carriers, since those behaviours, such as oversupply or fares below cost, distort the free market. In this respect, LACAC issued Recommendation A13-3, suggesting the introduction of a clause model in liberal commercial aeronautical agreements, in order to avoid unlawful competition practices. This recommendation is a very useful tool for flexibilization, which identifies not only unlawful practices but also their characteristics.

2.6 After 11 September 2001, several governments from developed countries have adopted measures that have somehow distorted the market, providing direct financial assistance to their airlines, in the way of subsidies. Likewise, several governments have provided support to their carriers, covering the risks that were left unprotected as a result of the decision adopted by the insurance sector following that date. Latin American States could not apply such measures due to economic limitations, which obviously affected the airlines of the region.

2.7 Another difficulty that the aeronautical authorities must face is that related with unilateral measures affecting safe competence, users or carriers, or that which pretends to give an extraterritorial character to national legislation, and rejection of such measures when imposed by other States.

2.8 In an increasingly flexible environment, and on the way towards full liberalization based on competition and free markets, the granting of State support, in the form of financial or other advantages, by governments to their own carriers, which surely is not extensive to the competition in the same international markets, could distort the trade of international air services.

2.9 Another issue that authorities have had to face has been the need to review the “substantial ownership and effective control” criterion for granting, denying, or revoking an operation permit to a foreign airline designated by another country. This need emerges because air carriers need to expand their financing sources and because investment in foreign airlines has gained importance both inside and outside the region, and could become even more important.

2.10 To the legitimate efforts to prevent a State that is not party to an air transport agreement from obtaining non-reciprocal benefits, and to the traditional efforts to give transparency to the relationship between the airline and the designating State, authorities have had to add the efforts to adopt criteria and define the “headquarters”, “sound links” and “commercial control” concepts. In this respect, two very important rights of the authorities must be considered: on the one hand, the right to designate the airlines that will benefit from the traffic rights granted under bilateral agreements and that will have market access; and, on the other, the right to deny such designation, as a legitimate measure of protection.

2.11 In recent years, the movement towards integration of the countries of the Latin American sub-regions, through the subscription of more liberal agreements, coordination meetings and studies for the establishment of common policies, continued to consolidate, stressing that air transport is a basic tool for achieving integration objectives. Within the framework of the Association of Caribbean States (ACS), a Resolution on “Common Commercial Air Transport Policy Criteria in the ACS” has been adopted; likewise, efforts continue for the development of a binding document that will permit the “unification of the Caribbean by air and sea”; and work is being done on the Draft Multilateral Air Transport Agreement.

2.12 With regard to the Agreement on Sub-regional Air Services within the framework of the Fortaleza Agreement, efforts to standardize the granting of operation permits for all sub-regional flights continues. As to the progress is made with respect to sub-regional services, consideration is being given to eliminating the overlap of two regulatory frameworks: bilateral agreements and the sub-regional system; likewise, it has been deemed advisable to liberalize traffic rights.

2.13 In turn, the CAN, based on the “open skies” principle, is carrying out air transport operations within the sub-region, to which the airlines of its member States are given free access. However, beyond the sub-region, no flexibility has been achieved.

2.14 Air transport in Latin American is slowly becoming more flexible through sub-regional and bilateral agreements. LACAC, as a specialized body, has been closely monitoring these developments, providing all possible support, and is focussed on harmonizing the positions of the various sub-regional groups with a view to defining an overall policy for all the sub-regions.

### **3. ACTION BY THE CONFERENCE**

3.1 The Conference is invited to take note of the information provided and to examine the topics mentioned, so as to permit a gradual liberalization while safeguarding less developed countries.

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2.3 Driven by a global trend, several States started to deregulate aspects which previously had rigid structures, such as supply and the fare system, which started to depend on market forces. All this occurred slowly at first and was then supported by a more decisive political position.

2.4 The rate at which this process has developed in the countries of the region has varied. For some aeronautical authorities, the liberalization of air transport markets still entails the risk of ruinous competition, and prefers the traditional system of regulating supply and setting prices. Others are convinced that regulation and restrictions hinder growth, while free competition encourages carriers to improve services and create new markets. There are also other authorities that have chosen to introduce flexibility into their policies in a progressive way, gradually adjusting to the new scenarios.

2.5 The process of flexibilization has not been easy in the region. It has required an environment that offered better conditions and some tools. One of these tools is the adoption of more liberal safeguard clauses in bilateral agreements, aimed at avoiding unlawful competition practices. These clauses should be aimed at providing safeguards against unlawful and anti-competitive behaviours by carriers, since those behaviours, such as oversupply or fares below cost, distort the free market. In this respect, LACAC issued Recommendation A13-3, suggesting the introduction of a clause model in liberal commercial aeronautical agreements, in order to avoid unlawful competition practices. This recommendation is a very useful tool for flexibilization, which identifies not only unlawful practices but also their characteristics.

2.6 After 11 September 2001, several governments from developed countries have adopted measures that have somehow distorted the market, providing direct financial assistance to their airlines, in the way of subsidies. Likewise, several governments have provided support to their carriers, covering the risks that were left unprotected as a result of the decision adopted by the insurance sector following that date. Latin American States could not apply such measures due to economic limitations, which obviously affected the airlines of the region.

2.7 Another difficulty that the aeronautical authorities must face is that related with unilateral measures affecting safe competence, users or carriers, or that which pretends to give an extraterritorial character to national legislation, and rejection of such measures when imposed by other States.

2.8 In an increasingly flexible environment, and on the way towards full liberalization based on competition and free markets, the granting of State support, in the form of financial or other advantages, by governments to their own carriers, which surely is not extensive to the competition in the same international markets, could distort the trade of international air services.

2.9 Another issue that authorities have had to face has been the need to review the “substantial ownership and effective control” criterion for granting, denying, or revoking an operation permit to a foreign airline designated by another country. This need emerges because air carriers need to expand their financing sources and because investment in foreign airlines has gained importance both inside and outside the region, and could become even more important.

2.10 To the legitimate efforts to prevent a State that is not party to an air transport agreement from obtaining non-reciprocal benefits, and to the traditional efforts to give transparency to the relationship between the airline and the designating State, authorities have had to add the efforts to adopt criteria and define the “headquarters”, “sound links” and “commercial control” concepts. In this respect, two very important rights of the authorities must be considered: on the one hand, the right to designate the airlines that will benefit from the traffic rights granted under bilateral agreements and that will have market access; and, on the other, the right to deny such designation, as a legitimate measure of protection.

2.11 In recent years, the movement towards integration of the countries of the Latin American sub-regions, through the subscription of more liberal agreements, coordination meetings and studies for the establishment of common policies, continued to consolidate, stressing that air transport is a basic tool for achieving integration objectives. Within the framework of the Association of Caribbean States (ACS), a Resolution on “Common Commercial Air Transport Policy Criteria in the ACS” has been adopted; likewise, efforts continue for the development of a binding document that will permit the “unification of the Caribbean by air and sea”; and work is being done on the Draft Multilateral Air Transport Agreement.

2.12 With regard to the Agreement on Sub-regional Air Services within the framework of the Fortaleza Agreement, efforts to standardize the granting of operation permits for all sub-regional flights continues. As to the progress is made with respect to sub-regional services, consideration is being given to eliminating the overlap of two regulatory frameworks: bilateral agreements and the sub-regional system; likewise, it has been deemed advisable to liberalize traffic rights.

2.13 In turn, the CAN, based on the “open skies” principle, is carrying out air transport operations within the sub-region, to which the airlines of its member States are given free access. However, beyond the sub-region, no flexibility has been achieved.

2.14 Air transport in Latin American is slowly becoming more flexible through sub-regional and bilateral agreements. LACAC, as a specialized body, has been closely monitoring these developments, providing all possible support, and is focussed on harmonizing the positions of the various sub-regional groups with a view to defining an overall policy for all the sub-regions.

### **3. ACTION BY THE CONFERENCE**

3.1 The Conference is invited to take note of the information provided and to examine the topics mentioned, so as to permit a gradual liberalization while safeguarding less developed countries.

— END —



## WORLDWIDE AIR TRANSPORT CONFERENCE: CHALLENGES AND OPPORTUNITIES OF LIBERALIZATION

Montreal, 24 to 29 March 2003

### Agenda Item 1: Preview

#### 1.1: Background to and experience of liberalization

### BACKGROUND OF LIBERALIZATION AND EXPERIENCES IN THE LATIN AMERICAN REGION

(Presented by Argentina, Aruba, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cuba, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay and Venezuela)<sup>2</sup>

#### SUMMARY

The main objective of this paper is to present to the international aeronautical community an overview of the situation of air transport liberalization in Latin America.

Action by the Conference is in paragraph 3.1.

#### REFERENCES

- LACAC Res. A15-5 - *Air transport policy criteria and guidelines*
- LACAC Rec. A13-3 - *Draft model clause to avoid unlawful competition practices*
- Presentations and conclusions of the Seminar on the Liberalization of Air Transport (Santo Domingo, Dominican Republic, 1-3 October 2002)
- ATRP/10 - Report of the tenth meeting of the Air Transport Regulation Panel (Montreal, 13 - 17 May 2002)
- Report of the II Meeting of Latin American Ministers of Transport and Aeronautical Authorities (Santiago, Chile, 2 April 2002)

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<sup>1</sup> Spanish version provided by Members of the Latin American Civil Aviation Commission (LACAC).

<sup>2</sup> Members of the Latin American Civil Aviation Commission (LACAC)

## 1. INTRODUCTION

1.1 Economic globalization, commercial integration, sub-regional development of integration processes and the possibility of regional free trade agreements have led to the holding of regional fora for coordinating and harmonizing positions in order to move in an orderly and efficient manner towards a more flexible air transport.

1.2 In terms of trade and integration it can be observed that, with respect to our region, various initiatives are being developed, and that the economic and structural differences of our countries must be given great consideration during the conformation of these integration processes.

1.3 At the same time, in terms of air transport, the traffic integration and flexibilization initiatives continue to move forward, fostered by aeronautical and trade authorities, as is the case of the Fortaleza Agreement, the Andean Community of Nations (CAN) decisions, and the work of the Association of Caribbean States (ACS). All these initiatives are aimed at harmonizing policies in order to make the granting of traffic rights and market access more flexible and air transport more fluid.

1.4 The Latin American Civil Aviation Commission (LACAC) fosters this type of processes by promoting harmonization and coordination, permitting the amalgamation of policies and the development of air transport, in such a way that it will not only respond to the interests of developed countries but mainly to those of less developed nations.

1.5 It should be noted that, within the framework of modernization of the political and economic management of governments, new actors have emerged in the aeronautical market during the last decade, following the implementation of more open economic policies by the States in the region. Consequently, not only aeronautical authorities and airlines, but also private airport operators and regulatory bodies have had to be considered as referential elements of this activity in the new scenario.

1.6 The work carried out by LACAC in this area has been intense. The steps taken to strengthen regional air transport and coordination among the different actors in this new scenario have been fruitful. LACAC, as a body specialized in civil aviation, has focussed on the strengthening of the link between economic policies and technical aspects, fostering political decisions that serve the interests of consumers and that seek the safety of this means of transportation.

1.7 As a result of its work, it has issued several resolutions, including one that contains air transportation policy criteria and guidelines, which is regularly assessed to match changes in the market, and which seeks a more flexible air transport at all levels and throughout the region. Among its whereases, it states that “such policy should seek to liberalize the provision of commercial air transport services in the region,...applying the principle of healthy competition, supported on a safe, orderly and efficient system”.

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