

## INDONESIAN CIVIL AVIATION POLICY TOWARD AIR SERVICES LIBERALIZATION

(Presented by Indonesia)

### BACKGROUND AND ISSUES

- Market access is a relatively new term in air transport, having originated in the trade field.
- Market access, in relation to traffic rights, is governed under the Chicago Convention by Articles 1 (sovereignty), 5 (non-scheduled flights), 6 (scheduled services) and 7 (cabotage).
- The principal market access provision is Article 6 which requires "special permission or other authorization" to operate scheduled international services, but does not specify the process for exchange of rights; such rights, including route, operational and traffic rights, determine the extent of market access granted.
- Any market access arrangement should protect the right of any State to a fair opportunity to participate in air transport (Article 44 *(f)*): "a fair opportunity to operate international airlines").
- Market access rights, i.e. traffic rights, are in practice, negotiated and exchanged between States bilaterally in air services agreements and multilaterally among groups of States (e.g. European Union and Andean Pact agreements, APEC plurilateral); rights are bilaterally exchanged based on such principles as reciprocity, non-discrimination and balanced exchange of benefits or opportunities.
- Traffic rights are negotiated and expressed in terms of five "freedoms of the air", as defined by the International Air Transport Agreement, and four additional "so-called freedoms" not formally defined by any international treaty.
- Market access raises some difficult and controversial issues, including questions of balance of opportunities, for negotiators. For example:
  - Fifth freedom: a complex issue to negotiate between two States, e.g. how to determine traffic "ownership" or the viability of a route; how much traffic is supplementary (5th) as against primary (3rd and 4th).
  - Sixth freedom: an opportunity for States that are well situated geographically and are able to exploit and maximize their traffic and market access by combining negotiated traffic rights.
  - Codesharing: usually requires underlying traffic rights for regulatory approval and depending on the market served, codesharing can enhance competition, providing for additional or better service, or threaten competition, reducing the number of airlines and limiting consumer choices.
  - Cabotage: a right that is hardly ever exchanged (except in the EU Single Market) and is usually seen as a threat to the national airlines (e.g. controversy over the Australian government opening up its domestic market to foreign airlines); refers, legally, only to traffic rights exchanged within a sovereign State and not a group of States.
- Market developments affecting market access, for example:

- Alliances allow an airline to increase access to traffic and to new markets that are restricted by capacity provisions in the bilaterals (see WP/9).
- Franchising allows an airline to diversify its market and generate revenue on minor routes, without the risk of capital investment (e.g. British Airways operates 11 franchise agreements with smaller airlines in Europe, Middle East and Africa).

## **PROGRESSIVE LIBERALIZATION**

- Liberalization was discussed at length at the Chicago Conference on the basis of a draft treaty envisaging multilateralism. However, the bilateral system of negotiating air service agreements emerged as a result because countries could not agree on a free or liberalized market access based on market forces, and settled for a more restrictive approach towards controlling capacity and tariffs and exchanging route rights.
- In the 1970s, air transport liberalization policies in the United States, (the Airline Deregulation Act) was followed by the spread of such policies to other parts of the world particularly in the 1990s.
- The trend towards liberalization continues to grow as approximately 80 (50 of which involve the US) "open skies" or full market access agreements (involving some 60 countries), some of them phased in, having been concluded.
- ICAO's Worldwide Air Transport Conference (1994) examined a new regulatory arrangement on market access prepared by a Group of Experts on Future Regulatory Arrangements (GEFRA), to enable States to move towards a more open, competitive air transport sector; the arrangement was for an integrated, interrelated package to be entirely used at the discretion of individual States in a bilateral or multilateral context; the package included: the introduction, in a phased or incremental manner, of full market access (unrestricted route, operation and traffic rights with optional Seventh Freedom and cabotage), in conjunction with a "safety net" (time-limited capacity freeze), and a safeguard mechanism including a code of conduct (to sustain healthy competition) and a new dispute settlement mechanism.
- The Conference concluded that a global commitment to full market access did not exist and recommended a "gradual, progressive, orderly and safeguarded change" which would ensure "participation, adaptation and regulatory flexibility". It also expressed concerns about the "safety net" concept and requested further refinement of the safeguard mechanism. It also recommended that States liberalize their market access progressively at their own pace, on a case-by-case basis, bilaterally, or at the subregional or regional level.
- Market access is also an issue in connection with the GATS (see WP/4). However, the most favoured nation (MFN) concept, which achieves progressive liberalization through successive rounds of negotiations, is not suited to the air transport bilateral environment, which is governed by reciprocity and balancing benefits or opportunities, because of the "free rider" consequence of any market access commitment under the GATS.
- States are working within the current system to expand regional and subregional liberalization (see WP/7); liberalization in most regional arrangements is taking effect in phases.
- Progressive liberalization is occurring; States are loosening their controls; airlines are responding to competition and market forces; a majority of the bilaterals negotiated in the past 5 years are either

"open skies" or they contain one or more liberalization measures (e.g. multiple designation, open routes, unrestricted traffic rights, capacity and traffic flexibility). No less than 85% of States are already involved with one or more partners in some form of liberalization, whether bilateral or regional.

## **SAFEGUARDS**

- Another relatively new concept in air transport and again from the trade field where it concerns protective actions in response to dumping situations or balance of payments problems; in air transport it has come to involve principles and institutionalized responses to unfair competition.
- A liberalizing environment in air transport where most States do not have comprehensive competition laws to address unfair competitive behaviour, needs some form of safeguard mechanism.
- Idea for a safeguard mechanism in a liberalizing environment was presented to the 1994 Conference as a means to ensure fair competition, through a code of conduct on unfair competitive behaviour and a dispute settlement mechanism; Conference requested further refinement of the idea.
- Air Transport Regulation Panel (ATRP) subsequently proposed (Recommendation ATRP/9-1) that in a liberalizing relationship, States mutually agree on the kinds of unfair competitive practices and provide some signals of such behaviour, for example, the addition of excessive capacity or abuse of a dominant position, and that a dispute settlement mechanism be established for use between traditional consultation and arbitration processes.
- The proposed dispute settlement arrangement, for rapid response to an unfair competitive situation, would entail either use of a high level meeting, up to Ministerial level, or agreement between the parties to use a mediator or panel drawn from a list of air transport experts maintained by ICAO (see Recommendation ATRP/9-2 and State Letter SP 38/4.1-99/53).
- Safeguards in a completely open market access relationship would normally consist of use of competition laws, although the ICAO guidance on safeguards could also be used; in a situation where partners do not wish to liberalize then the traditional concepts of fair and equal opportunity to compete could be used to ensure fair competition.
- Future issues and problems include: acceptance of the need for a safeguard mechanism; how to build such a mechanism into the bilateral or regional relationship; and resources and expertise needed to monitor competitive practices in the market place and to implement a safeguard mechanism.

## **PARTICIPATION**

- Continued participation is a particular characteristic of international air transport vis-à-vis other service sectors and is a fundamental objective of all States for their trade, commerce and development needs.
- Participation can be described as "a reliable and sustained involvement by a State in the international air transport system". It does not necessarily mean the existence of a national carrier.
- States can participate in air transport through providing direct international air services by a) their designated national carrier, with their own equipment and crew (traditional way sometimes described

as the "flag carrier"); or b) by their designated air carrier through commercial agreements (e.g. codesharing, franchising) with another air carrier.

- Participation can also be indirect through providing air services by a) a designated carrier of a State by using the aircraft of another (foreign) carrier (e.g. codesharing, block space); b) contractual arrangements between a State and a foreign air carrier; c) indirect providers (e.g. tour organizers); and d) equity holdings in designated carriers of another State.
- Following the recognition of participation as a fundamental objective of States, the 1994 Conference considered progressive liberalization of market access and the "safety net" concept in terms of effective and sustained participation; the latter was emphasized in the Conference Recommendation and was a principal outcome of the meeting.
- Air Transport Regulation Panel (ATRP) in 1997 developed lists of participation measures as a substitute for the "safety net"; panel saw such measures as an appropriate preventative tool to be used in progressively liberalized agreements; in bilateral agreements potential measures could include, for example, moving from a dual approval tariff provision to country of origin to a dual disapproval regime; capacity could be moved progressively in stages such as from 50/50 to 70/30; and designation from single to multiple (see Recommendation ATRP/9-3).
- Participation for small developing countries is a problem, particularly those without an international airline; in these situations Panel foresaw the need for special measures or approaches such as exclusive contracts with foreign carriers.
- Participation in the traditional way is likely to be an increasing problem in future in the face of globalization, alliances, competitive pressures and high costs of participation; it will necessitate each State to examine its own circumstances to decide how and to what extent it will participate as well as how to maintain or support that participation.

## **PREFERENTIAL MEASURES**

- A concept drawn from the trade field where trade preferences for developing countries are found in various global (e.g. General Systems of Preferences and Lomé IV) and regional arrangements.
- Concept was introduced at the 1994 Conference by the African States and, in the context of wide disparities in aviation, was presented as a means to "guarantee the effective participation of developing countries"; its promoters indicated that the idea was not intended to hinder liberalization; Conference response to the idea was mixed and ICAO was asked to study it further.
- ICAO Secretariat Study on Preferential Measures examined the purpose and nature of such measures, existing systems and preferences in the air transport system and included a potential list of preferential measures for consideration and possible use by States (see Doc 9587, Appendix 3).
- Preferential measures are to be distinguished from participation measures (see section on Participation) in that the former are non-reciprocal; reciprocity, which is the cornerstone of bilateral relationships, identifies the concept as a departure from established practices; preferential measures therefore require a willingness to depart from traditional approaches and expectations in air transport relationships.

- Thus, the two obstacles to the broad use of preferential measures are: a) conceptual (i.e. it is the opposite of normal practice) and b) practical (in terms of which measures might be acceptable and which would achieve the purpose of ensuring effective participation).
- Suggestions in the ICAO Study cover market access, ownership and control, slot allocation and "doing business".
- As an example of methodology, under the CLMV arrangement (Cambodia, Laos, Myanmar, Viet Nam) (see WP/7), the members agree to specifically seek preferential measures from any outside potential bilateral partner on a non-reciprocal basis, drawing potential measures from the ICAO guidance.

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