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U.S.-China Aviation Relations: Flight Path Toward Open Skies?

Gabriel S. Meyer†

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Introduction

On January 7, 1981, a Civil Aviation Authority of China (CAAC) Boeing 747 touched down at San Francisco International Airport, marking the resumption of air service between the People's Republic of China and the United States for the first time since the Communist Revolution of 1949.1 While the flight's 139 passengers shuffled off the aircraft and made their way through customs and immigration, San Francisco Mayor Dianne Fein-

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stein and Chinese Consul General Hu Ding-yi stood nearby, taking part in a celebratory ribbon-cutting ceremony. Mayor Feinstein called the event "an exciting and historic occasion," while Consul General Hu predicted that the opening of the air route would lead to increased travel between China and the United States. Later that month, Pan American World Airways (Pan Am), which had itself offered U.S.-China service until 1949, resumed service with flights to Shanghai and Beijing.

The resumption of flights from the United States to China was made possible in part by a September 1980 bilateral aviation agreement that granted each country the right to designate two airlines to provide international service between the nations. Without such an agreement in place, the two nations could not have restored international air links. Even today, international flights only operate where authorized by a treaty between the nations served.

The agreement governing U.S.-China airline service was similar to the bilateral agreements that had governed the airline industry since the end of the Second World War. Like its predecessors, the agreement imposed sharp limitations upon the number of flights each country's airlines could operate and limited them to two airports, known as gateway cities, in China, and five in the United States. The agreement also gave each nation the power to review and reject fares charged by the other's airlines.

2. Id.
3. Id.
4. Id.
5. Agreement Between the Government of the United States of America and the Government of The People's Republic of China Relating to Civil Air Transport, Sept. 17, 1980, U.S.-P.R.C., T.I.A.S. No.10,326, at 4 [hereinafter U.S.-China 1980 Agreement]. In 1980, the Civil Aviation Authority of China (CAAC), the Chinese state-run airline, operated all civilian passenger flights in China. Craig S. Smith, China to Merge Domestic Carriers in Reorganization, N.Y. Times, July 22, 2000, at C2. In the late 1980s, however, CAAC was split into six regional carriers. Id. In addition, the Chinese government later allowed provincial governments to create their own airlines. Id.
7. U.S.-China 1980 Agreement, supra note 5, at 40. Initially, both countries could designate two airlines, each of which could operate two weekly roundtrip flights between the United States and China. However, the treaty allocated additional roundtrip frequencies in the event that an airline chose to operate its flights utilizing aircraft with certified maximum takeoff weights of less than 710,000 pounds. Id. An aircraft with a maximum takeoff weight between 430,000 and 710,000 pounds could operate one and a half roundtrips, while, an aircraft with a maximum takeoff weight of less than 430,000 pounds could fly two roundtrips. Id.
8. Id. at 35-36. Under the 1980 agreement, international flights operating between the United States and China were restricted to the following airports in the United States: New York City (John F. Kennedy International Airport), Los Angeles (Los Angeles International Airport), San Francisco (San Francisco International Airport), Honolulu (Honolulu International Airport), and Anchorage (Anchorage International Airport). Id. In China, flights were restricted to the following airports: Beijing (Capital Airport) and Shanghai (Hongqiao Airport). Id. In addition, the agreement specified fourteen alternate airports in the United States and three alternate airports in China to be used in the event of a diversion from the assigned airport. Id.
9. Id. at 17.
In the years that followed, the agreement evolved through a series of amendments to allow an increase in the number of flights and airlines that could operate them. In 1999, the United States and China modified their agreement to allow each nation to authorize four carriers to fly between the two nations beginning in 2001.\textsuperscript{10} As under the original version of the treaty, each carrier can operate passenger service, cargo service or a combination of both.\textsuperscript{11} The amended agreement also allows the designated airlines to serve a number of additional gateway cities\textsuperscript{12} and allows them to serve the gateway cities from any city within their home countries.\textsuperscript{13} Despite liberalization, the agreement continues to cap the total number of weekly flights each country may operate at fifty-four.\textsuperscript{14} Furthermore, the agreement continues to restrict service by U.S. passenger carriers to a handful of gateway cities in China, while similarly limiting the U.S. gateway cities that Chinese passenger carriers may serve.\textsuperscript{15} Currently, U.S. carriers United Airlines, Northwest Airlines, FedEx, and United Parcel Service, and Chinese carriers Air China, China Eastern, and China Southern, share exclusive rights to serve the U.S.-China market.\textsuperscript{16}

\textsuperscript{10} See generally Protocol to the Agreement Between the Government of the United States and the Peoples Republic of China Relating to Civil Air Transport, as amended, Apr. 8, 1999, U.S.-P.R.C., Hein’s No. KAV 5630 [hereinafter 1999 Amendments] (allowing the United States and China to designate up to four airlines to provide U.S.-China service, with each nation’s airlines offering up to fifty-four weekly roundtrip frequencies). Hong Kong, which became a part of China in 1997, continued to be covered under a separately negotiated and less restrictive aviation treaty, which was recently further liberalized.

\textsuperscript{11} Id. at 3–5; U.S.-China 1980 Agreement, supra note 5, at 6. Under the 1992 Amendments, which authorized each country to designate three airlines to provide international service, one designated airline from each nation was limited exclusively to cargo operations. Agreement Between the Government of the United States of America and the Government of The People’s Republic of China Amending the Agreement of September 17, 1980, Feb. 10, 1992, U.S.-P.R.C., T.I.A.S. No.12, 448, at 6-7 [hereinafter 1992 Amendments].

\textsuperscript{12} 1999 Amendments, supra note 10, at 3–5. The 1999 amendments designate Guangzhou, Shanghai, and Beijing as the Chinese cities that U.S. passenger flights may serve. Id. The U.S. government may select two additional Chinese gateway cities that U.S. passenger carriers may serve. Id. The 1999 amendments also permit Chinese passenger flights to serve additional U.S. gateway cities including Chicago, Fairbanks, Seattle, Atlanta, and Portland. Id. The Chinese government may also select two additional U.S. gateway cities to be used for Chinese airline passenger operations. Id. Cargo carriers from both countries may fly to any airport in either country open for scheduled operations. Id.

\textsuperscript{13} Id. at 5.

\textsuperscript{14} Id.

\textsuperscript{15} Id. at 3–5.

\textsuperscript{16} However, it is possible to travel between the United States and China on third-nation carriers. For example, British Airways offers service between the United States and China, requiring a change of planes in London. Although such service is generally non-competitive with direct or non-stop service offered by U.S. and Chinese carriers, third-nation airlines carry approximately one third of all U.S.-China traffic. Alan Larson, Under Secretary of State for Economic, Business, and Agricultural Affairs, U.S. China Aviation Relations: Building for the Future, Remarks at the U.S. China Aviation Symposium, Washington, D.C., Oct. 17, 2000, available at http://usembassy-australia.state.gov/hyper/2000/1017/epf206.htm.
While the airlines of most nations continue to conduct substantial portions of their international flight operations under the auspices of bilateral agreements similar to the U.S.-China agreement, a new liberalization trend has rapidly taken hold in recent years.\textsuperscript{17} The foundation of this U.S.-led trend has been new, nearly restriction-free bilateral treaties, better known as “open skies” agreements.\textsuperscript{18} Under an open skies agreement, the airlines of the nations party to the agreement may operate flights between the two nations, restricted only by safety concerns and airport capacity issues.\textsuperscript{19} Unlike standard bilateral agreements, open skies agreements eliminate traditional governmental roles in determining routes, designating the airlines that may fly them, and controlling frequency of service and pricing.\textsuperscript{20} Instead, under an open skies agreement, market forces determine these matters.\textsuperscript{21}

Proponents of open skies agreements contend that such arrangements stimulate airline competition, which in turn lead to lower fares and better service for the traveling public.\textsuperscript{22} They argue that open skies permit aviation markets to grow in accordance with demand, thereby allowing airlines to offer more convenient and affordable air service to both passengers and shippers.\textsuperscript{23} This growth, they argue, leads to economic expansion for the nations party to the agreement.\textsuperscript{24} Although the oldest open skies agreements date back only a decade, evidence suggests that the proponents of such agreements are correct.\textsuperscript{25} In numerous instances, growth in open skies aviation markets has significantly outpaced growth in similar markets governed by traditional, more restrictive bilateral treaties. Furthermore, in open skies markets, service levels have increased while fares have fallen.\textsuperscript{26}

Counted among the ranks of open skies proponents are U.S. airlines, which seek to expand their operations, especially in rapidly growing economies like China’s. In fact, China, with a population of well over one billion people and a GDP of one trillion dollars, represents a potential gold

\textsuperscript{18} Id. at 1213-15.
\textsuperscript{19} Id. at 1213.
\textsuperscript{20} Id.
\textsuperscript{21} Id.
\textsuperscript{22} U.S. Department of Transportation Secretary Rodney Slater has made such an argument. Aviation Pact Lifts Flight, Price Restrictions for Pacific Rim, AIRLINE FIN. NEWS, Nov. 27, 2000.
\textsuperscript{23} Id.
\textsuperscript{24} See China Liberalization Seen As Key To WTO, PNTR Benefits, AVIATION DAILY, Oct. 19, 2000, at 7.
\textsuperscript{26} Id.
mine for the U.S. airline industry. Although China's passenger aviation market stands at approximately one fifth the size of the U.S. market, its potential for growth appears enormous. Additionally, China is the United States' second largest trading partner, and air cargo traffic between the two nations grew at twice the rate of passenger traffic during the late 1990s.

There remain, however, opponents of open skies agreements, most notably governments of nations that subsidize national flag carriers and therefore fear the consequences of unrestrained competition against more efficient foreign carriers. Other opponents include the airlines themselves, which may benefit from their positions as incumbent carriers in markets closed to new entrants. Additionally, some airline industry observers have warned of the risk of "destructive competition" among airlines that may accompany a move toward a deregulated open skies environment.

Parts I and II of this Note examine the developments leading to the implementation of open skies agreements, and their effects upon the airline industry and the member countries' economies. In Part III, this Note discusses the impact of early open skies agreements. Parts IV and V review recent developments in the U.S.-China aviation market and explore the sources of resistance to the implementation of an open skies agreement in

29. See Brookings Economist Says U.S. Should Use New China Air Services to Expand Air Cargo Capacity; Robert C. Litan Says Economic Value to the U.S. of New Cargo Capacity Exceeds Benefits of Adding New Passenger Routes, PR NEWSWIRE ASS'N INC., Apr. 4, 2000, LEXIS, News Library [hereinafter Brookings Economist]. According to Brookings Institution economist Robert E. Litan, forty percent of world trade, measured by value, travels via air cargo. Id. U.S. exports of high value goods, such as computers and telecommunications equipment, to China shipped via all modes of transport have grown rapidly in recent years. Id.
30. One U.S. airline observer recently commented, "Like most governments, the [Chinese] transport ministries are a bit too preoccupied with the health of their airlines and therefore spend little time understanding the effects transport systems have on the economy as a whole." China Says Slow, U.S. Pushes for Go, WORLD AIRLINE NEWS, Oct. 20, 2000, LEXIS, News Library [hereinafter U.S. Pushes for Go].
31. For example, British Airways has benefited tremendously in recent years from its status as the dominant carrier at London's Heathrow Airport. The U.S.-Britain aviation treaty, a restrictive bilateral agreement known as Bermuda II, severely limits American airlines' access to Heathrow. See, e.g., Lick, supra note 17, at 1264.
32. Andras Vamos-Goldman, The Stagnation of Economic Regulation Under Public International Law Air Law: Examining Its Contribution to the Woeful State of the Airline Industry, 23 TRANSP. L. J. 425, 444-45 (1996). Destructive competition, Vamos-Goldman notes, may result from overcapacity, which can accompany a move towards deregulation, as numerous new airlines simultaneously enter the market. Id. The inherent unpredictability of open skies and deregulation makes it difficult for airlines to engage in long-range planning, which is necessary for many aspects of operations—notably fleet acquisition. Id.
that market. In Part VI, this Note considers the potential impact of a U.S.-China open skies agreement and proposes strategies for the U.S. government to employ in negotiating such an accord with China. This Note concludes that in addition to any inducements the U.S. government offers China to move toward open skies, the United States must continue to steadfastly promote the benefits of open skies, which extend far beyond the airline industry.

I. Pre-Open Skies: An Overview

Traditional bilateral aviation agreements are best characterized by the restrictions they impose upon the airlines flying between the signatory nations. These restrictions typically limit the number of airlines authorized to fly between the two nations, the number of flights operated, the total passenger and cargo traffic carried, and the fares charged.

A. The Chicago Convention

Two international conventions provided the impetus for the creation of traditional, restrictive bilateral agreements that governed international airline operations for nearly half a century. The Paris Convention of 1919, signed by thirty-two nations, set forth aircraft operation standards and specifications, and required party nations to release aviation information necessary for international flights to occur. During ensuing decades, however, world leaders realized that the rapidly expanding commercial aviation industry required a more comprehensive agreement. This led to the Conference on International Civil Aviation in Chicago, attended by more than fifty nations in late 1944.

The resulting Convention on International Air Services Transit Agreement (Chicago Convention) established two key "freedoms" of the sky among the signatory nations: (1) the right of a nation's airlines to fly over the territory of another nation in order to reach a third; and (2) the right of a nation's airlines to make technical stops for fuel and maintenance, but not to load or unload passengers or cargo, in another nation while in

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33. These include efforts to establish additional cooperative agreements between U.S. carriers and their Chinese counterparts as a condition to an open skies agreement. Cooperative agreements, ranging from coordination of services to strategic alliances and partnerships, could help Chinese airlines begin to close the gap with their U.S. competitors and allay Chinese government officials' fears of the elimination of their airlines by a highly efficient and competitive U.S. airline industry operating under the guise of an open skies agreement. However, as indicated by the tremendous financial losses that the U.S. airline industry suffered in the aftermath of the events of September 11, 2001, the invincibility of the U.S. airline may not equate with the Chinese government's fears. See infra, subpart V(C).

34. Lick, supra note 17, at 1211.

35. Id.


37. Id.

38. Id. at 544-45.
transit to a third nation.\textsuperscript{39}

Notwithstanding these advances, the Chicago Convention proved more notable for what it did not establish. Despite strong U.S. support, the signatory nations failed to ratify a proposed annex\textsuperscript{40} setting forth three more freedoms: (1) the right of one nation's airlines to freely transport cargo and passengers from its home nation to a second nation; (2) the right of one nation's airlines to freely transport cargo and passengers from a second nation back to its home nation; and (3) the right of one nation's airlines to freely transport cargo and passengers between a second and third nation, also known as a "fifth freedom" or a "beyond right."\textsuperscript{41} Instead, the Chicago Convention left these rights to individual nations to negotiate with each other on a case-by-case basis.\textsuperscript{42} Had these three freedoms won approval, the Chicago Convention would, in effect, have established a broad, multilateral open skies agreement among many of the world's industrialized nations.

B. Bermuda I and Its Progeny

In 1946, following the Chicago Convention, the United States negotiated a treaty with Great Britain,\textsuperscript{43} creating the first of more than 1,200 bilateral aviation agreements currently in existence.\textsuperscript{44} Known as Bermuda I,\textsuperscript{45} the agreement represented a compromise between two sharply opposing views on the regulation of international air transport.\textsuperscript{46} The United States supported a largely unregulated aviation market; whereas, Britain sought greater governmental control.\textsuperscript{47}

More importantly, Bermuda I helped to institute acceptance of government involvement in the regulation of international air service.\textsuperscript{48} In the aftermath of World War II, most nations shared Great Britain's desire for government regulation of international air service.\textsuperscript{49} While the U.S. airline industry had prospered during the war, European airlines, many of them

\begin{itemize}
  \item \textsuperscript{39} Id. at 545-46.
  \item \textsuperscript{40} Agreement Between the United States of America and the Powers Respecting Air Transport, Dec. 7, 1944, 59 Stat. 1701.
  \item \textsuperscript{41} Id. The following is an example of a beyond right: Delta Airlines at one time offered flights from New York City to Frankfurt, Germany, in accordance with the terms of an open skies agreement between the United States and Germany. From Frankfurt, these flights continued onto Bombay (Mumbai), India. Under the agreement, Germany could not restrict Delta's right to carry passengers and cargo between Frankfurt and Bombay (Mumbai). Id.
  \item \textsuperscript{42} Id. at 546.
  \item \textsuperscript{43} Baliles, supra note 6, at 8; Goo, supra note 36, at 548.
  \item \textsuperscript{44} Baliles, supra note 6, at 8.
  \item \textsuperscript{45} Agreement Between the Government of the United States of America and the Government of the United Kingdom Relating to Air Service Between their Respective Territories, Feb. 11, 1946, U.S.-U.K., 60 Stat. 1499.
  \item \textsuperscript{46} Goo, supra note 36, at 545-48; Paul Stephen Dempsey, Turbulence in the "Open Skies": The Deregulation of International Air Transport, 15 TRANSIT. L. J. 305, 315-16 (1987).
  \item \textsuperscript{47} Dempsey, supra note 46, at 316-17.
  \item \textsuperscript{48} Id. at 316.
  \item \textsuperscript{49} Goo, supra note 36, at 545.
\end{itemize}
state-owned, had been decimated and faced the challenge of rebuilding. As a result, British negotiators sought to create a restrictive agreement, which they hoped would allow their nation's war-ravaged airline industry an opportunity to recover and grow, rather than suffer in the face of heavy competition from U.S. carriers.

While economic fears undoubtedly led to the Chicago Convention and the subsequent Bermuda I agreement, national security concerns may also have played a role. The Chicago Convention came near the end of World War II, which saw aerial warfare rise to new heights, and witnessed previously unimaginable levels of destruction inflicted by military aircraft. According to one commentator, as a result of the recent devastation, "It is no wonder that national security considerations played as great of a role as economic protectionism, in making absolute state sovereignty the basic legal premise of public international air law." While the United States and Britain remained close allies, their agreement still created a precedent helping to promote this principle.

Under the terms of Bermuda I and similar agreements that followed, the airlines of each nation could operate service only to and from designated gateway cities in each country. Although Bermuda I allowed airlines to operate an unlimited number of flights, the agreement left responsibility for fare determination in the hands of the International Air Transport Association (IATA). In addition, while the airlines were free to set their own flight schedules, each nation retained the right of ex post facto review of the other's airline operations. Provisions in Bermuda I and its progeny required that the "interest of the air carriers of the other government shall be taken into consideration so as not to affect unduly the services which the latter provides on all or part of the same route."

The United States subsequently negotiated Bermuda I-style agreements with most of the seventy-five nations with which it had established aviation relations. Meanwhile, around the world, other nations modeled their own international aviation accords in the image of Bermuda I. Such restrictive agreements allowed these nations to develop their aviation

50. Id.
51. Dempsey, supra note 46, at 312.
52. Vamos-Goldman, supra note 32, at 430.
53. Id.
54. Id.
56. Id. at 318. The International Air Transport Association (IATA) is composed of airlines certified to offer scheduled operations. Historically, this organization dealt primarily with fare determination on international routes. However, IATA also focuses on international civil aviation from technical, legal, and financial standpoints. Id. at 314-15.
58. Id. at 317 (citing United States Standard Form of Bilateral Air Transport Agreement, art. 8-10 (1953)).
59. Dempsey, supra note 46, at 316. Most of these subsequent agreements took the form of executive agreements rather than treaties. Unlike treaties, executive agreements do not require the approval of the U.S. Senate before they take effect. Id.
60. Baliles, supra note 6, at 8.
industries at their own paces, free from the forces of unchecked economic competition.\textsuperscript{61} This system of restrictive, individually negotiated bilateral aviation treaties did not impose a serious impediment to economic growth because a small number of people traveled by air during the early decades of the post-war era,\textsuperscript{62} and because of the primitive state of aviation technology, which limited the practicality of long-haul international air service.\textsuperscript{63}

II. The Flight Path to Open Skies

A. Untenable Agreements

As world aviation markets developed during the ensuing decades, the system of restrictive agreements modeled after Bermuda I became increas-ingly untenable. Gerald L. Baliles, the chair of the National Airline Commission during the early months of the Clinton Administration, noted that the old system of agreements "represent[s] a global regulatory morass that has the ultimate effect of managing trade in basic transportation in order to maintain major countries' market share and protect home carriers and labor forces."\textsuperscript{64}

Furthermore, Bermuda I ceased to exist.\textsuperscript{65} Great Britain renounced the agreement in 1976 and negotiated an even more restrictive treaty known as Bermuda II.\textsuperscript{66} Senate Commerce Committee Chairman Howard Cannon (D-Nev.) described Bermuda II as "the greatest step backward in forty years of attempting to bring market-oriented competition to international aviation."\textsuperscript{67} In addition to wiping out U.S. carriers' beyond rights, which under Bermuda I had allowed them to fly between Britain and points in Continental Europe, Bermuda II reduced the number of U.S. carriers permitted to fly to London's sought-after Heathrow Airport to two.\textsuperscript{68} Bermuda II helped give rise to British Airways' domination over the transatlantic market, and, by 1997, allowed British carriers to capture more than sixty percent of U.S.-Britain passenger traffic.\textsuperscript{69} Bermuda II, however, came as an anomaly in an era marked by movement toward airline deregulation.

\textsuperscript{61.} Id.
\textsuperscript{62.} Id.
\textsuperscript{63.} For example, in 1949, shortly before China's Communist takeover, Pan Am's U.S.-China operations consisted of a single weekly flight, departing Los Angeles at 7:45 p.m. Thursday and arriving in Shanghai at 3:15 p.m. Sunday. En route, this flight made stops in Honolulu, Wake Island, and Tokyo, Japan for servicing and refueling. PAN AMERICAN WORLD AIRWAYS, PAN AMERICAN WORLD AIRWAYS SYSTEM TIME TABLE, May 1, 1949, at 2.
\textsuperscript{64.} Baliles, supra note 6, at 8.
\textsuperscript{65.} Dempsey, supra note 46, at 331.
\textsuperscript{66.} Id.
\textsuperscript{67.} Id. at 332.
\textsuperscript{68.} Lick, supra note 17, at 1264. The two American carriers are American Airlines and United Airlines. Id.
\textsuperscript{69.} Id. United Airlines claims that Bermuda II has cost the United States "billions of dollars in revenue and thousands of jobs." Id.
B. The Birth of Deregulation

The recent trend toward open skies agreements began not with liberalization of the international air market, but rather with U.S. enactment of the Airline Deregulation Act of 1978. Prior to the passage of the Airline Deregulation Act, the Civil Aeronautics Board (CAB) maintained tight control over the U.S. airline industry, awarding new routes and permitting fare adjustments with deliberate hesitancy. Airlines seeking the right to serve new routes or alter their fare structures had to petition the CAB, which would then solicit input from adversely affected carriers before rendering a decision.

Following the passage of the Airline Deregulation Act, the CAB loosened its grip on the industry, granting airlines full freedom to select domestic routes by the end of 1981, and dropping all domestic fare regulations by the end of the following year. The CAB itself ceased to exist by the mid-1980s. Between 1978 and 1999, in the aftermath of deregulation, inflation-adjusted fares fell twenty-seven percent while passenger counts rose from just under 275 million air travelers in 1978 to more than 665 million in the year 2000.

The impact of deregulation spilled over into international aviation markets as well. Pleased with the initial success of deregulation, the Carter Administration, in conjunction with the CAB, granted several U.S. airlines new authority to serve international markets in the 1970s. In the U.S.-London market, the CAB awarded new routes to Braniff and Delta Airlines, both of which had not previously flown transatlantic routes. At the same time, the CAB finished reviewing several airline route petitions, which led to decisions granting United Airlines a Pacific Northwest-Tokyo route, and several new carriers the rights to serve the Philadelphia-Bermuda market.

72. Id.
73. Id. at 319-20.
74. Id.
75. Virginia Postrel, Don't Blame Deregulation for Airline Problems; Blame Not Enough Deregulation, N.Y. TIMES, Oct. 5, 2000, at C2 (citing a study conducted by Northeastern University economist Steven A. Morrison and Brookings Institution economist Clifford Winston).
79. Id. at 330. However, under the terms of Bermuda II, Delta and Braniff could not serve Heathrow airport. They were, therefore, relegated to using London's secondary airport—Gatwick. Id.
80. Id. at 339.
III. Open Skies Emerge

The United States signed its first open skies agreement in October 1992 with the Netherlands. The agreement came as the first in a series of open skies agreements advocated by U.S. Secretary of Transportation Andrew Card earlier that year. Card proposed initially establishing open skies agreements with all European nations with the hope that other nations would follow suit and enter into similar agreements. These agreements granted all airlines of signatory nations nearly unrestricted marketplace freedom, including the right to offer any number of flights and level of capacity on routes between the nations. Additionally, these early open skies agreements eliminated restrictions on beyond rights. The agreements also virtually eliminated fare restrictions, instead implementing "double-disapproval pricing." Under this scheme, rejection of an airline's fare structure required disapproval by both nations party to the agreement. Furthermore, open skies agreements allowed airlines to form strategic alliances with their foreign counterparts in order to provide enhanced service between the United States and European nations.

By the middle of 1998, the United States had negotiated open skies agreements with thirteen European nations, and forty percent of all transatlantic traffic traveled on flights operated under open skies agreements. England and France, however, remained notable exceptions, not becoming parties to open skies agreements. The United States also launched an effort to establish open skies agreements with its non-European aviation partners, including a 1995 agreement with Canada. Additionally, the United States implemented agreements with nations in South America, Asia, and Oceania, including, Peru, Malaysia, Taiwan, and New Zealand. By early 2002, the United States had entered into open skies agreements

81. Goo, supra note 36, at 552.
82. See id. at 550-51.
83. Id. at 551.
84. See Gilbert Fisher, Note, 1998 Amendment to the U.S.-Japan Civil Air Transport Agreement: The Battle May be Won, but the War for Open Skies is Far from Over, 9 MINN. J. GLOBAL TRADE 327, 331 (2000). Open skies agreements are said to incorporate, at a minimum, the first five freedoms contained in the Chicago Convention. Id.
85. Goo, supra note 36, at 551.
86. Id. This applies to third and fourth freedom markets. Id.
87. Lick, supra note 17, at 1216-17.
88. Id. at 1215-18.
89. Id. at 1216, 1218. Great Britain has a history of restrictive aviation agreements with the United States that significantly benefited its major carrier, British Airways. Id. at 1264. The United States reached a new aviation agreement with France in 1998. See id. at 1216. Although the treaty falls short of previously negotiated open skies agreements because it fails to provide unlimited beyond rights, it removes all capacity controls on U.S.-France flights over a five-year period. See Michael A. Taverna & Pierre Sparaco, U.S., France Approve Long-Awaited Bilateral, AVIATION Wk. & SPACE TECH., Apr. 13, 1998, at 60. Part of France's resistance to an immediate elimination of capacity controls and beyond rights restrictions may lie with the fact that French airlines lack the capacity to expand their operations so as to take full advantage of an open skies agreement. Id.
91. Lick, supra note 17, at 1219-20.
with fifty-six nations, including a first-of-its-kind multilateral agreement with Brunei, Chile, New Zealand and Singapore, which allowed the airlines of each country to fly between the five nations without restrictions.

A. The Benefits of Open Skies

Open skies agreements thus far appear to have had their desired effects. A 2000 U.S. Department of Transportation (DOT) report indicated that average fares fell by twenty percent between 1996 and 1999 in U.S.-Europe open skies markets. In U.S.-Europe markets not operated under open skies agreements, the DOT report found that fares during the same period declined by little more than ten percent. Additionally, the DOT report found that total passenger traffic between the United States and Europe rose by more than fifty percent between 1992 and 1999, with the greater part of the increase occurring between 1997 and 1999, after a significant number of open skies agreements had come into effect. The DOT report further noted that airlines that formed alliances with foreign airlines in the wake of open skies agreements enjoyed substantially higher traffic growth than those carriers that did not form such alliances. Another study concluded that in European markets and beyond, allied carriers charged fares averaging twenty-five percent less than those charged by non-allied airlines serving identical markets.

The 1995 U.S.-Canada agreement also proved quite successful. Prior to the inauguration of the agreement, U.S.-Canada passenger traffic had grown at an annual rate of 1.5 percent, whereas, following the agreement, growth skyrocketed to eleven percent.

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92. Daniel Dombey & Mark Odell, EU Court Finding Threatens ‘Open Skies’ Agreements: Efforts to Consolidate Fragmented Airline Sector May be Boosted, FIN. TIMES, Feb. 1, 2002, at 1. However, a recent ruling by the European Court of Justice could jeopardize open skies agreements already in effect between the United States and EU members. Mark Landler, Europe’s Highest Court Voids Air Treaties, N.Y. TIMES, Nov. 6, 2002 at C1. The Court ruled that the treaties are void because under EU law, individual EU members cannot negotiate bilateral treaties with foreign nations. Id. While the various open skies agreements will remain in effect until the United States and EU members can negotiate new ones, the Court’s ruling raises the possibility that the United States may seek to conclude a U.S.-EU open skies treaty to take the place of the previously negotiated individual agreements. See id.

93. Aviation Pact Lifts Flight, Price Restrictions For Pacific Rim, supra note 22.

94. U.S. DOT REPORT, supra note 25, at 3.

95. Id.

96. See id. at 4.

97. Id. at 5–9.

98. Jan K. Bruekner & W. Tom Whalen, The Price Effects of International Airline Alliances, 43 J. L. & ECON. 503, 542 (2000). According to the author’s study, allied carriers coordinate their schedules with one another and offer cooperative pricing which minimizes operational inefficiencies, thus allowing the allied carriers to reduce fares further, and as a result, draw even more passenger traffic. Id. at 504, 542.

99. See Biederman, supra note 90, at 37 (quoting Rep. Jim Oberstar, senior Democrat on the House Transportation Committee and former Chairman of the House Subcommittee on Aviation).
B. Not All Airlines Win Under Open Skies

Clearly, that which benefits the traveling public is not always in every airline's best interest. Some airlines will thrive in the competitive environment created by open skies agreements, while others will undoubtedly fail. Because most of today's open skies agreements are only a few years old, it is difficult to judge their long-term impact upon the affected airlines. Perhaps the best indicator of open skies agreements' long-term effects is the experience of U.S. airlines in the aftermath of deregulation, more than twenty years ago.

Although the Airline Deregulation Act of 1978 solely affected domestic airline service, parallels between it and open skies agreements abound. Under both schemes, airlines may fly where they choose when they wish, and charge any fare for their service. The absolute freedom of deregulation prompted some U.S. airlines, including American, United, and Delta Airlines to prosper as they adjusted to the newly deregulated environment by building hub and spoke route networks that made it possible for them to transport passengers virtually anywhere in the country. Other carriers, notably aviation pioneer Pan Am, could not adapt to the new system, and after many painful years, went out of business. Just as important, the successful carriers avoided the costly labor that other carriers experienced, such as Eastern Airlines, which, along with Pan Am, closed its doors in the early 1990s. Thus, as with deregulation in the U.S. domestic market, a shift toward open skies in the U.S.-China market carries with it the potential to force some airlines out of the industry.

IV. The United States and China

During the years leading up to the 1999 amendments, the U.S. and Chinese airline industries were a study in contrast. The U.S. airlines had enjoyed handsome profits for several years, while the Chinese airlines struggled to cut losses and deal with issues as fundamental as safety. Against this backdrop, the Chinese government was reluctant to open up any of its air travel market to free competition.

100. Heppenheimer, supra note 71, at 341.
101. See, e.g., Robert Gandt, Skygods: The Fall of Pan Am (1995). When deregulation took effect, Pan Am operated almost no domestic routes within the continental United States, having traditionally flown overseas routes exclusively. Following deregulation, Pan Am's overseas routes suffered as carriers like American, United, and Delta, made inroads into these markets, and used their hub and spoke networks to feed traffic into them. Id. In the early 1980s, Pan Am acquired National Airlines in an attempt to establish a domestic network to bolster its international operations. However, Pan Am's weak financial position soon forced it to sell off other assets. Id. The airline sold its Pacific Division, including its China routes, to United Airlines for $750 million in 1985, and ceased operations completely in 1991. Id.
102. Id.
A. Chinese Airlines: A Turbulent History

Although home to more than 1.2 billion people, China does not yet have an aviation market to match its population. Prior to 1988, when the CAAC relinquished its monopoly on Chinese airline service and authorized the formation of semi-autonomous airlines, it functioned in a manner similar to the former Soviet Union’s Aeroflot. Best known among its few passengers for poor service, unreliable schedules, and a disastrous safety record, the CAAC earned nicknames like “China Airlines Always Cancels,” and “China Airlines Always Crashes.” Today, the CAAC retains regulatory oversight over the rapidly expanding airline industry. Chinese airlines, which carried slightly more than eleven and a half million passengers during 1987, the final year of the CAAC monopoly, grew to carry approximately sixty-one million passengers in 1995. Although passenger traffic growth stagnated for several years during the late 1990s, in 1999, the total number of passengers carried by Chinese airlines remained near sixty million. Nevertheless, the IATA forecasts that China's total number of airline passengers will reach 291.5 million by 2010, while the Boeing Company predicts that by 2020, China's civil aviation market will grow to become second only to that of the United States.

Chinese airlines have struggled in recent years with both safety and economic issues. Rapid expansion led to a spate of accidents in the early 1990s that temporarily made Chinese airlines the most dangerous in the world. Between 1989 and 1994, 642 people died in accidents involving Chinese airlines, although safety has improved considerably since then as the result of aggressive government-sponsored efforts. Nevertheless, the traveling public's safety fears linger. Despite Chinese air-

103. WORLD BANK GROUP, supra note 27.
104. Despite having a population four times larger than that of the U.S., China generates approximately one tenth the number of air passengers each year. Id.; see China Forecasts Need For 900 Aircraft for Its Carriers, supra note 28; HISTORICAL AIR TRAFFIC STATISTICS ANNUAL: 1981-2000, supra note 29.
111. Id.
112. Fisher, supra note 84, at 329.
114. Smith, supra note 5, at C2.
115. Id.
lines’ improved safety records, many travelers still avoid them due to the perception that they are less safe than their American competitors.\(^\text{117}\) Several major crashes involving Asian airlines in recent years—including two involving Chinese airlines in 2002—have only fueled these fears.\(^\text{118}\)

In more recent years, the stagnation of passenger traffic has contributed to Chinese airlines’ economic losses. The Chinese airline industry collectively lost $294 million in 1998,\(^\text{119}\) and another $200 million during the first six months of 1999\(^\text{120}\) before rebounding in 2000.\(^\text{121}\) Despite profitability in 2000 by some of the larger carriers, the earlier losses prompted the Chinese government in July 2000 to order a consolidation of its airline industry.\(^\text{122}\) Under its recently finalized plan, nine state-owned airlines, as well as smaller airlines owned by local government authorities, are to merge into three large groups of airlines, each headed by one of three established Chinese carriers: Air China, China Eastern, and China Southern.\(^\text{123}\) Meanwhile, in the United States, the airline industry remained prosperous through the latter half of the 1990s, posting a net income of $4.6 billion in 1999.\(^\text{124}\)

All of China’s airlines continue to be owned in part by regional or national government authorities.\(^\text{125}\) While the CAAC itself no longer operates the airlines, and will soon give up its ownership stake in them once the consolidation process is completed, it has continued to hold them on a short leash in recent years, dictating matters including merger activity, route planning, fare determination and aircraft acquisition. In addition to its order to consolidate the airline industry in 2000, the CAAC called on Chinese airlines to develop hub and spoke route networks modeled after


\(^{118}\) See id. The airlines of the P.R.C. should in be confused with Taiwan’s China Airlines, also known for its poor safety record in recent years. See id. However, China’s airlines suffered a spate of accidents in early 2002. A China Northern Airlines plane crashed into the ocean off the coast of northeastern China, while an Air China flight plowed into a mountain in South Korea. *Analysis: China’s Air Safety*, *BBC News*, May 10, 2002, available at http://news.bbc.co.uk/1/hi/world/asia-pacific/1974946.stm. Nearly 250 passengers and crewmembers died in the two accidents. Id.


\(^{121}\) *China Civil Aviation May Earn Little This Year*, *Xinhua Gen. News Service*, Nov. 9, 2000, LEXIS, News Library.


\(^{123}\) See id. (noting these were the same three Chinese airlines that were already designated to fly between the U.S. and China); Guo Aibing, *Airline Mergers Get Green Light*, *China Daily*, Feb. 6, 2002, available at 2002 WL 7167165. In October 2002, China’s State Council finalized the merger plan, which was expected to take a year to implement. Nicholas Ionides, *China’s State Council Blesses Mergers*, *Airliner Business*, Nov. 1, 2002, at 27. Under the plan, the CAAC is to give up ownership in the nation’s airlines. Id.

\(^{124}\) See id. (noting these were the same three Chinese airlines that were already designated to fly between the U.S. and China); Guo Aibing, *Airline Mergers Get Green Light*, *China Daily*, Feb. 6, 2002, available at 2002 WL 7167165. In October 2002, China’s State Council finalized the merger plan, which was expected to take a year to implement. Nicholas Ionides, *China’s State Council Blesses Mergers*, *Airliner Business*, Nov. 1, 2002, at 27. Under the plan, the CAAC is to give up ownership in the nation’s airlines. Id.

\(^{125}\) See id. (noting these were the same three Chinese airlines that were already designated to fly between the U.S. and China); Guo Aibing, *Airline Mergers Get Green Light*, *China Daily*, Feb. 6, 2002, available at 2002 WL 7167165. In October 2002, China’s State Council finalized the merger plan, which was expected to take a year to implement. Nicholas Ionides, *China’s State Council Blesses Mergers*, *Airliner Business*, Nov. 1, 2002, at 27. Under the plan, the CAAC is to give up ownership in the nation’s airlines. Id.
In the area of fare regulation, the CAAC announced in early 2001 that it would restrict the ability of airlines to increase their fares to compensate for rising fuel prices. The CAAC took this measure despite evidence that rising ticket prices had only a negligible effect on demand for domestic air travel in China and despite fears that higher fuel costs would drive the Chinese airline industry back toward unprofitability. And, once again trying its hand in aircraft acquisition policy, in 2000 the CAAC pressured Xinjiang Airlines (one of many carriers expected to disappear following the industry consolidation) to purchase several Russian-made Ilyushin aircraft. This course of action came as an about-face from the CAAC's call several months earlier for Chinese carriers to rid their fleets of Russian aircraft. The CAAC has also declared that, in the long-run, it intends to deregulate China's aviation industry.

B. The U.S. Airline Behemoths

Predictably, the turmoil in the Chinese airline industry left the nation's authorities in no mood to pursue an open skies agreement with the United States, the largest player in the aviation world. As the CAAC's Director General for the Department of International Affairs and Cooperation noted, "You must remember that there are individual airlines in the U.S. that have a larger fleet than the whole of China." One such carrier was United Airlines, one of the two U.S. passenger carriers authorized to serve China, which in July 2000 maintained a fleet of 594 aircraft or seventy-four more than the total number of aircraft operated by all the civil carriers in China combined. Another such carrier was FedEx, which operated cargo flights to China, drawing on its fleet of approximately 650 aircraft. The third and final airline authorized to

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126. Nicholas Ionides, China Outlines Hub and Spoke Strategy, AIR TRANSPORT INTELLIGENCE, Nov. 8, 2000, LEXIS, News Library. In addition to calling on Chinese Airlines to develop hub and spoke route networks, the CAAC also encouraged the airlines to acquire a fleet of smaller aircraft necessary to support such a route structure. Id. At the end of the year 2000, Chinese airlines collectively owned only sixty-two aircraft seating less than seventy passengers. Id.

127. China Civil Aviation May Earn Little This Year, supra note 121.


129. Id.

130. Id.

131. Thomas, supra note 120, at 49-50.

132. See U.S. Pushes for Go, supra note 30. CAAC's Wang Ronghua stated in October 2000, "We should not lose sight of the fact that the aviation systems of the U.S. and China are at different levels, and it will take time for China to catch up. It is in all our best interests that the progress be taken gradually." Id.

133. Id.


provide U.S.-China service prior to April, 2001 was Northwest Airlines. With a fleet of more than 400 aircraft, Northwest continues to operate a combination of passenger and cargo-only flights to China.

Although in 2001 the U.S. airline industry plunged into its darkest hour in the wake of the September 11 terrorist attacks, the 1999 amendments to the U.S.-China aviation treaty were negotiated against a backdrop of U.S. airline prosperity and continued morass in the Chinese airline industry. United, FedEx, and Northwest Airlines remained highly profitable into the late 1990s, posting annual profits in 1999 of $1.24 billion, $442 million, and $300 million, respectively. A variety of other statistics, including passenger traffic data and aircraft utilization rates, also attest to the U.S. airline industry's dominance during the late 1990s.

137. U.S. Pushes For Go, supra note 30.
140. In the passenger traffic category, Northwest Airlines reported that during 2000, its Pacific operations, which included its flights to China, generated nearly twenty-three billion revenue passenger miles (one RPM equals one passenger flown one mile). Northwest Airlines Corp., Investor Relations, Northwest Airlines Reports December and Year-End Traffic, Jan. 5, 2001, at http://www.corporate-ir.net/ireye/ir_site.zhtml?ticker=NWAC&script=410&layout=9&item_id=142012. Northwest's Pacific operations include flights operating between the United States and Asia, as well as intra-Asia flights; data for Northwest's overall U.S.-China operations was unavailable. See id. Pacific operations flights operated with an average passenger load factor (percentage of seats sold) of 81.7%. Id. Load factors are a key measure of an airline's performance; a high load factor, indicating that an airline sells a high percentage of its available seats, suggests efficient operations. The load factor on Northwest's bi-weekly Detroit-Shanghai service, which it launched during the spring of 2000 using newly allocated slots, averaged eighty-five percent during its initial months of operation. NW Non-stop Detroit Profits, ASIANINFO DAILY CHINA NEWS, July 5, 2000, at 4, LEXIS, News Library. United Airlines performed similarly during the first six months of 2000 with its Pacific operations producing 11.5 billion revenue passenger miles, with an average load factor of 70.8%.UAL Corp., United Airlines Investor Relations, United Airlines' June Traffic Increases 6.5% as Passenger Load Factor Surges 5.7%, July 5, 2000, at http://www.corporate-ir.net (United's Pacific operations include flights operating between the United States and Asia, as well as intra-Asia flights; data for United's U.S.-China operations was unavailable.) [hereinafter United June Traffic]. FedEx also posted respectable numbers, carrying an average cargo weight load factor (the percentage of maximum cargo capacity utilized, measured by weight) of 64.2% on its international flights in 1998. IATA: World Air Transport Statistics, June 1999, at 91 (data for China-U.S. service unavailable).

By contrast, Chinese airlines' operating statistics did not compare with those of the U.S. carriers. The three providers of service to the United States—Air China, China Eastern, and China Southern—generated passenger load factors of 59.6, 58, and 53.1%, respectively, in 1998 on their international routes. Id. at 60, 79-80 (including all international service operated by each airline; data for China-U.S. service was unavailable). While Chinese airlines rarely disclose load factors generated by their transpacific operations, industry analysts estimated that load factors on these flights averaged only fifty percent during the late 1990s. Patrick Baert, China Ill-Prepared to Profit from Aviation Accord with U.S., AGENCE FR. PRESSE, Apr. 8, 1999, LEXIS, News Library. During the same time period, China's airlines' collective international operations produced approximately 10.3 billion revenue passenger miles, or less than half of that generated by either United's or Northwest's Pacific operations in 2000. See id. (converting kilometers to miles by multiplying each figure by 0.621). More recently, however, China Southern Airlines reported that during December 2001, its Los Angeles-Guangzhou flights produced a stunning passenger load factor of ninety percent. China Southern Posts Record
These statistics illustrate the disparities between the mature and relatively efficient U.S. airline industry and its less experienced Chinese competition. Such disparities lay at the heart of China's resistance to an open skies agreement with the United States. From the Chinese perspective, the possibility of greater U.S. airline access to Chinese markets represented a threat. The Chinese airlines feared they would either be forced to withdraw from the U.S.-China market, or compete with money-losing service.

V. Amending the U.S.-China Agreement

The 1999 amendments to the U.S.-China aviation treaty represent the greatest step toward liberalization of the U.S.-China aviation trade since the original agreement took effect in 1980.141 However, progress prior to 1999 came in smaller increments.142 In the decade that followed implementation of the 1980 agreement, service gradually expanded until negotiations led to the 1992 amendments, which authorized a dramatic increase in the number of flights that each nation's airlines could fly.143 The United

Passenger Loads on China-U.S. Service, AVIATION DAILY, Jan. 22, 2002. Data from other Chinese carriers suggests that their load factors may also have risen recently. China Airlines' Costs from Sept. 11 Attacks Seen at 1.41 Bln. Yuan, AFX-Asia, Nov. 20, 2001 [hereinafter China Airlines Sept. 11 Costs].

Through the 1990s, aircraft utilization rates also reflected the advantages U.S. carriers held over their Chinese competitors. A higher utilization rate, as measured by the average number of hours an aircraft is used each day, generally indicates a more efficient airline. In 1998, both United and Northwest Airlines operated each of their Boeing 747-400 aircraft, the workhorses of their U.S.-China operations, an average of more than twelve hours each day. IATA: World Air Transport Statistics, June 1999, at 109, 126. Air China, which also relied heavily upon the same type of aircraft in its U.S.-China operations, utilized each of its 747-400s only slightly more than nine hours each day. Id. at 60. China Eastern, which used Boeing MD-11's on its U.S.-China flights, operated these aircraft an average of 9.4 hours each day, while China Southern used each of its Boeing 777's, the mainstay of its international operations, an average of only 7.8 hours per day. Id. at 79-80. Modern aircraft, which cost in excess of $100 million each, are among the airlines' most expensive assets. See Semi-Annual Jet AIRCRAFT VALUE Listing, AIRCRAFT VALUE NEWS, Jan. 15, 2001. In recent years, new Boeing 747-400 and 777-200ER aircraft, the mainstays of U.S.-China operations, have commanded average prices of approximately $140 million and $118 million, respectively. Id. The greater the number of hours an airline keeps its aircraft aloft, earning revenue, the fewer it needs to maintain a given operation, thereby creating a more efficient airline.

141. The 1999 amendments permitted each nation's airlines to operate an additional twenty-seven weekly roundtrips, the greatest increase in service allowed by any of the U.S.-China agreements. See 1999 Amendments, supra note 10, at 5 (allowing fifty-four frequencies); cf. U.S.-China 1980 Agreement, supra note 5 (allowing two frequencies).

142. The 1992 amendments allowed the United States and China each to increase their weekly roundtrip flights to twenty-seven, up from the two originally permitted by the 1980 agreement. See 1992 Amendments, supra note 11, at 11; U.S.-China 1980 Agreement, supra note 5, at 15, 28, 40-41.

143. The 1980 agreement called for the United States and China to discuss, within two years, implementation of additional service to be operated by a second airline from each nation. See U.S.-China 1980 Agreement, supra note 5, at 28. The 1992 amendments called for an incremental rise in the number of flights operated by each nation, from eighteen in 1992 to twenty-seven in 1996. See 1992 Amendments, supra note 11, at 11.
States and China also agreed to several smaller changes in their agreement in 1995.

A. Code-Sharing and New Routes

The 1992 amendments authorized Chinese and U.S. airlines to enter into code-sharing arrangements with one another. Under code-sharing arrangements, one airline operates a flight using its aircraft and crew while selling blocks of seats on that flight to a second airline. The second airline, in turn, markets those seats as if it operated the flight itself and lists the flight in its schedules as its own. Code-sharing arrangements help boost traffic in several ways. They prompt participating air carriers to coordinate connecting flight schedules so that passengers can more easily complete a journey requiring a change of aircraft. Code-sharing also simplifies the reservations process because rather than purchasing two separate tickets for each leg of their journey, passengers can buy a single ticket, as though they are taking a trip involving connecting flights on the same airline. Frequent flyers also benefit from code-sharing arrangements, which allow them to earn mileage credit on either airline in the partnership.

To date, three U.S. carriers have formed code-sharing relationships with their Chinese counterparts. In 1998, American Airlines launched a code-sharing arrangement with China Eastern, which operates service between Los Angeles and Beijing, while in 1999, Delta Airlines did the same with China Southern, which flies between Los Angeles and Guangzhou. Northwest Airlines and Air China also began code-share service in October 1998 on one another’s U.S.-China services.

The United States and China revisited their agreement again in 1995. Their negotiations led to expanded code-sharing opportunities (although up to that point, no airlines had taken advantage of them in the U.S.-China market) and authorized Northwest Airlines to inaugurate tri-weekly passenger/cargo combination service between Detroit and Beijing. This non-

144. See 1992 Amendments, supra note 11, at 4. The 1999 amendments permitted the addition of eight additional weekly roundtrip frequencies by each nation’s airlines, effective April 1, 1999, raising the total number of allotted frequencies to thirty-five for each side. 1999 Amendments, supra note 10, at 5. The amendments granted an additional nine frequencies to each side on April 1, 2000, and a final ten additional frequencies on April 1, 2001, thereby allowing each nation to operate a total of fifty-four weekly roundtrip U.S.-China frequencies. Id.
145. Id.
146. Id.
147. Id.
150. Id.; U.S. Officials Encouraging China to Expand Aviation Services, supra note 148, at 4D.
151. Agreement Reached With China Permitting Expanded Air Services, PR NEWSWIRE, Financial News, Dec. 23, 1995. The frequency of this flight was later increased. Id.
stop flight, the first operated by a U.S. carrier between the United States and China, cut several hours from a trip that previously required a change of planes at Tokyo's congested Narita Airport.132 The agreement also permitted China Southern Airlines to operate the first-ever non-stop service between Guangzhou and the United States.153

B. The 1999 Amendments

The most recent amendments to the U.S.-China aviation agreement, signed in April 1999, authorize each nation to operate a maximum of fifty-four weekly roundtrip flights, effective April 1, 2001.154 The 1999 amendments represent a one-hundred percent increase over the previous amendments of 1992, which authorized the United States and China each to operate twenty-seven weekly roundtrips.155 Also, effective April 1, 2001, the 1999 amendments permitted each nation to increase the number of airlines designated to provide U.S.-China service from three to four.156 The 1999 amendments granted the airlines the freedom to operate service from any city of their choice in their respective home countries, while also increasing the number of cities they may serve in the foreign nation.157

Although the 1999 agreement fell short of the United States' desire for an open skies accord, at the same time it may have opened up the aviation trade further than China desired. Whereas four U.S. carriers fought to become the fourth carrier permitted to operate U.S.-China flights,158 no Chinese carriers sought the same opportunity.159 The possibility of a fourth designated Chinese carrier remains unlikely in the near future due to the government's plan to consolidate Chinese airlines into three groups.160 Air China, China Eastern, and China Southern—the flagship airlines that are to head the groups—each offered U.S.-China service prior to the amendments.161 Airline analyst Peter Haribson of the Centre for Asia Pacific Aviation noted at the time, "There is little going on in China over the new slots. They just have other more pressing things on their plate at the moment."162 The Chinese airline industry, with its financial losses of recent years, continued to retrench and consolidate in its effort to achieve long-term profitability, while the U.S. industry sought expansion, especially in potentially lucrative overseas markets. Industry analysts believed that only China Southern was in a position to utilize any of the

152. See id.
153. Id.
154. 1999 Amendments, supra note 10, at 5.
155. Id.; 1992 Amendments, supra note 11, at 11.
156. 1999 Amendments, supra note 10, at 1.
157. Id. at 3–5.
158. U.S. Majors Go to War Over China, WORLD AIRLINE NEWS, Mar. 3, 2000. Delta, American, UPS and Polar Air Cargo were attempting to gain access for the first time. Id.
159. Id.
161. U.S. Majors Go to War Over China, supra note 158.
162. Id.
slots created by the amendments.\textsuperscript{163}

In the United States, American Airlines, Delta Airlines, Polar Air Cargo, and United Parcel Service (UPS) all sought to win the designation as the fourth U.S. airline to serve China.\textsuperscript{164} Each airline presented its case to the DOT, arguing that its plans for new service using the newly created slots would produce the greatest benefits. American Airlines' Chairman Don Carty pitched the benefits of his company's plans to fly non-stop to China from its Chicago hub.\textsuperscript{165} American Airlines' plan would have created same-airline service between eighty U.S. communities and China, he said, noting that, "No other carrier comes close."\textsuperscript{166} Delta Airlines' Chairman Leo Mullin contended that his airline's proposed service between New York City and China would fill a "glaring omission" in the U.S.-China market.\textsuperscript{167} Polar Air Cargo argued that its planned cargo services would serve a greater public interest than the addition of new passenger service.\textsuperscript{168} Citing a need for greater competition in the cargo market, the DOT ultimately awarded the new designation to UPS and granted it six of the final ten slots.\textsuperscript{169} The DOT split the remaining four slots, handing two to United Airlines, and one each to Northwest Airlines and FedEx.\textsuperscript{170}

At approximately the same time, the U.S. and Chinese governments invited American and Delta Airlines to discuss the possibility of "wet-lease" agreements with their respective code-share partners.\textsuperscript{171} Under the proposal, which appears unlikely to come to fruition, China Eastern and China Southern would have leased an aircraft and its crew from American and Delta, respectively.\textsuperscript{172} These flights would operate using slots granted to the Chinese carriers, which they are currently unable to utilize, but the U.S. carriers would use their own aircraft and codes.\textsuperscript{173}

\textsuperscript{163.} Id. During January 2001, China Southern's passenger load factor on its Los Angeles-Guangzhou flight averaged eighty percent, suggesting that it is more likely to grow than other Chinese airlines with lower load factors in the U.S.-China market. See \textit{China Southern} Airlines Reports Strong January 2001; 80% Transpacific PAX Loads Between LAX & Guangzhou; 91% Economy PAX, Bus. Wire, Feb. 6, 2001, LEXIS, News Library.


\textsuperscript{165.} \textit{U.S. Majors Go to War Over China}, supra note 158.

\textsuperscript{166.} Id.

\textsuperscript{167.} Id.

\textsuperscript{168.} Id.

\textsuperscript{169.} U.S.-China Air Services, DOT Order 2001-1-6 (Jan. 5, 2001). In its decision the DOT stated, "[W]e have found that the public interest is best served by affording the public the benefit of another airline service, particularly in the all-cargo market . . . At the same time, we recognized the continuing unmet demand for additional service from the incumbent carriers and the public benefits that would result from expanded service by each of them." Id.

\textsuperscript{170.} Id.

\textsuperscript{171.} DEP'T OF TRANSP., U.S. Transportation Secretary Slater Calls for Liberalization of U.S.-China Aviation Rights, Announces Tentative Decision on New Services, \textit{Fed. Dep't and Agency Documents} (DOT), Nov. 21, 2000 [hereinafter Slater Calls for Liberalization].

\textsuperscript{172.} Id.

\textsuperscript{173.} Id.
C. The Aftermath of September 11

The events of September 11, 2001 dealt a blow of unparalleled proportions to the U.S. airline industry. Following the attacks, U.S. carriers suspended all flight operations for two days due to security concerns. When flights resumed, passenger counts plummeted. This disaster came on the heels of a downturn in the U.S. economy that had already driven most airlines’ bottom lines deep into the red. To prevent the industry’s collapse, the federal government funded a $15 billion bailout consisting of a combination of grants and loans. In the weeks that followed September 11, most carriers pared their workforces, fleets, and flight schedules by twenty percent or more. Even some China flights did not escape the axe. United Airlines announced a temporary suspension of its Chicago-Beijing flight, while Northwest Airlines discontinued its non-stop flight between Detroit and Shanghai, and later, its non-stop flights between Detroit and Beijing.

On the other side of the Pacific Ocean, Chinese airlines also suffered the consequences of September 11. For several days following the attacks, Chinese carriers suspended their U.S. operations as U.S. airspace was off limits to all carriers. When flights resumed, they too experienced diminished passenger counts, and incurred additional costs associated with new security measures, and the increased cost of insurance for their aircraft. In 2001, China’s three flagship carriers sustained a narrow loss of just under $10 million, but industry officials predicted that losses would rise to several hundred million dollars in 2002. Nevertheless, while U.S. carriers pared some China service, Chinese carriers gradually added service. Air China inaugurated tri-weekly non-stop flights between New York City and Beijing beginning in September 2002, using available slots under the existing open skies agreement. During the

175. Id.
176. Id.
177. Id.
178. Id.
180. John Gallagher, NWA to Lay Off 10,000, Cut Late-Night Flights, DETROIT FREE PRESS, Sept. 22, 2001, Business and Financial News. This flight became a connecting route through Narita, Japan. Id. Although no news release is available regarding the discontinuance of Detroit-Beijing flights, several airline reservations systems indicate that Northwest no longer offers such flights. See, e.g., http://www.travelocity.com (last visited Sept. 15, 2002).
182. Id.
same month, China Southern launched tri-weekly cargo flights between Los Angeles and Guangzhou, supplementing its four-time-a-week passenger service on the same route.\textsuperscript{186} And in October, Air China once again boosted service, adding a two-time-a-week cargo flight between Portland, Oregon and Beijing.\textsuperscript{187}

Although Chinese airlines have sustained losses in recent years, they pale in comparison to those suffered by the U.S. airline industry, which in 2001, by a staggering margin, suffered its worst year in history, with collective losses exceeding $7 billion.\textsuperscript{188} United Airlines alone sustained a loss of $2.1 billion, the largest ever incurred by a single carrier, prompting some airline observers to speculate that the company would be forced to seek bankruptcy protection.\textsuperscript{189} As 2002 drew to a close, the outlook for the U.S. airline industry remained bleak, as the Air Transport Association predicted record industry losses of $8 billion for the year.\textsuperscript{190} Although for the wrong reasons, these recent events may have somewhat leveled the playing field on which the U.S. and Chinese airline industries compete.

VI. New Horizons

While the pressure to expand U.S.-China operations may have subsided post-September 11, this situation will likely be temporary. Despite the calamities of 2001, the U.S. airline industry will probably recover and grow along with a rebounding economy. In the long run, demands for expanded service to China are a near certainty. Even though the U.S. airline industry’s short-term situation may be precarious, this is not cause to neglect planning for long-term growth, and the open skies agreements such growth will require.

Furthermore, although events have provided a reminder that the U.S. airline industry is not invincible, the Chinese airlines have begun to show

\textsuperscript{188} Terry Maxon, With Airline Losses at a High, Analyst Suggests Buying Stocks, DALLAS MORNING NEWS, Feb. 11, 2002, at 1D; see also Kristin S. Krause, The Worst, By Far: After Years of Wealth, Major Airlines’ Losses for 2001 to Nearly Double 1992’s Previous Low, TRAFFIC WORLD, Jan. 28, 2002, at 34.
some indications of their own potential. For example, during the first eight months of 2001, Chinese airlines reported that average passenger load factors, or percentage of seats filled, were nearly seventy-five percent on their U.S. flights.\textsuperscript{191} And, despite the industry’s collective financial losses in 2001, Air China posted a slim profit of slightly more than $4 million.\textsuperscript{192} Ongoing consolidation within the Chinese airline industry should boost the long run viability of the remaining carriers. The day may come when the Chinese government has less need to protect its no longer fledgling airline industry from the U.S. behemoths.

Like many prior agreements, dating back to Bermuda I, the 1999 amendments to the U.S.-China bilateral agreement unnecessarily restrict the expansion of international air service. By limiting growth, the agreement does not properly serve the interests of either nation. Evidence strongly indicates that around the world, improved air service promotes economic growth and benefits the communities it serves.\textsuperscript{193} The benefits range from increased passenger traffic and jobs at airports, to increased tourism and long-term job growth as businesses and industry, attracted by the advantages of convenient air service, expand their operations.\textsuperscript{194} Although not all airlines will benefit equally from a shift toward open skies in the U.S.-China market, this alone is not a reason to preserve a hodgepodge of aviation agreements that reflect the needs of a bygone era. Today’s world economy, with its growing reliance on international trade, depends heavily upon the existence of a market-driven airline service.\textsuperscript{195}

A. The U.S. Perspective

Under the current U.S.-China agreement, U.S. interests remain unfulfilled, from a national economic perspective and probably from an airline industry perspective as well. While U.S. airlines would stand to gain from an open skies agreement with China, such an agreement would create some economic uncertainty inherently associated with a transition from a

\textsuperscript{191} China Airlines’ Sept. 11 Costs, supra note 140. Of course, load factors may not provide an accurate reflection of profitability; fares may be too low, and cost structures too high, for a carrier to earn a profit, even while flying at capacity. See id. Information regarding revenue yields and operating costs are very difficult to obtain. Id.

\textsuperscript{192} Top Three Airlines Lose $9.66 Million in 2001, supra note 183.

\textsuperscript{193} For example, the growth of commercial aviation has given rise to a booming worldwide tourism industry, which in the 1990s accounted for more than twelve percent of global consumer spending and $3.5 trillion in combined gross national product. See Vamos-Goldman, supra note 32, at 440. Additionally, commercial aviation provides an essential conduit for the transport of high value goods, which in 1999 made up forty percent of global trade, as measured by value. See Brookings Economist, supra note 29.


\textsuperscript{195} Alan Larson, U.S. State Department Undersecretary and Acting Deputy of the National Economic Council of Economic Affairs, recently commented, “Aviation is a facilitative industry in that it supports the rest of the economy. In many ways, air service and connections lead investment into regions and cities.” China Says Slow, U.S. Pushes Fast Cargo Access, WORLD AIRPORT WK., Nov. 7, 2000, 2000 WL 6771821 [herein-after U.S. Pushes Fast Cargo Access].
regulated environment to an open market. Just as some airlines prospered while others failed in the aftermath of deregulation of the U.S. airline industry, a U.S.-China open skies agreement could also have an impact on airlines' bottom lines. However, despite growth in international markets, the consequences would not be as substantial as the effects of deregulation in the United States because U.S. carriers continue to do most of their business at home. At worst, some U.S. carriers could be forced to withdraw from the U.S.-China market if their operations became consistently unprofitable. However, that appears unlikely, as U.S. carriers still possess a competitive advantage over their Chinese counterparts.

B. The Chinese Perspective

The 1999 amendments also fail to serve the interests of China's economy. Improved air service under an open skies agreement would benefit the Chinese economy, regardless of whether American or Chinese airlines provide the service. However, the impact of an open skies agreement upon Chinese airlines is less certain. Their interests lie in building consistently profitable operations before they compete directly with U.S. carriers. Few, if any, Chinese airlines currently have the desire and capability to utilize the new route created by the 1999 amendments effectively. This could change in the future, but it is not a certainty. One could imagine a scenario under the existing bilateral treaty in which Chinese airlines never attain lasting profitability, yet stay in business with the aid of government subsidies. Even though a government subsidized and controlled airline industry should not preclude an open skies agreement, it is difficult to imagine the Chinese government allowing unfettered competition against its marginal airline industry. A continued protectionist agreement would guarantee the Chinese airlines a place in the U.S.-China market. Apart from that benefit—if it can be called a benefit given that the profitability Chinese airlines'...
U.S.-China operations remains uncertain—it is difficult to imagine that Chinese airlines would gain any advantage from a continued protectionist agreement.

Furthermore, government officials who fear the demise of Chinese airlines under an open skies agreement lack grounds for their belief. Even under an open skies agreement as advocated by the United States, Chinese carriers would retain complete control of the Chinese domestic market. The United States and China prohibit cabotage, a practice in which an airline provides domestic service in a nation other than its home nation.200 The Chicago Convention affirms a nation’s right to outlaw cabotage within its borders.201 Only in emergencies has the United States wavered from its firm opposition to the practice.202 Given this background, it is difficult to imagine the United States demanding, let alone obtaining, cabotage rights in China. On the other hand, it is conceivable that an open skies agreement with China could include beyond rights because most agreements bearing the "open skies" label include such rights. However, even if an agreement included a beyond rights provision, past experience suggests that airlines would seldom utilize these rights.203

The Chinese government should be less concerned with the competitiveness of its airlines in the U.S.-China market, and more concerned with ensuring sufficient aviation links with the rest of the world. Having adequate international air service is more important than which airlines provide that service. Although globetrotting airlines flying their national flags around the world are a source of pride for their homeland governments, the economic benefits associated with free aviation markets, although sometimes less glamorous, are more important. The Chinese government has little to fear under an open skies agreement. Even under the worst of scenarios, Chinese carriers would merely lose out to the U.S. competition on their U.S.-China routes. But even that scenario appears less likely in light of the U.S. airline industry’s ongoing financial distress.

Although individuals with a direct stake in the Chinese airline industry might not win under an open skies agreement, nearly everyone else including tourists, business travelers, and anyone who gains from an

202. Id. at 156-57. In a rare exception to its policy, the U.S. Department of Transportation granted permission to Australia’s Qantas Airlines to transport a shipment of live camels from Honolulu to Los Angeles. Id. The camels had become stranded in Honolulu after another airline ceased operations and no other U.S. carrier was willing to transport the camels. Id.
203. A quick browse through most airlines' flight schedules will confirm this. A notable exception exists in Japan, where United Airlines, Northwest Airlines, and FedEx, exercise fifth-freedom rights to provide onward service to a number of Pacific rim destinations. See Fisher, supra note 84, at 331-33. These fifth-freedom rights were created as part of a restrictive bilateral treaty between the U.S. and Japan, forty years before the first open skies agreements. See id.
expanding economy, will benefit. Service expansion and greater competition would occur among the U.S. carriers which would probably gain the upper hand in the market, as well as a handful of Chinese carriers. This would promote increased traffic and its associated benefits. China's airlines should not be written off any more than the U.S. carriers should. Open skies and the competition associated with that policy could jump-start Chinese airlines, as they learn from, and are forced to adopt, the more efficient practices of their U.S. competitors. Furthermore, China's domestic aviation market will inevitably continue to grow as long as its economy expands. Projections suggest that passenger counts will nearly quadruple during the next decade.\textsuperscript{204} This rising tide will spill over into international markets as well.

C. Mitigating Potential Harm

Although the open skies scenario presented above is not one to fear,\textsuperscript{205} the United States and China could modify it to mitigate many of the short-term negative effects that concern the Chinese carriers, while planting the seeds of long-term opportunity. Specifically, as part of an open skies agreement, China could allow for increased investment in its airline by U.S. carriers. This would give the U.S. a stake in the future success—not failure—of the Chinese airline industry. And even more importantly, close partnerships between U.S. and Chinese carriers achieved through investment would allow the Chinese airlines to draw on U.S. airlines' wealth of experience.

With China's aviation market poised to expand, U.S. carriers would welcome the chance to play a role. Already, three Chinese carriers have entered into extensive code-sharing arrangements with U.S. airlines, and it appears that both sides would welcome the opportunity to establish closer ties.\textsuperscript{206} In negotiations with other nations, the possibility of partnerships among the carriers has spurred serious discussion of open skies agreements. In one notable example, the United States and Great Britain reopened negotiations for a possible open skies agreement after American Airlines and British Airways announced plans to form a partnership, which would have required such an agreement in order to take effect.\textsuperscript{207} Observers noted that the proposed partnership provided the impetus for the renewed, although ultimately unsuccessful, negotiations between the two

\textsuperscript{204} See Asia/Pacific Growth Slows, supra note 109; Fisher, supra note 84, at 328–29.
\textsuperscript{205} Although some airlines may suffer, evidence from deregulation in the United States and open skies agreements forged between the United States and other nations suggests that free market competition generally leads to lower fares and increased traffic. See Postrel, supra note 75, at C2; HISTORICAL AIR TRAFFIC STATISTICS: ANNUAL: 1954-1980, supra note 76; HISTORICAL AIR TRAFFIC STATISTICS: ANNUAL 1981-2000, supra note 28.
\textsuperscript{206} Slater Calls for Liberalization, supra note 171. Recall American Airlines' interest in entering a wet-lease agreement with China Southern Airlines. \textit{Id}.
\textsuperscript{207} Baliles, supra note 6, at 8; Lick, supra note 17, at 1268. The proposed American Airlines-British Airways partnership would have required exemption from U.S. anti-trust laws. \textit{Id}.
Presently, China caps foreign ownership of its airlines at thirty-five percent, although industry observers speculate this could increase to forty-nine percent. Some observers believe foreign capital may be essential in revamping the Chinese airline industry.

D. The Chinese Government’s Need to Retain Control

Another issue underlying the communist Chinese government’s aversion to an open skies agreement may be its fear of losing control of the airline industry. For much of its existence since the 1949 revolution, the Chinese government has retained a tenuous hold on power, and it has taken draconian measures in instances when it has felt threatened, most notably when it crushed the Tiananmen Square demonstrations in 1989. Providing jobs for the population represents yet another form of control, as Chinese leaders fear that the disappearance of government-sponsored jobs could spark civil unrest.

Although such concerns may contribute to the Chinese government’s aversion to letting market forces, even in small measure, chart the course of its airlines, with the possible exception of the international arena, market forces will mandate the continued existence of Chinese airlines. Many economists have made the very strong argument that, unlike other industries, a functional airline industry is an essential prerequisite for a prosperous economy. Goods, people, and commerce all depend on the ability to travel quickly and at an affordable cost between locations. Therefore, any job losses the Chinese airline industry experiences as the result of an open skies agreement would necessarily be confined to the realm of its international operations, which are a very small portion of Chinese airlines’ overall business. No foreign carriers have sounded the call for access to Chinese domestic markets, and the possibility of this occurring in the foreseeable future appears remote. Under a worst-case scenario,

208. Lick, supra note 17, at 1268.
209. Thomas, supra note 120, at 49.
210. Id.
211. See Henry Chu, Chinese Rulers Fear Angry Workers May Finally Unite; Labor: Ten Years After Tiananmen Square Crackdown, Unemployment, not Lack of Democracy, Fuels Discontent, L.A. TIMES, June 4, 1999, at A1, A23. Some commentators say the demonstrations were fueled in part by labor concerns. Id.
212. Id. China’s Vice President Hu Jintao recently delivered a message to Chinese workers: “Without stability, nothing can be achieved, and successes already attained will be lost . . . . Workers must wholeheartedly cherish the nation’s political stability and unity.” Id.
213. Alan Larson recently stated, “The new economy is also creating very important new types of demands on air transport, where there is a more logistical focus on a just-in-time basis. To benefit from this you need to have a flexible and rapid air transport system.” U.S. Pushes Fast Cargo Access, supra note 195.
214. Chinese airlines continue to generate most of their traffic in domestic markets. See, e.g., IATA: World Air Transport Statistics, supra note 140. For example, in 1998, China Southern Airlines, China’s largest carrier, transported 13.6 million passengers and 236,289 tons of cargo in domestic markets, while carrying 888,682 passengers and 19,554 tons of cargo in international markets. These statistics are representative of the Chinese airline industry as a whole. Id. at 69, 79–80.
even if Chinese airlines find themselves unable to compete against an onslaught of U.S. airline competition in the U.S.-China market, they will continue to fulfill an essential, and increasingly substantial niche in the Chinese domestic market.

E. Looking Ahead

The message emanating from Beijing is that an open skies agreement with the United States may one day occur, but only when China and its airlines are ready. Right now, government officials correctly point out, the two airline industries remain unequal. However, this does not justify China's reluctance to enter into an open skies agreement. The airline industries of each nation may never be equal. An open skies agreement, however, may provide the necessary impetus for Chinese airlines to catch up with the competition.

In the near future, amending the 1999 U.S.-China aviation accord may not be a high priority. The U.S. economy has soured, and several of its carriers, including United, are teetering on the edge of bankruptcy. Meanwhile, the Chinese airline industry appears to be taking small steps toward self-sufficiency, although it still faces the turbulence associated with government-imposed consolidation. Ultimately, the U.S. airline industry are likely to rebound along with the nation's economy, and Chinese carriers may become a force to be reckoned with. Perhaps it should come as little surprise, then, that in early 2002, the Chinese government, pending consultation with its own carriers, expressed an interest in further formal negotiations with the United States aimed at amending the 1999 agreement. Indicative of a continued protectionist attitude, however, the Chinese government announced that it would not consider the possibility of allowing U.S. carriers to utilize unused route authorities allocated to Chinese airlines.

Conclusion

Little more than a decade ago, before the inauguration of the world's first open skies agreements, one could have argued that restrictive bilateral aviation agreements would have minimal detrimental effect upon the nations party to them. All nations with international air service subscribed to some form of such an agreement. In essence, all nations stood on equal footing with one another, and operated under similar sets of rules, almost all of which limited international air service. But today, an ever-expanding number of nations have adopted a new set of rules under the guise of open skies agreements. Evidence, in the form of rising air traffic and lower fares in open skies markets, suggests that the agreements have largely been a success, certainly for the traveling public if not for all airlines.

216. Id. This is called zombie code sharing. Id.
Nations that forge open skies agreements will benefit just as certainly as those nations that fail to enter such agreements will not benefit. Despite recent events, the world’s airline industry will continue to expand and in doing so will follow the path of least resistance. Airlines will readily fly where they are free to come and go as they wish. They will avoid markets they can enter only as the result of an arduous and politically charged negotiation process. Where airlines fly, trade and economic growth will follow. Where they do not fly, economic development will suffer.

The U.S. government must continue to pressure China’s leaders to abandon their protectionist position with regard to their airline industry. While Chinese airlines may incur some short-term pain as the result of an open skies agreement, the long-term benefits are much greater and cannot be ignored. An open skies agreement and the improved air service that accompanies it will facilitate trade and commerce, to the benefit of both nations. The earlier that the United States and China sign an open skies agreement, the sooner they will be able to enjoy its fruits.