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Speech

INTERNATIONAL AVIATION PRIORITIES

Remarks of
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It is a pleasure to be here in Phoenix after too long a hiatus. The Annual Phoenix Sky Harbor Aviation Symposium has emerged over the years as one of the most important gatherings for the aviation community, and it is therefore a privilege to be able to speak to you today.

I would like to take a few moments to discuss some big issues from the perspective of the U.S. Department of Transportation: where we believe international aviation is headed, and where we believe it *should* be headed.

I would like to begin by bringing you greetings from Secretary Mineta. Under the Secretary's leadership, we are working on a variety of important international aviation matters.

Safety

Everyone knows that the promotion of safety is DOT's top aviation priority, but not many are aware of some of the important steps we are taking to enhance the quality of safety management around the world. For example, Secretary Mineta recently returned from a highly successful trip to four East and South Asian nations. In India, he announced an aviation cooperation program that will assist India in modernizing its aviation infrastructure and accommodating traffic growth. The program will utilize both public and private sector aid to support initiatives such as technical assistance, job training, and personnel exchanges between the U.S. and Indian governments.

With the help of a number of private sector partners, we have launched a similar program with China and hope to do the same elsewhere. We pursue these programs because we know that, no matter how many headlines new international services generate, those services will not succeed unless passengers and shippers can rely on the carriers, airports, and the air traffic control systems of multiple nations to function safely. It is very much in the interests of the United States to work with our partners to meet those expectations.

Also in the international safety arena, we are working with our Canadian, Mexican, and European partners on an exciting initiative that concerns fractional ownership operations. Private operations using fractionally-owned aircraft are common in U.S. aviation, and our regulations accommodate those operations without compromising safety. As international fractional operations proliferate, however, they confront differing regulatory treatment from different aviation agencies. We have responded by seeking to develop a common regulatory approach that could govern fractionals more consistently when they operate internationally. In this way, we hope to make certain that this increasingly popular form of international aviation can grow, without sacrificing vigorous and effective safety oversight in the process.

As we take these steps forward in international aviation, we should also endeavor to avoid taking any steps back. Last month, French President Jacques Chirac reportedly proposed an international airline fuel and ticket tax, the proceeds of which would be used to provide development aid to the nations of Africa. It will come as no surprise that many in the aviation community oppose this tax, and for very good reasons. Today, fuel costs are second only to labor costs when it comes to overall industry expenses, and an international fuel tax will drive up industry costs even more, at a time when airlines have found it impossible to pass such increases along to their customers. Major international airlines – ours and Europe's included – are more reliant than ever on their international operations, and therefore less equipped to absorb a new international tax earmarked for causes that, however worthy, will not assist in building aviation infrastructure and ensuring aviation's continued contribution to global economic health.

System Capacity

I would be remiss if, at a conference hosted by a major U.S. airport, I did not talk about system capacity and congestion. Of course, airport congestion knows no distinction between domestic and international flights – it fouls up all of them. And, with 2.3 billion passengers expected to fly annually by 2010, things will not improve if we sit by and do nothing. That is why the Administration has embarked on a dual-track program to expand and upgrade our airport capacity. First, through its Operational Evolution Plan, the FAA has identified airports around the nation that will have trouble accommodating demand in the coming years. We are working with these airports to address their near-term operational and safety issues. Through these efforts and steadily improving technology, we are making significant progress in adding capacity to the system in the near term.

Yet, looking down the road, we will still face a deficit in capacity, unless we take bolder action. By 2025, we expect demand to be three times what it is today. This problem threatens more than the smooth functioning of the system; it represents a major potential impediment to our economic health as a nation.

To respond to this challenge, Secretary Mineta in January 2004 announced his historic Next Generation Air Transportation System initiative. The initiative is designed to increase system efficiency and capacity to keep pace with projected demand. The plan calls for a tripling of system capacity over the next two decades, along with measurable improvements in security, situational awareness, and other areas. The Next Generation effort is being led by a Joint Planning and Development Office, or JPDO, a multi-agency office housed in the FAA that has surveyed the private sector, government agencies, and the academy for the best ideas about how to meet the objectives established by the Secretary for the new system. In December 2004, the JPDO delivered to Congress a national plan that makes detailed recommendations about the new system. But this is not another blue-ribbon panel, whose recommendations sit on the shelf gathering dust. We want to effect real change. So, with the JPDO's continuing help, we are building on the national plan to see what it will take to begin putting those recommendations into place.

International Aviation Liberalization

So we have been quite active. But it is in air services liberalization where we have been perhaps the busiest, and most successful. During his recent Asian trip, Secretary Mineta signed an open skies agreement with India, an agreement that has already spawned newly proposed services between our two countries. One U.S. airline has already announced its intention to launch daily nonstop service between the U.S. and India, which, if approved, would be the first such service in many years. During the same trip, Secretary Mineta reached agreement with leaders in Thailand and Hong Kong to renew bilateral negotiations intended to seek out a basis for further liberalization in those markets as well. The Hong Kong talks began in Washington this week.

The Secretary's Asian trip reminds us that the Open Skies model remains the keystone of U.S. international aviation policy. Indeed, the Bush Administration has entered into 13 open skies agreements with nations across the world in the past four years. In July 2004, we reached an agreement with China that, once fully phased in by 2010, will provide for a nearly five-fold increase in weekly flights between our countries over the next six years, to a total of 249 weekly flights. Although we hope that the Chinese will embrace a more thoroughgoing liberalization of the U.S.-China relationship soon, the 2004 protocol is a major step forward. That agreement, coupled with the Open Skies agreements that we have concluded with India and – also in July 2004 – with Indonesia, extends liberalized aviation regimes to 2.6 billion people.

The global economy is only as successful as the transportation networks that support it, and international aviation plays a critical role in making that economy work. Proof of this abounds. Although more cargo is shipped by sea or by surface transport than by air, fully 40% of global exports, by value, are shipped via aircraft. We have estimated that a single new daily B-777 roundtrip between the U.S. and China will produce a $158 million total annual benefit to the U.S. economy.

Not surprisingly, therefore, we are continuing to look for opportunities to build on the Administration's record. For starters, we are engaged with our aviation partners in this hemisphere in an effort to produce similar results. We have had a number of informal, high-level conversations with our counterparts in Mexico, and I look forward to doing so again soon. As many of you know all too well, our bilateral agreement with Mexico still contains restrictions on airline entry, designation, and codesharing. We are hopeful that we can modify that agreement to bring it more into line with the close and comprehensive relationship that we have with Mexico. We have also engaged with Canada, especially since Prime Minister Martin's election some months ago. Although we have yet to reach new agreements with either nation, we continue to look for opportunities to roll back restrictions on international service with our closest neighbors.

U.S.-EU Aviation Relations

In the on-deck circle, of course, is the European Union. The U.S. and the EU both seek a new, comprehensive agreement that would fully liberalize air services between the United States and the 25 nations of the newly-expanded EU. An agreement of that kind would bring nearly 750 million people and many of the world's great airlines together under a single liberalized regime.

As everyone here surely knows, the U.S. and the EU Commission, after several meetings, agreed to a package last June that the negotiators on both sides felt would represent a major step forward in bringing about a fully liberalized common aviation area across the Atlantic. The EU Council of Ministers rejected the package, and so we are now consulting with the Commission on the parameters and timing of a renewed effort to bring the two sides together.

There has been no dearth of press coverage of the U.S.-EU aviation relationship over the past year, and lots of discussion in conferences like this. Frankly, I find much of what I've read and heard unsatisfying. I want to take a few moments, therefore, to discuss this most important of aviation relationships and to offer an American perspective on where we are headed.

Consider, first, two different trans-Atlantic aviation route maps as they appear today. You don't need to look at real maps to follow what I want to say; just use your imagination. The first map shows – with lines connecting every conceivable trans-Atlantic city pair -- all of the opportunities currently available to every U.S. airline wishing to fly to Europe. Basically, every U.S. airline today is able to connect any point in the vast landmass of the United States with any point in the vast landmass of Europe. There are some famously anachronistic restrictions at London's Heathrow Airport and some other less important exceptions, but it's still pretty difficult to see the outlines of the continents under the dense tangle of available routes on this first map – the opportunities available to U.S. carriers.

The second map looks very different. It shows the trans-Atlantic city pairs currently available to EU carriers. Instead of the dense tangle of routes we saw on the first map, this map shows a separate spray of routes coming out of each EU country to the United States. The airlines of each of our many EU Open Skies partners are certainly allowed to fly to and from any city in the U.S., but all those flights must funnel in and out of their individual home countries. At the present time, in other words, *no* EU carrier has the ability under the current bilateral agreements to do what *every* U.S. carrier can do: connect any point in the U.S. to any point in Europe.

The reason for this disparity in respective opportunities, of course, is the famous nationality clause that appears in every bilateral agreement – even in Open Skies agreements. To operate services under one of those agreements, an airline must be owned and controlled by citizens of one of the two contracting parties. By severely restricting the scope of every EU airline's operations, the clause prevents EU carriers from competing with each other in trans-Atlantic O&D markets. It also impedes consolidation among EU airlines. If one EU airline acquires another from a different EU member state, the acquired airline is no longer owned and controlled by citizens of its home country, and so it potentially loses its ability to operate to the U.S. – and most likely to other countries – from its home territory.

When the European Court of Justice ruled on the Commission's lawsuit against a number of EU Open Skies countries in late 2002, it said that the nationality clause was inconsistent with the Treaty of Rome and called upon the Member States in question to get it out of their bilateral agreements

That decision, of course, was the most important factor in bringing U.S. and EU negotiators together to begin discussing a different model for trans-Atlantic air services. I remember saying at the time that these talks would not be "negotiations" in the traditional sense because the two sides represented markets comparable in importance, represented airline industries comparable in size, and most importantly shared a common vision of what the trans-Atlantic air services market should be.

The largest and most important specific objective of the talks was the Commission's need to eliminate the nationality clause from the framework for air services between the EU and the U.S. Concomitantly, the largest immediate *concession* sought during the talks was from the U.S. – a request that it give up the nationality clause and accept for the first time the concept of an "EU carrier." Understand the importance of that concession: Once made, U.S. airlines would face competition not just from Lufthansa at Frankfurt, not just from Alitalia at Milan, not just Air France at Paris, not just from KLM at Amsterdam, but potentially from any and all EU carriers at every EU city. Every EU-U.S. city pair market heretofore limited to one or two EU national carriers by the operation of the nationality clause would henceforth be open to *all* EU carriers. For the first time, in other words, those two aviation maps would look exactly the same.

I had said that it wouldn't be a negotiation in the traditional sense. Consistent with that assessment, the U.S. delegation declared at the outset of the talks that it would accept the concept of the EU carrier as part of a satisfactory agreement – by which we meant nothing more than an agreement in which the U.S. achieved its Open Skies objectives with those EU member states that hadn't already joined the Open Skies club bilaterally.

And that brings me to a point that I believe has been largely overlooked from the outset: That concession by the United States – a willingness to treat all EU airlines as eligible to fly to the U.S. from anywhere in the EU, accepting far more competition from EU airlines in every market served by U.S. carriers than is possible under the existing arrangements, facilitating a likely strengthening of EU carriers through consolidation – that concession was *the single most important concession ever made in the history of air services negotiations*. And yet it was barely discussed across the table. The U.S. simply treated it as a given; it *would* be part of any agreement with the EU. The Commission achieved its most important mission on Day One without breaking a sweat. They had us at hello.

Then something curious happened: The most transformational success in the history of international aviation negotiations was quietly pocketed by our Commission counterparts and never spoken of again. From that point onward, all the world knew was that the U.S. and the EU were locked in a struggle over cabotage and the right of establishment. Some reward for acceding to the Commission's most important requirement up front! Suddenly the U.S. – pioneer of deregulation, the world's foremost champion of aviation liberalization everywhere for more than a quarter of a century -- was being characterized as a protectionist holdout.

By June of last year, as I mentioned, the two delegations did reach agreement on a package they characterized as a first phase accord. It would have facilitated a dramatic reshaping of the European airline industry and a major ramping up of convenient, competitive air services between the two continents. It would have been good for airlines –especially EU airlines—and good for consumers. And it would have paved the way for further talks in the future and the prospect of even more liberalization. As I said, the Council of Ministers rejected the package.

What's Next?

We haven't given up. Our negotiators have stayed in touch, and Secretary Mineta recently met with the new European Commission Vice President and Transport Commissioner, Jacques Barrot, in the hope of getting the talks back on track. I believe we can do so. But it is important that we remain focused on what can be achieved in the near term. More specifically, we need to engage more productively on the value of the changes that we can bring about through the exercise of our respective existing legal authorities. The old line about the perfect being the enemy of the good was never more apt than in this context.

Let me talk directly about the issue that still has the potential to keep us from enjoying the fruits of a revolutionary new U.S.-EU agreement – foreign ownership and the right of establishment.

For all the success that our Open Skies policy has wrought, it does not address ownership and control. Today, in major industries, capital flows freely across national borders so that competitors can establish a truly global brand presence, exploit economies of scope and scale, respond to customer demand and tap market opportunities wherever they arise. It's a simple proposition, and one that applies even in industries long thought essential to the nation's national and economic security, such as financial services, automobiles, telecommunications, information technology, steel, and pharmaceuticals.

The one industry in which capital is *not* allowed to flow freely across national boundaries, ironically, is the very industry that has facilitated the globalization of all the others – commercial aviation. Yes, in 2005, federal law continues to place severe restrictions on the amount of foreign investment a U.S. airline may accept without putting its certificate in jeopardy. As I'm sure everyone here knows, not more than 25 percent of the voting shares of a U.S. airline can be owned by foreign citizens, and the law prohibits any semblance of foreign control over a U.S. airline, even where foreign-held equity is under the statutory ceiling.

It does not seem radical in 2005 to suggest that it is time to reconsider the justification for a law that restricts U.S. airlines' access to the global capital marketplace. If the restriction were removed both here and abroad, our airlines would be able to consolidate services and connections and build truly global networks. They might well enhance their efficiency and expand their geographic scope. They would exploit more effectively the global branding strategy that has proven so successful in other worldwide industries. And, without doubt, they could respond more aggressively to new opportunities in domestic and international markets. It is not surprising that forward-looking leaders within the industry – like United Chairman Glenn Tilton – are beginning to call for what they characterize as a long overdue change in the law.

This is a big issue for the future of aviation, and it is one that undoubtedly will be the subject of serious deliberations within our Congress when the time comes. My point today is that it is simply unrealistic to think that the time for that deliberation will be driven by our consultations with the EU Commission. First, there is always a lot on Congress's plate, and it is uncertain how quickly the subject would be taken up even if it were directly raised by the Administration. Even if it were taken up promptly, the deliberations would be long and difficult and the outcome highly uncertain. However much importance the U.S. Government attaches to the value of a new civil aviation agreement with the EU – and that's a lot – decisions on U.S. law regarding inward investment will necessarily be predicated on domestic considerations.

We should not allow the pace of those internal deliberations to compromise the prospects for a U.S.-EU agreement that – even without a right-of-establishment clause – has the potential to transform the trans-Atlantic aviation market in fundamental ways. It would be an historic achievement, and I believe it would quickly become a template for the rest of the world to follow.

Whatever happens on the EU front, you may rest assured that we will continue to seek liberalized agreements wherever we can find them – and will continue to engage our allies on aviation matters large and small. We will continue to plan for the future of aviation, and, of course, we will continue to insist that the safety of that system remains second to none.

Thank you for listening. I look forward to your questions.

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