THE BELGIUM-IRELAND AIR TRANSPORT AGREEMENT ARBITRATION

by

Alfred L. MERCKX*
Licentiaat in de Rechten (Leuven)
LL.M., D.C.L. Cand (Mc Gill)
Research Assistant, Mc Gill University, Montreal

The Arbitral Award in the air transport dispute between Belgium and Ireland, given at Dublin on July 17th, 1981 by *sole* arbitrator H. Winberg, is somewhat different from the few existing arbitrations in this field (1). The issue at stake was a capacity dispute between Belgium and Ireland on the Brussels-Dublin route (2). Rendered by a *sole* arbitrator as the result of a

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(1) For the text of the award, see *appendix II* and also Naveau, J., *Away from Bermuda? An Arbitration Verdict on Capacity Clauses in the Belgium/Ireland Air Transport Agreement,* 8 AIR LAW at 50 *et seq.* (1983). For the text of previous arbitral awards dealing with disputes under bilateral air transport agreements, see *Decision of the Arbitration Tribunal Established Pursuant to the Arbitration Agreement signed at Paris on January 22, 1963 between the United States of America and France, decided at Geneva on December 22, 1963,* III I.L.M. at 668 *et seq.* (1964); *Italy-U.S. Air Transport Arbitration: Advisory Opinion of Tribunal (Given at Geneva,* July 17, 1965), IV I.L.M., at 974 *et seq.* (1965); *Case Concerning the Air Services Agreement of 27 March 1946 (United States v. France),* 54 I.L.R. at 304 *et seq.* (1979). See further Bradley, M.A., *International Air Cargo Services: The Italy-U.S.A. Air Transport Agreement Arbitration,* 12 McGILL LAW JOURNAL at 312 *et seq.* (1966); Cot, J.-P., *Interprétation de l'accord franco-américain relatif au transport aérien international,* 10 A.F.D.I. at 352 *et seq.* (1964); Damrosch, L.F., *Retaliation or Arbitration - or Both? The 1978 United States-France Aviation Dispute,* 74 A.J.I.L. at 785 *et seq.* (1980); de Visscher, C., *L'interprétation de l'accord aérien France-Etats-Unis du 27 mars 1964. Sentence arbitrale du 22 décembre 1963,* 1 R.B.D.I. at 1 *et seq.* (1966); Dutheil de la Rochère, J., *L'interprétation de l'accord franco-américain relatif au transport aérien international. Changement d'appareil à Londres. Sentence du 9 décembre 1978,* 25 A.F.D.I. at 314 *et seq.* (1979); Larsen, P.B., *Arbitration of the U.S.-France Air Traffic Rights Dispute,* 30 J.A.L.C. at 231 *et seq.* (1964); Metzger, S., *Treaty Interpretation and the United States-Italy Air Transport Arbitration,* 61 A.J.I.L. at 1007 *et seq.* (1967); Monaco, R., *Etats-Unis et Italie. Interprétation de l'accord aérien du 6 février 1948. Avis consultatif du tribunal arbitral constitué par le compromis du 30 juin 1964 émis le 17 juillet 1965,* 72 R.G.D.I.P. at 461 *et seq.* (1968).

(2). In relation to a specified air route, the term «capacity» refers to the total number of seats and, or cargo space carriers operating on that route can offer to the public during a parti-

quick and unique procedure, the decision is highly practical and economic in nature. It highlights some questions of public international air law which have so far received little attention such as the recourse to analogy in the interpretation of bilateral air transport agreements and the legal relationship between bilateral air transport agreements and inter-carrier agreements. Finally, the decision is worthwhile to situate in the context of the present EEC regulatory proposals in the air transport field.

I. THE DISPUTE

The operation of scheduled air services between Belgium and Ireland is governed by the bilateral air transport agreement concluded in 1955 between the countries (3). The two governments mutually exchanged third, fourth and fifth freedom traffic rights in passengers, mail and cargo for their respective designated national air carriers (4). SABENA Belgian World Airlines,

cular period (usually a week) as a result of the payload (total number of seats and, or cargo space) of the aircraft (aircraft capacity) flown on the route and the number of flights (frequency) during that period. In order to operate economically a certain percentage of aircraft capacity must be sold. This percentage called a «reasonable load factor» is generally assumed to be around 60%. The unsold capacity below this percentage can be defined as «overcapacity». In other words overcapacity can be cut through adjusting the aircraft type or number of flights without the carrier losing actual traffic, see Cheng, B., *The Law of International Air Transport,* London, Stevens at 411-412 (1962); Naveau, J., *Droit du transport aérien international,* Bruxelles, Bruylant at 97 *et seq.* (1980); O'Connor, W., *An Introduction to Airline Economics,* New York, London, Praeger Publishers at 41 (1978); Wassenbergh, H., *Public International Air Transportation Law in a New era,* Deventer, Kluwer at 31 (1976). As the present dispute deals only with scheduled international air services, the capacity regulation of non-scheduled international air services will be left out of the further discussion. On the distinction between scheduled and non-scheduled air services, see Matte, N., *Traité de droit aérien-aéronautique,* Paris, Pedone at 148 *et seq.* (1980); Merckx, A., *New Trends in the International Bilateral Regulation of Air Transport,* 17 E.T.L. at 138 (1982).

(3) *Air Transport Agreement between the Government of Belgium and the Government of Ireland,* signed at Brussels the 10th September 1955 CATC (55) 197, *hereinafter* cited as the Bilateral Agreement. See also *Exchange of Notes betweeen the Government of Ireland and the Government of Belgium modifying the Annex to the Air Transport Agreement of 10th September 1955, Dublin, 16th December 1957,* CATC *(55) 197A.* On bilateral air transport agreements in general, see Haanappel, P., *Bilateral Air Transport Agreements - 1913-1980,* 5 THE INTERNATIONAL TRADE LAW JOURNAL at 241 *et seq.* (1980).

(4) The first two «technical freedoms of the air», i.e. the right of over-flight and technical stops were exchanged on a multilateral basis in the *International Air Services Transit Agreement* to which both Belgium and Ireland are parties. (See ICAO Doc. 7500). The so-called «commercial freedoms of the air» are exchanged on a bilateral basis. The «third freedom» is the right to pick up traffic in the home State of the carrier destined for foreign States on the route. The «fourth freedom» is the right to pick up traffic in a foreign State on the route destined for the home State of the carrier. The «fifth freedom» is the right to carry traffic in both directions between foreign States on the route. For a detailed analysis of the «freedoms of the air», see Cheng, B., *op cit.,* note 2 above, at 9 *et seq.;* Guillot, J., *L'économie du transport aérien. Libertés de l'air et échanges de droits commerciaux,* Bibliothèque de droit maritime, fluvial, aérien et spatial, Tome XVI, Paris, Librairie générale de droit et de jurisprudence at 17 *et seq.* (1970); Haanappel, P., *Pricing and Capacity Determination in International Air Transport. A Legal Analysis,* Deventer, Kluwer at 10 *et seq.* (1984).

as designated carrier of the Belgian Government, obtained traffic rights between Brussels and Dublin in both directions and between Brussels via intermediate points to Shannon and beyond, in both directions (5). Air Lingus Irish Airlines, as designated carrier of the Irish Government, was granted traffic rights between Dublin and Brussels in both directions on the one hand and between Dublin-Manchester-Brussels-Dusseldorf and/or Frankfurt in both directions on the other (6).

The regulation of capacity in the *Bilateral Agreement* can be found in Article VIII coupled with Article XI(1):

> «Article VIII
>
> 1) The capacity offered by the airlines of the contracting parties operating agreed services shall be adapted to traffic requirements.
>
> 2) On common routes the airlines of the contracting parties shall take into consideration their mutual interests so as not to affect unduly their respective services».
>
> «Article XI
>
> 1) In a spirit of close collaboration, the competent aeronautical authorities of the contracting parties shall consult each other from time to time with a view to ensuring the application of the principles defined in this Agreement and in the Annex thereto and their satisfactory execution».

Article VIII is a very rudimentary *Bermuda I* type capacity clause leaving the designated carriers the freedom to determine the actual capacity, subject to a periodical *ex post facto* review by both governments (Art. XI (1)) (7).

(5) See *Bilateral Agreement,* Annex II, Table I.

(6) *Ibidem,* Annex II, Table II.

(7) *Bermuda I* type capacity clauses go back to the *Air Services Agreement between the Government of the United States of America and the Government of the United Kingdom of Great Britain and Northern Ireland,* February 11, 1946, TIAS 1507, *hereinafter* cited as Bermuda I Agreement. The Capacity Principles of this agreement are stated in Para. 3 to 6 of the *Final Act of the Civil Aviation Conference held at Bermuda,* January 15 - February 11, 1946, TIAS 1507. We will *hereinafter* refer to these principles as the Bermuda I Capacity Principles. The representatives of the two Governments in Conference resolve and agree as follows:

> «(3) That the air transport facilities available to the travelling public should bear a close relationship to the requirements of the public for such transport.
>
> (4) That there should be a fair and equal opportunity for the carriers of the two nations to operate on any route between their respective territories (as defined in the Agreement) covered by the Agreement and its annex.
>
> (5) That in the operation by the air carriers of either Government of the trunk services described in the Annex to the Agreement, 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 routes.
>
> (6) That is the understanding of both Governments that services provided by a designated air carrier under the Agreement and its Annex shall retain as their primary objective the provision of capacity adequate to the traffic demands between the country of which such air carrier is a national and the country of ultimate destination of the traffic. The right to embark or disembark on such services international traffic destined for and coming from third countries at a point or points specified in the Annex to the Agreement shall be applied in accordance with the general prin-

Upon the conclusion of the *Bilateral Agreement,* both countries also exchanged a Confidential Memorandum of Understanding relating to the agreement which determined *inter alia* that the exercise of certain fifth freedom traffic rights were subject to the conclusion of a pooling agreement between the designated airlines (8).

ciples of orderly development to which both Governments subscribe and shall be subject to the general principle that capacity should be related:

(a) to traffic requirements between the country of origin and the countries of destination;

(b) to the requirements of through airline operation; and

(c) to the traffic requirements of the area through which the airline passes after taking account of local and regional services».

On the *Bermuda I Agreement* in general and the *Bermuda I Capacity Principles* in particular, see Baker, G., *The Bermuda Plan as the Basis for a Multilateral Agreement,* Lecture delivered at McGill Univ., Montreal, April 18, 1947, reprinted in Vlasic and Bradley, *The Public International Law of Air Transport, Materials and Documents,* Vol. I, McGill Univ., Montreal at 245 *et seq.;* (1974); Cheng, B., *,op cit.,* note 2 above at 412 *et seq.;* Cooper, J., *The Bermuda Plan: World Pattern for Air Transport,* in *Explorations in Aerospace Law. Selected Essays by John Cooper,* Ed. by I.A. Vlasic, McGill Univ. Press, Montreal at 381 *et seq.* (1968); Haanappel, P., *op. cit.,* note 4 above, at 32 *et seq.;* Lowenfeld, A., *The Future Determines the Past: Bermuda I in the Light of Bermuda II,* 2 AIR LAW at 2 *et seq.* (1978); Matte, N., *op cit.,* note 2 above, at 230 *et seq.;* McCaroll, J.C., *The Bermuda Capacity Clauses in the Jet Age,* 29 J.A.L.C. at 115 *et seq.* (1963); van der Tuuk Adriani, P., *The Bermuda Capacity Clauses,* 22 J.A.L.C. at 406 *et seq.* (1955).

The opposite of the *Bermuda I* type of capacity regulation is predetermination. Predetermination consists of *prior* governmental approval or determination of the route capacity and sometimes also of frequency, schedules and aircraft type to be used, see Haanappel, P., *op. cit.,* note 4 above, at 35-36. Predetermination can take various forms. The total route capacity and the way it has to be shared between the designated carriers can be determined in the agreement (see *e.g.* Articles 8 and 9 of the *Agreement between the Government of Belgium and the Government of the Union of South Africa in regard to Air Services,* Pretoria, June 11, 1958, CATC (58) (189). The bilateral air transport agreement can also contain the *Bermuda I Capacity Principles* subject to prior governmental approval of the actual capacity or the agreement can contain an agreed sharing formula (*e.g.* 50/50 division of route capacity) subject to prior governmental approval. In the last two cases predetermination can also be obtained by laying down an obligation on the carriers to conclude a capacity agreement which has to be approved by both governments. Sometimes even a pooling agreement can be required or permitted. The latter can be defined as a contract *sui generis* between airlines for the operation of some or all of their services on a common route according to a capacity share between the two carriers. The contract always provides a formula for the allocation of revenues and sometimes of the expenditures resulting from such operations, see Cheng, B., *op. cit.,* note 2 above, at 278 *et seq.;* Dutoit, B., *La collaboration entre compagnies aériennes. Ses formes juridiques. Etude de droit international,* Lausanne, Nouvelle bibliothèque de droit et de jurisprudence, at 131 *et seq.* (1957); Naveau, J., *Les accords de pool entre les entreprises de transport aérien,* 6 E.T.L. at 198 *et seq.* (1971).

A more recent method of capacity regulation has been introduced in the so-called «liberal» bilateral air transport agreements recently concluded by the USA with a number of countries including Belgium, Germany and the Netherlands. This method relies upon competitive responses of carriers to market forces and on abrogation of direct governmental control, see Haanappel, P., *op. cit.,* note 4 above, at 143 *et seq.;* Merckx, A., *op. cit.,* note 2 above, at 123 *et seq.*

(8) See *infra,* text to notes 28 and 29. The capacity clause of the *Bilateral Agreement* does not contain the classical restriction on fifth freedom traffic rights found in the *Bermuda I Capacity Principles,* see *supra,* note 7.

Until the summer of 1979 only Air Lingus operated between Dublin and Brussels. Beginning in the summer of 1979 Air Lingus terminated its fifth freedom operations between Brussels and points in Germany. At the same time SABENA resumed its operations on the Brussels-Dublin route pursuant to the conclusion of a pooling agreement with Air Lingus.

Soon after the Belgian national carrier resumed its service it became apparent that both airlines, but especially SABENA, were operating at abnormally low and economically unjustified load factors (28 % during the summer months, 19 % during the winter months). SABENA held the view that this situation was not in conformity with the capacity principles of the *Bilateral Agreement* and insisted on a curtailment of capacity. The Belgian national carrier suggested that there be eight flights a week, to be equally divided between the two carriers, instead of eleven flights a week (7 for Air Lingus and 4 for SABENA). As efforts to obtain a solution through direct negotiations, first at an inter-airline and then at an inter-governmental level, failed both governments decided to refer the matter to arbitration.

II. THE PROCEDURE

Article X of the *Bilateral Agreement* lays down the following procedures for the settlement of disputes: (9)

> «1) Any disputes relating to the interpretation and application of this Agreement or the Annex thereto which cannot be settled by direct negotiation shall be submitted to arbitration.
>
> 2) Any such dispute shall be referred for decision to the Council of the International Civil Aviation Organization.
>
> 3) Nevertheless, the contracting parties may, by mutual agreement, settle the dispute by referring it either to an arbitral tribunal or to any other person or body designated by them.
>
> 4) The contracting parties undertake to comply with the decision given».

(9) On bilateral air transport agreements and dispute settlement in general, see Cheng, B, *Dispute Settlement in Bilateral Air Transport Agreements,* in *Settlement of Space Law Disputes. The Present State of the Law and Perspectives of Further Development,* STUDIES IN AIR AND SPACE LAW, Vol. I, Ed. by K.H. Böckstiegel, Köln, Carl Heymanns Verlag K.G. at 97 *et seq.* (1980); Larsen, P., *Arbitration in Bilateral Air Transport Agreements,* ARCHIV FÜR LUFTRECHT at 145 *et seq.* (1964); Wessberge, E., *L'arbitrage et les accords internationaux de transport aérien,* 14 R.G.A. at 3 *et seq.* (1951).

(10) See *Bermuda I Agreement,* Article 9. ICAO (International Civil Aviation Organization) is a specialized UN agency which was set up by the *Convention on International Civil Aviation* signed at Chicago, December 7th, 1944 (ICAO Doc. 7300/5), *hereinafter* cited as the Chicago Convention. The ICAO Council, a political body composed of representatives of States elected by the ICAO Assembly has the power to settle disputes arising under the *Chicago Convention* and its Annexes (Article 84 of the *Chicago Convention)* and under the *International Air Services Transit Agreement* and the *International Air Transport Agreement* (PICAO Doc. 2187) (See Article 66 of the *Chicago Convention).* As the *Chicago Convention* is silent on the subject, the Council's competence to consider disputes arising under bilateral air transport agreements is based on Resolution A1-23 adopted in 1947 by the first ICAO Assembly (See ICAO Doc. 9275).

In the case where a dispute cannot be settled by direct negotiations, the parties are under an obligation («shall») to resort to binding arbitration. As in the *Bermuda I Agreement* the normal procedure allows for direct referal to the ICAO Council with the possible alternative choice of arbitration (10). This contrasts with most other post-war bilaterals which provide for arbitration through an *ad hoc* tribunal before reference to the ICAO machinery. The ICAO machinery only intervenes when the parties cannot agree to an arbitral procedure or on the choice of the arbitrator (11).

Up until now the ICAO Council has never been called upon to decide a dispute arising under a bilateral air transport agreement (12). Even in the three cases where a dispute was submitted to the ICAO Council under Chapter XIII of the *Chicago Convention,* no decision on the merits was ever reached (13).

On the role of the ICAO Council in the settlement of disputes, see Buergenthal, T., *Law-making in the International Civil Aviation Organization,* Syracuse, Syracuse University Press at 123 *et seq.* (1969); Cheng, B., *op. cit.,* note 2 above, at 100 *et seq.;* Mankiewicz, R., *Pouvoir judiciaire du conseil et règlement pour la solution des différends,* 3 A.F.D.I. at 324 *et seq.* (1975); Milde, M., *Dispute Settlement in the Framework of the International Civil Aviation Organization (ICAO),* in *Settlement of Space Law Disputes. The Present State of the Law and Perspectives of Further Development,* STUDIES IN AIR AND SPACE LAW, Vol. I, Ed. by K.H. Böckstiegel, Köln, Carl Heymanns Verlag K.G. at 87 *et seq.* (1980).

(11) Some bilateral air transport agreements provide, in that case, that the dispute be referred directly to the ICAO Council, see *e.g.* Art. 16 of the *Agreement between the Kingdom of Belgium and the Kingdom of Egypt relating to Scheduled Air Transport,* Alexandria, 19th September 1949, CATC (53) 6. Others refer the dispute to «an arbitral tribunal which may be established within ICAO or the ICJ», see *e.g.* Art. 13 of the *Agreement between the Government of the Kingdom of Belgium and the Government of the Kingdom of Iran relating to Air Transport between and beyond their respective Territories,* Teheran, April 14th, 1958, CATC (59) 79. Other bilaterals may contain a provision to call upon the President of the ICAO Council to appoint a President of a tripartite *ad hoc* tribunal in case the other two arbitrators appointed by the Parties cannot come to an agreement, see *e.g.* Art. 15 of the *Agreement between the Government of the Kingdom of Belgium and the Government of the Republic of Kenya for Air Services between and beyond their Respective Territories,* Nairobi, June 14th, 1979, CATC (80) 46.

(12) States are reluctant, in general, to refer disputes under bilateral air transport agreements to arbitration. «In the absence of authoritative statements», writes Prof. Bradley, «one can only surmise the reasons: Both parties lose control of the dispute. There is a danger of an adverse decision which would financially have more adverse results than a compromise. Suspicion exists as to the impartiality of arbitral tribunals. It is better to cut one's losses by compromise rather than suffer the losses from unilateral restrictions during the period - not less than twelve months - that the matter is under arbitration. Perhaps the major reason is that the benefit of a favourable decision may be lost by the losing state giving twelve months notice of termination of the agreement», Bradley. M.A., *op cit.,* note 1 above, at 312, note 5.

Moreover, the ICAO Council is a political body composed of State representatives who do not act in their individual capacity but are instructed by their respective governments. Dispute settlement is also from the primary task of the ICAO Council and its members do not necessarily have any special legal competence, see Sohn, L., *Settlement of Disputes Relating to the Interpretation and Application of Treaties,* 150 RECUEIL DES COURS, II, at 264 (1976); Sohn considers binding dispute settlement by the ICAO Council not as arbitration but as a method of dispute settlement *sui generis, op. cit.,* at 264; and further Cheng, B, *op. cit.,* note 9 above at 109; Milde, M., *op. cit.,* note 10 above at 90.

(13) The first case was brought in 1952 by India against Pakistan alleging a breach of Article 5 (non-scheduled air services) and Article 9 (prohibited zones) of the *Chicago Convention.* This dispute was settled by negotiation between the Parties, see Buergenthal, T., *op. cit.,* note 10

In the present case, the parties obviously availed themselves of the possibility provided by Article X, (3) of the *Bilateral Agreement* which provides for a reference of the dispute «either to an arbitral tribunal or to any other person or body designated by them». As both parties were willing to proceed to arbitration, they agreed on *sole* arbitrator H. Winberg.

Contrary to previous air transport arbitrations no formal *compromis* was signed (14). Instead, each party simultaneously forwarded a letter of similar wording to Mr. Winberg, formally requesting him to act as an arbitrator (15). Although no precise legal questions on the interpretation of the *Bilateral Agreement* were put forward, the terms under which the dispute was submitted to the arbitrator can be stated as follows:

> «1. Is the total number of weekly roundtrip flights operated by Air Lingus and SABENA between Brussels and Dublin too high? (16).
>
> 2. Is a 50/50 division of capacity between Air Lingus and SABENA in conformity with the *Bilateral Agreement?*» (17).

The letters forwarded to the arbitrator contain no provision on the applicable law. As stated by Cheng, «where the *compromis* is silent, the application of international law must be deemed to be the intention of the parties, inasmuch as the parties are international persons, the instrument setting up the tribunal is an international treaty, and the subject matter is one regulated by international law» (18).

The actual procedure proved to be very quick and efficient. The arbitrator met with the airline and governement representatives from both countries. The latter presented oral and written arguments. Both parties also approved a temporary traffic program pending the outcome of the arbitration. Finally, on July 17, 1981, less than two months after the proceedings were initiated, H. Winberg rendered his decision at Dublin.

above, at 137 *et seq.* In 1967 a dispute between the U.K. and Spain concerning a prohibited zone over Gibraltar was also brought before the ICAO Council. In 1969 this case was deferred by the Council *sine die* at the request of the Parties, see Milde, M., *op. cit.*, note 10 above, at 91. In 1971 Pakistan filed a complaint under Article 84 of the *Chicago Convention* and Article II, Sections 1 and 2 of the *International Air Services Transit Agreement* following a suspension by India of flights by Pakistani aircraft over India's territory as the result of a hijacking incident against an Indian aircraft in Pakistan. The jurisdiction of the ICAO Council to entertain the dispute which had been challenged by India was upheld by the ICJ in its decision of August 18th, 1972 *(Appeal Relating to the Jurisdiction of the ICAO Council (India v. Pakistan),* /1972/ I.C.J. Rep. 46, 70), see also Fitzgerald, G., *The Judgment of the International Court of Justice in the Appeal Relating to the Juridiction of the ICAO Council,* XII, C.Y.I.L. at 153 *et seq.* (1974). But also in this case the proceedings on the merits were discontinued and the case was closed following a joint statement by India and Pakistan in 1976 to discontinue the proceedings before the Council.

(14) On *compromis*, see Karin Oellers-Frahm in *Encyclopedia of Public International Law, 1, Settlement of Disputes,* Amsterdam, North-Holland Publishing Company at 45 *et seq.* (1981).

(15) See *infra,* appendix I.

(16) See *infra,* sub III, A.

(17) See *infra,* sub III, B.

(18) Cheng, B., *op. cit.*, note 9 above at 109.

III. THE DECISION

A. THE TOTAL NUMBER OF FLIGHTS PER WEEK BETWEEN BRUSSELS AND DUBLIN

a) *General*

The Belgian Government insisted that the number of eleven flights a week was not in proportion to the traffic demands on the route and asked for a cutback to eight flights a week. The Irish Government, on the other hand, pointed out that a further curtailment of frequency would not be in the public interest and would be counter-productive in terms of market development.

Winberg found the actual number of flights to be not in conformity with the capacity principles contained in Article VIII of the *Bilateral Agreement*. The first part of Article VIII which requires that capacity be adapted to traffic requirements is explained by the arbitrator as follows:

> «This means that the capacity shall be sufficient to cater for the demand for traffic at a certain fare level. Every demand cannot be satisfied due to the collective nature of public transport, which can be made available only at certain times of the day/week, etc. The provision also means that capacity shall be limited and that excess capacity may not be mounted on the route, which may lead to uneconomic operations» (19).

Due to the high number of flights per week between Brussels and Dublin, the total route capacity no longer conformed to the actual demand. This lead to a situation of overcapacity which in the present case was also due to the non-observance of the second part of Article VIII obliging the airlines «to take into consideration their mutual interest so as not to affect unduly their respective services». According to Winberg,

> «This means in particular, that one airline should not operate excess capacity which could endanger the viability of the other airline's operations on the route or limit its access to high yield sectors of the route» (20).

This statement reflects the very specific character of the dispute. When SABENA decided to start operating again on the Brussels-Dublin route, which it was entitled to do, it did not get a proper chance to reestablish itself because Air Lingus continued operating at too high a frequency. Under Article VIII, (2) of the *Bilateral Agreement,* no carrier should try to get the upper hand on the route by unfair competition. It becomes evident, from the arbitral award, that there is no reason why this obligation should not apply when, after an interruption, a carrier starts operating again on a route.

From the foregoing, the arbitrator concluded that, as future traffic growth would not be enough to remedy the situation of overcapacity, a reduction of the number of flights was needed. In coming to this conclusion, a lot of weight was given to the principle that operations have to be economically justified. Winberg derived this principle not only from the capacity clause

(19) See *infra,* appendix II, 1.2.1.

(20) See *infra,* appendix II, 1.2.2.

but also from the tariff clause of the *Bilateral Agreement* and the Preamble of the *Chicago Convention* (21).

b) The comparative Method of Treaty Interpretation and bilateral Air Transport Agreements

Upon explaining the first part of Article VIII of the *Bilateral Agreement* Winberg compares this clause to a similar provision in the *Bermuda I Agreement:*

> «I do not regard the corresponding provision in the original Bermuda Agreement or alternative provisions, that capacity shall bear a close relationship to the traffic demand, to be significantly different from the expression used in Article VIII of the Belgium-Ireland Agreement. The differences are in my opinion of no relevance with regard to the actual capacity situation on the route» (22).

The comparative method, even though in this case it may only confirm the result reached by a direct interpretation of Article VIII (1) is an inadequate method for the interpretation of capacity principles in bilateral air transport agreements (23). While it is true that the *Bermuda I Capacity Principles* are reproduced almost *verbatim* in the majority of the bilateral air transport agreements concluded between other States, this does not mean they are *ipso facto* interpreted in the same way as by the original Bermuda parties. Although neither the U.S.A. nor the U.K. ever gave a clear official interpretation of the *Bermuda I Capacity Principles,* it is understood that they were intended to create a liberal regime of capacity regulation giving the airlines the freedom to operate services at the capacity and frequency they desire subject to an eventual periodical *ex post facto* review by the States concerned (24).

(21) Article 7 of the *Bilateral Agreement* provides *inter alia* that «Fares shall be fixed at reasonable levels, with particular regard to economy of operation, normal profits and the characteristics of each service, such as standards of speed and comfort».

Reference is also made to the following provision of the Preamble of the *Chicago Convention: « Therefore, the undersigned governments having agreed on certain principles and arrangements in order that international civil aviation may be developed in a safe and orderly manner and that international air transport services may be established on the basis of equality of opportunity and operated soundly and economically».* On the legal value of this principle, see Wassenbergh, H., *Post-War International Civil Aviation Policy and the Law of the Air,* The Hague, M. Nijhoff, at 136 (1962).

(22) See *infra,* appendix II, 1.2.1.

(23) On the comparative method of treaty interpretation, see Bos, M., *Theory and Practice of Treaty Interpretation,* 27 N.I.L.R. at 140 *et seq.* (1980); Degan, V., *L'interprétation des accords en droit international,* La Haye, M. Nijhoff at 100 *et seq.* (1963); Guggenheim, P., *Traité de droit international public,* Tome I, Genève, Librairie de l'Univ. Georg S.A. at 263 *et. seq.* (1967); Oppenheim, L., *International Law. A Treatise, Vol. I Peace,* Ed. by H. Lauterpacht, London, Longmans, at 954 (1957); Rousseau, C., *Droit international public, Tome I, Introduction et sources,* Paris, Sirey at 275 *et seq.* (1970).

(24) *Joint Statement by the U.S. and British Governments,* 15 U.S. DEPT. OF STATE BULL. at 577-578 (1946); see also the statement of G. Baker: «I can categorically say, as Chairman of the United States Delegation, that there would have been no Bermuda Agreement signed by the United States if that Agreement were understood to approve or condone the intergovernmental allocation of capacity», *op. cit.,* note 7 above at 255.

This liberal interpretation has never been uniformly accepted by other States which have entered into *Bermuda* I type bilaterals. In fact, the general way in which the *Bermuda I Capacity Principles* are drafted allows both a more liberal and a more restrictive interpretation. The former is, in practice, only possible between States having equal bargaining power (25). States with a less favourable bargaining position have always tried to impose restrictions or to seek compensation from the stronger State (26). These restrictive interpretations can take various forms. Some States interpret the « fair and equal opportunity » clause as a basis for a 50/50 division of the total route capacity. Others correlate the amount of fifth freedom traffic to third and fourth freedom traffic carried on the route or impose the fifth freedom traffic conditions to the so-called sixth freedom traffic (27). Furthermore, limitations on frequency, timetables, cargo or equipment are not unusual. Very often, the *Bermuda I Capacity Principles* appear in an air transport agreement between other States while the actual interpretation of these principles is recorded in a secret memorandum of understanding or an exchange of letters. These instruments have little in common with what is known in international law as interpretative agreements (28). In fact, they often constitute the actual regulation of the air transport services between the two States concerned. Traffic rights granted in the bilateral air transport agreement can be restricted or more rights can be granted. On the other hand, the *Bermuda I Capacity Principles* can be turned into a regime of pre-determination of capacity or *vice versa* (29). In this context, it becomes obvious that the comparison of the texts of two official bilateral air transport agreements is a rather inaccurate way of assessing the actual intention of the respective parties (30).

(25) The bargaining power of a State in the exchange process of air traffic rights is largely determined by the value of the market in terms of possible airline revenues it has to offer. In many cases, however, the negotiating process is affected to a very important extent by political or other non-aviation objectives, see Loy, F., *Bilateral Air Transport Agreements: Some Problems in Finding a Fair Route Exchange,* in *Freedom of the Air,* Ed. by E. McWhinney and M.A. Bradley, Leiden, Sijthoff at 193 *et. seq.* (1968); Thornton, R., *International Airlines and Politics. A Study in Adaptation to Change,* Ann Arbor, Michigan, Graduate School of Business Administration, Univ. of Michigan, at 80 *et seq.* (1970).

(26) See Wassenbergh, H., *Aspects of Air Law and Civil Air Policy in the Seventies,* The Hague, M. Nijhoff at 31 (1970);

(27) The so-called « sixth freedom » refers to the carriage of traffic between two foreign States via the home State of the carrier under two separate bilaterals, see Cheng, B., *op. cit.,* note 2 above, at 13.

(28) On interpretative agreements, see Voicu, I, *De l'interprétation authentique des traités internationaux,* Paris, Pedone at 157 *et seq.* (1968).

(29) It is especially with regard to bilateral air transport agreements that Anzilotti's remark on interpretative agreements is right: « Il peut, parfois, y avoir doute sur le point de savoir si l'accord est vraiment interprétatif de normes existantes ou au contraire constitutif de normes nouvelles », Anzilotti, D., *Cours de droit international, Premier Vol.: Introduction - Théories générales,* Paris, Sirey at 110 (1929). Naveau rightly describes secret memoranda of understanding relating to bilateral air transport agreements as « de véritables contre-lettres au sens du droit civil continental », Naveau, J., *op. cit.,* note 2 above, at 113.

B. THE DISTRIBUTION OF FLIGHTS BETWEEN SABENA BELGIAN WORLD AIRLINES AND AIR LINGUS IRISH AIRLINES

a) General

Belgium held the view that capacity and frequency on the Brussels-Dublin route should be equally divided between Air Lingus and SABENA. Ireland, on the other hand, considered that a 50/50 division of capacity «would fail to acknowledge either the work which Air Lingus had done in building up the Dublin-Brussels route or the degree to which Air Lingus had already eut back its services to accommodate SABENA».

Ireland supported its view with the argument that 60% of the traffic was of Irish origin and should be carrried by the Irish airline. Such an interpretation is supported by various States who consider the traffic originating in their territory as their property and wish to reserve it accordingly to their national carrier(s) (31). According to Winberg this argument can be used to show

> «that there is a need to provide frequencies and timings suitable for the Irish originating traffic, and not, *per se* to argue that this traffic should be carried by the national airline, which would not have any support in the provisions of the air agreement» (32).

Belgium made reference to a particular clause of a pooling agreement concluded between Air Lingus and SABENA in June 1979 which was worded as follows:

> «In principle the agreed capacity/frequency in any traffic period shall be shared equally. However, the partners may with regard to the practical circumstances agree to deviate from this principle for specifie traffic periods» (33).

This provision was explained by the arbitrator as follows:

> «My understanding is that this provision may well reflect a realistic assessment that the application of the liberal air agreement described above will - sooner or later - lead to an equal sharing of capacity/frequencies. *However, the agreement itself does not contain any specific provision to that effect» (34).*

(30) The same unfortunate reasoning was followed although to a lesser extent in the Italy-U.S. Air Transport Arbitration where the Arbitral Tribunal also relied indirectly on the objectives of the *Bermuda I Agreement* in the interpretation of a provision of the bilateral air transport agreement between Italy and the U.S.A., see *Italy-U.S. Air Transport Arbitration: Advisory Opinion of Tribunal* (given at Geneva, July 17, 1965), IV ILM at 982 (1965); Bradley, M.A., *op. cit.*, note 1 above, at 320.

(31) This comes close to the so-called «Ferreira Doctrine» according to which international air transport between two States is the joint property of these two States, each of them being allowed to carry an equal share of the total capacity between their territories, see Jimenez de Aréchaga, E., *South American Attitudes Towards the Regulation of International Air Transportation,*in *Freedom of the Air,* Ed. by E. McWhinney and M.A. Bradley, Leiden, Sijthoff at 79 (1968). On these interpretations and the difficulties in determining the real origin and destination of international air traffic, see Wassenbergh, H., *op. cit.*, note 26 above, at 23 *et seq.; ibidem, op. cit.*, note 2 above, at 21 *et seq.*

(32) See *infra,* appendix II, 1.3.3.

(33) See *infra,* appendix II, 1.3.2.

(34) Author's italics, *ibidem.*

From a provision in the Confidential Memorandum of Understanding relating to the *Bilateral Agreement* saying that the exercise of certain fifth freedom traffic rights were subject to the conclusion of a pooling agreement between the designated airlines, the arbitrator further concluded, on the basis of an *a contrario* reasoning, that the third and fourth freedom traffic rights could be exercised without a pooling agreement (35). As a result and after a very detailed economic analysis of the market characteristics of the Brussels-Dublin route, Winberg finally decided that SABENA, which was operating four roundtrips, should eut back one roundtrip and Air Lingus, which was operating six roundtrips, would cut back two (36). This was only a temporary measure. In the words of the arbitrator:

> «I regard the reduction of total capacity and the apportionment of the remaining capacity as a *temporary measure* in order to bring the operations of the airlines back within the framework of the air agreement. *It is without prejudice to the establishment of the total capacity and the apportionment of capacity in the future within that framework*» (37).

b) *Pooling Agreements as an Element of Subsequent Practice of the Parties in the Application of a Bilateral Air Transport Agreement*

According to Winberg, neither the *Bilateral Agreement* itself, nor the confidential exchange of notes relating to it required *per se a* 50/50 division of frequency as provided for in the pooling agreement:

> «There is no provision in the agreement that the designated airlines shall share the capacity 50/50. Such a distribution of capacity may well be in conformity with the air agreement, but that can also be the case with a distribution of capacity in other proportions provided that the airlines observe the said principles» (38).

Though the capacity clause of the *Bilateral Agreement* would allow both a 50/50 division of capacity as well as any other division of capacity, the arbitrator thus refused to take into account the clear intention of both SABENA and Air Lingus to come to an equal share of capacity and frequency, as expressed in the 1979 pooling agreement, since there was no basis for such a division in the *Bilateral Agreement* and a pooling agreement was not required by that agreement. Even in the absence of a restriction on the arbitrator's mandate in the terms of reference to the arbitration, Winberg's position could still be justified as in the present case the pooling agreement, which was only a seasonal one and no longer in force at the time of arbitration, was a rather insufficient decisive factor.

In explaining his approach, however, the arbitrator gives too much consideration to text of the *Bilateral Agreement* itself which is in fact only the top of the legal iceberg governing the regulation of air transport services bet-

(35) See *infra,* Sub b.

(36) The arbitration only reduced the capacity for the business market (Sunday evening to Friday evening) leaving the airlines the freedom to develop their services for the transit and VFA market (Saturday and Sunday).

(37) Author's italics, appendix II, 3.5.

(38) See *infra,* appendix II, 1.1.

ween two States. Even when a bilateral air transport agreement or a Confidential Memorandum relating to it is silent on pooling, nothing prevents the carriers from concluding a valid and binding pooling agreement provided this agreement does not contravene the capacity principles of the bilateral air transport agreement and is not prohibited by national laws (39). When filed with the aeronautical authorities such an agreement may receive the express or at least the tacit consent of both governments (40). There should be no reason why this consent to a private commercial contract between airlines could not constitute a relevant subsequent practice of the parties to a bilateral air transport agreement which should be taken into account in assessing the intention of the parties (41). This is the more true given the particular nature of an international air transport arbitration which was very well characterized by Larsen in his comments on the 1963 France-US air transport arbitration:

> «Consequently, the airlines are the real parties in the arbitration between the United States and France. They both furnish arguments for their States and are, indeed, the subjects of arbitration. Because of the airlines' strong private interest, the proceedings assume the character of a commercial arbitration between two airlines. The competitiveness with which arguments are brought forth in the United States-France arbitration indicates how the airlines bring pressure to bear on their governments to further their case» (42).

IV. THE DISPUTE AND THE EMERGING EEC AIR TRANSPORT LAW

The present arbitral award deals with a capacity dispute on an intra-EEC air transport route. In the framework of the emerging Common Market air transport policy, the regulation of capacity is likely to become more closely

(39) In the USA, the CAB (Civil Aeronautics Board) has constantly refused to exempt pooling agreements from the operation of the US Anti-trust laws under Sections 412 and 414 of the *Federal Aviation Act* (72 Stat 731 as amended), see Haanappel, *op. cit.*, note 4 above, at 83 *et seq.* For the postion of the EEC Commission on pooling agreements, see *infra,* sub IV.

(40) Although most States do have the administrative power to require the filing of pooling agreements, the actual State control over pooling agreements is in most cases very minimal, see *ECAC (European Civil Aviation Conference) Report on Competition in Intra-European Air Services,* Paris, 1982, ECAC Doc. 25 at 43.

(41) In the air transport arbitration between the U.S. and France in 1963, the conduct of a U.S. airline as notified to the Secretary General of the French Civil Aviation Administration was taken into account as relevant subsequent practice of the parties, see *Decision of the Arbitration Tribunal Established Pursuant to the Arbitration Agreement signed at Paris on January 22, 1963 between the United States and France, decided at Geneva on December 22, 1963,* III I.L.M. 713 *et seq.* (1964). On the role of subsequent practice of the parties for the interpretation of a treaty in general, see *Vienna Convention on the Law of Treaties,* Art. 31(3), 8 I.L.M. (1969) at 679; and further Cot, J.P., *La conduite subséquente des Parties à un Traité,* 70 R.G.D.I.P. at 632 *et seq.* (1966); de Visscher, C., *Problèmes d'interprétation judiciaire en droit international public,* Paris, Pedone at 131 *et seq.* (1963); Mc Nair, L., *The Law of Treaties,* Oxford, The Clarendon Press at 425 *et seq. (1961).*

(42) Larsen, P.B., *op. cit.*, note 1 above, at 246.

scrutinized by the Commission (43). In February 1984 the Second Civil Aviation Memorandum «*Progress Towards The Development of a Community Air Transport Policy*» was presented by the Commission to the EEC Council (44). This document, a follow-up to the Commission's 1979 First Memorandum in this field, contains further formulation and implementation of the Common Market air transport policy (45). The Commission proposed it would gradually relax the present regulatory system of air transport within the Common Market. The aim of this would be to arrive at a more competitive air transport system, serving the interests of the consumers without overlooking the benefits of the present system (46). For the purpose of this article, it will be sufficient to point out the Commission's proposals on the regulation of capacity and pooling agreements.

The Commission proposed a *Council Decision on Air Transport Bilateral Agreements, Arrangements and Memoranda of Understanding between Member States* urging the Member States not to make capacity and pooling agreements a condition under bilateral air transport agreements nor «refuse capacity increases and/or impose capacity restrictions on airlines designated by another Member State for services on routes between itself and that other Member State, unless the scheduled traffic share of the airline(s), it has designated of operation of the routes between itself and that other Member State, had during the previous six months, been less than 25 % of the total scheduled traffic carried by the airlines designated by itself and that other Member State for those routes» (47).

Provided the EEC competition rules effectively apply to the air transport sector, capacity and pooling agreements will be contrary to Article 85 (1) of the EEC *Treaty* (48). However, the Commission will be prepared to exempt those agreements under Article 85 (3) of the EEC *Treaty* under certain con-

(43) On the application of the *Treaty Establishing the European Economic Community (hereinafter cited as* Eec Treaty) to international air transport in general and the first steps towards a Common Market air transport policy, see Merckx, A,. *Het EEG Verdrag en de Luchtvaart, Onuitgegeven Licentiaatsverhandeling, Faculteit der Rechtsgeleerdheid, K.U. Leuven (1980);* Weber, L., *Die Zivilluftfahrt im Europäischem Gemeinschaftsrecht,* Berlin, Heidelberg, New York, Springer-Verlag (1981).

(44) See *Civil Aviation Memorandum No. 2. Progress Towards the Development of a Community Air Transport Policy,* Brussels, 22 February 1984, COM (84) 72 Final, *hereinafter* cited as Civil Aviation Memorandum No. 2.

(45) See *Air Transport: A Community Approach,* EEC Bulletin, Suppl 5/79.

(46) See *Civil Aviation Memorandum No. 2,* para. 46 at p. 26-27.

(47) See *Civil Aviation Memorandum No. 2.,* Annex I.

(48) On July 31, 1981 the Commission submitted a *Proposal for a Council Regulation applying Articles 85 and 86 of the Treaty (rules on competition applying to undertakings) to air transport,* COM (81) 396 final. See also proposed amendment in O.J. No. C 317, 3.12.1982 p. 3. Once adopted by the Council, this Regulation will give the Commission the full power to enforce Articles 85 and 86 of the EEC *Treaty* to air transport. The Commission's actual powers are very limited under Article 89, apart from those of the Member States under Article 88 of the EEC *Treaty,* see further Weber, L., *op. cit.,* note 43 above, at 194 *et seq.*

ditions (49). Capacity agreements will be eligible for a group exemption under Article 85 (3) provided that any party can withdraw from such an agreement without penalty on giving three months notice (50). As to pooling agreements, the Commission draws a distinction between «open» pooling agreements with no ceiling on the share of revenues and «limited» pooling agreements with a limitation on the level of revenue sharing. The former cannot be exempted under Article 85 (3) of EEC *Treaty*. The latter could qualify for a group exemption under Article 85 (3) provided they limit the transfer of revenue from one airline to the other to 1 % of the pooled revenue, «no costs are shared or accepted by the transferring parties and the transfer is made by way of compensation for the detriment incurred by the transferee in scheduling flights at less busy times of day or during less heavy periods» (51). Other limited pooling agreements might be exempted on an individual basis according to certain conditions (52).

The present dispute illustrates how both the interests of the consumers and the airlines' economic viability could be better served by a pooling agreement which would assure a reasonable distribution of flights outside the peak periods and thus remedying the situation of overcapacity. One could even go further in this case and think of «dormant» pooling agreement whereby only one airline operates on the route on the basis of a joint cost and revenue sharing agreement with the the other airline (53).

Finally, whereas air transport might come under the scope of the EEC *Treaty* the economic specificity of this industry, especially in a European context, should be the underlying guideline to any legal approach (54). In the case discussed here the arbitrator took this approach. His very pragmatic decision and due consideration of the economic realities behind this dispute could serve as a future example in the EEC context.

(49) To that effect a *Proposal for a Council Regulation on the Application of Art. 85 (3) of the Treaty to certain Categories of Agreements and Connected Practices in the Air Transport Sector* was introduced by the Commission to the Council, see *Civil Aviation Memorandum No. 2,* Annex IIIB.

(50) See *Civil Aviation Memorandum No. 2,* para. 51 at p. 30 and also Annex IIIC.

(51) See *Civil Aviation Memorandum No. 2,* Annex IIIC.

(52) The Commission recognizes that pooling agreements might improve the service to the consumer by assuring a spread of services in the less busy and less profitable periods. The following criteria are listed by the Commission: «The revenue sharing resulting from a pool agreement must therefore be clearly related to the improvement in air transport service resulting from the agreement; it must represent the give and take of schedule compromises with the minimum anti-competitive effect. The improvements may be with respect to the service itself or to the cost effectiveness of the service», *Civil Aviation Memorandum No. 2,* at p. 31.

(53) It seems that the Commission might even be prepared to exempt such agreements on an individual basis in cases when «only a single airline could operate economically both from the point of view of the airline and the consumer...», *Civil Aviation Memorandum No. 2,* para. 55, at p. 31.

(54) Naveau recently devoted a complete monography to develop this thesis, see Naveau, J., *L'Europe et le transport aérien,* Bruxelles, Bruylant (1983).

APPENDIX I

ADMINISTRATION
DE
L'AERONAUTIQUE
—
Le Directeur Général

1000 Bruxelles, 25 May, 1981
World Trade Center
Tour I - 8e étage
Boulevard E. Jacqmain 162

Dear Mr Winberg,

As agreed with Mr Mac Mahon, Secretary of the Departement of transport of Ireland, I am writing to you concerning difficulties which have arisen between the Belgian and Irish aeronautical authorities in connection with air services between Brussels and Dublin.

The problem at issue revolves around the level and frequency of services between Brussels and Dublin and the sharing of traffic between Sabena and Aer Lingus.

The Belgian side has maintained a view that the traffic figures for the foreseeable future suggest that an offered capacity of eight flights per week, equally divided between Aer Lingus and Sabena, is in conformity with the capacity provisions of the bilateral agreement.

The Irish side has disputed this interpretation and has maintained that a curtailment of frequencies from the present level of 11 a week (7 Aer Lingus and 4 Sabena) would not be in the public interest and would be counter productive in terms of market development. They also maintain that a 50/50 divide *(sic)* of capacity fails to acknowledge either the work which Aer Lingus has done in building up the Dublin-Brussels route or the degree to which Aer Lingus has already cut back its services to accomodate SABENA.

Both aeronautical authorities endeavoured initially to have the problem resolved at inter-airline level. Those efforts failed. Two rounds of negociations at inter-governmental level followed and both the Belgian and Irish aeronautical authorities are *(sic)* now agreed that the best means of resolving the problem is to have recourse to an arbitrator as provided for in article X of our bilateral agreement.

Article X of the agreement reads as follows:

« 1) Any disputes relating to the interpretation and application of this Agreement or of the Annex thereto which cannot be settled by direct negociation shall be submitted to arbitration.

2) Any such dispute shall be referred for decision to the Council of the International Civil Aviation Organisation.

3) Nevertheless, the contracting parties may, by mutual agreement, settle the dispute by referring it either to an arbitral tribunal or to any other person or body designated by them.

4) The contracting parties undertake to comply with the decision given ».

Since both the Belgian and Irish sides are very anxious to have the problem resolved as expeditiously as possible, it would be the intention of both parties to have recourse to the provisions of paragraph 3 of article X.

In that connection, both aeronautical authorities consider that in view of your long experience in the aviation field and your high international standing, you would be an excellent arbitrator.

Both authorities have accordingly agreed jointly to invite you to act as arbitrator in the present dispute; both sides would agree in accordance with the provisions of the bilateral agreement to comply with the decision arrived at by you.

If you agree to accept this invitation, detailed arrangements in relation to terms of reference and other modalities (including such matters as expenses) can be the subject of a further communication.

The address of the Belgian aeronautical authoritity is Administration of Civil Aeronautics - World Trade Center - Tower I - 8 th Floor - 162 Bd. E. Jacqmain - Box 60 - 1000 Brussels.

Mr Mac Mahon is writing to you in similar terms.

With my highest consideration,

To Mr Henrik WINBERG,
Svanhildsvägen, 1
16141 BROMMA
SWEDEN

W. VANDERPERREN.

APPENDIX II

Arbitral Award in the dispute between the Belgian and the Irish Civil Aviation Authorities over services between Brussels and Dublin by SABENA and Aer Lingus given at Dublin on 17 July, 1981.

Parties:

The Belgian Civil Aviation Authority on behalf of the Belgian Government represented by Mr. W. Vanderperren, assisted by Mrs. M. Soupart and Mr. J. Verstappen. The Irish Civil Aviation Authority on behalf of the Irish Government represented by Mr. N. McMahon, assisted by Mr. K. Kealy.

Arbitrator:

Mr. Henrik Winberg, Bromma Aeroconsulter H B, Svanhildsvagen 1, S-16141 Bromma.

Terms of Reference:

The Parties request for arbitration is contained in their letters of 25 May to the Arbitrator. The letters (Appendix I) constitute the terms of reference for the arbitration.

The Air Agreement:

The air services between Brussels and Dublin are governed by the terms of the Air Transport Agreement of 10 September, 1955 as amended by exchange of notes of 16 December, 1957.

Designated Carriers:

SABENA, designated by the Belgian Government. Aer Lingus, designated by the Irish Government.

The Dispute:

The dispute between the Parties concerns the capacity to be provided by SABENA and Aer Lingus on the Brussels-Dublin route in terms of frequen-

cies and timetables. The present traffic programs are approved by Parties only on a temporary basis pending the outcome of the arbitration.

The Belgian Party has maintained the view that a total capacity of 8 flights per week, equally divided between Aer Lingus and SABENA is in conformity with the capacity provisions of the bilateral agreement.

The Irish side has disputed this interpretation and has maintained that a curtailment of frequencies from the present level of 11 a week (7 Aer Lingus and 4 SABENA) would not be in the public interest and would be counter-productive in terms of market development. They also maintain that a 50/50 divide of capacity fails to acknowledge the work which Aer Lingus has done in building up the Dublin-Brussels route or the degree to which Aer Lingus has already cut back its services to accommodate SABENA.

Proceedings:

The Arbitrator has met with the Parties in Paris on 10 June, 1981, in Brussels on 25 June, 1981 and in Dublin on 16/17 July, 1981. At the first meeting the parties presented their argumentation orally and made written submissions, which were exchanged. The Belgian and the Irish Party have submitted written comments, dated 15 and 19 June, 1981 respectively. The Arbitrator has sought further information from the designated airlines at a meeting in Brussels on 24 June, 1981 and has received from the Irish party statements of timing requirements and load factors dated July, 1981 and from the Belgian Party a timetable made up by SABENA, dated July 6, 1981. The airlines have jointly submitted a note dated 15 July, 1981 on a common traffic program.

Grounds for decision:

The Arbitrator has considered the argumentation of the Parties and the other material submitted to him and will deal with the relevant elements in the dispute in the following order:

1. Characteristics of the Air Agreement

1.1. General

The air agreement is a liberal agreement of the original Bermuda type, which leaves the airlines with great freedom in establishing their air services and to compete with each other within the framework of the principles contained in the capacity clause and of those underlying the tariff clause.

The airlines have full freedom of access to the air transport market as a whole and to any submarket that may exist, such as the market for duty and business travel, for tourist travel and for VFR travel, subject to the observance of the aforementioned principles.

There is no provision in the agreement that the designated airlines shall share the capacity 50/50. Such a distribution of capacity may well be in con-

formity with the air agreement, but that can also be the case with a distribution of capacity in other proportions provided that the airlines observe the said principles.

1.2. The Framework of Principles (limitations, safeguards)

1.2.1. Article VIII subpara (1) of the air agreement provides that capacity shall be adapted to the traffic requirements (aux necessites *(sic)* du trafic). This means that the capacity shall be sufficient to cater for the demand for traffic at a certain fare level. Every demand can not be satisfied due to the collective nature of public transport, which can be made available only at certain times of the day/week etc. The provision also means that capacity shall be limited and that excess capacity may not be mounted on the route, which may lead to uneconomic operations (see point 1.2.3.). I do not regard the corresponding provision in the original Bermuda agreement or alternative provisions, that capacity shall bear a close relationship to the traffic demand, to be significantly different from the expression used in Article VIII of the Belgium/Ireland agreement. The differences are in my opinion of no relevance with regard to the actual capacity situation on the route (see point 2).

1.2.2. Article VIII subpara (2) provides that the airlines shall take into consideration their mutual interests so as not to affect unduly their respective services. This means, in particular, that one airline should not operate excess capacity which could endanger the viability of the other airline's operations on the route or limit its access to high yield sectors of the route.

1.2.3. Article VII subpara (1) states that fares shall be fixed at reasonable levels, with particular regard to economy of operation (frais d'exploitation), normal profits and the characteristics of each service. This provision indicates that the Contracting Parties have intended that their designated airlines should operate economically and with normal profit. They have in another context subscribed to the principle that air services shall be operated soundly and economically (the preamble to the Chicago Convention).

If nevertheless an airline would not obtain normal profits from the operation of the route and still more if revenue would not cover costs, the airline would have to consider to withdraw from the operation of the route, unless the unsatisfactory economic results could be due to non-observance by either or both airlines of the above mentioned principles. In such case the aeronautical authorities shall consult with each other and, as the case may be, eventually proceed to arbitration. This is what has happened in the present dispute and the primary objective of the arbitration is to examine if the operations are in conformity with the said principles.

1.3. Particular Aspects

Before going into an analysis of the actual situation (see points 2 and 3) I wish to take up some arguments advanced in the course of the arbitration, which are related to the interpretation of the air agreement.

1.3.1. According to a confidential exchange of notes in connection with the conclusion of the air agreement 1955 the Contracting Parties have agreed that the exercise of certain 5th freedom traffic rights were subject to the conclusion of a pool agreement between the designated airlines. I have, a contrario, concluded that the 3/4th freedom traffic rights can be exercised without any requirement for the conclusion of a pool agreement.

1.3.2. It has been pointed out from the Belgian side that the pool agreement concluded between the designated airlines in June, 1979 contains the following provision in article 1 subpara 3:

> «In principle the agreed capacity/frequency in any traffic period shall be shared equally. However, the partners may with regard to the practical circumstances agree to deviate from this principle for specific traffic periods».

My understanding is that this provision may well reflect a realistic assessment that the application of the liberal air agreement described above will - sooner or later - lead to an equal sharing of capacity/frequencies. However, the agreement itself does not contain any specific provision to that effect.

1.3.3. It has been pointed out from the Irish side that almost 60 % of the traffic is Irish originating. This argument has been carried forward in order to support the view that there is a need to provide frequencies and timings suitable for the Irish originating traffic, and not, per se, to argue that this traffic should be carried by the national airline, which would not have any support in the provisions of the air agreement.

2. Total Capacity

2.1. Traffic, Load Factors and Economy

During the last four years 1977/78-1980/81 the passenger traffic on the Brussels-Dublin route has been relatively stable in the range of 46,000-51,000 passengers/year. The output of capacity has until July, 1979 been determined by Aer Lingus alone.

From the summer 1979 both airlines have operated the route non-stop point to point. The total number of frequencies in the Summer season was increased compared with 1978 (13 peak, 12 shoulder) by one in the peak and two in the shoulder. In 1980 the number of frequencies was brought back to the 1978 level and in 1981 there was one frequency less than in 1978 (12 peak, 11 shoulder).

During the Winter seasons the airlines together operated one frequency more 1979/80 (4 + 9) than Aer Lingus alone 1978/79 and last Winter Aer Lingus cut back two frequencies (to 7) so as to arrive at 11 frequencies for both airlines together.

The output of seats has not changed in proportion to the number of frequencies, because Aer Lingus has terminated its operations through Brussels to Frankfurt and Dusseldorf after the Winter season 1978/79 and SABENA has used higher capacity aircraft than Aer Lingus during the Winter season and part of the shoulder season (B737 with 107 seats in lieu of BAC 111 with 74 seats).

The aggregate effect of the traffic development and the capacity planning has been average passenger load factors of about 40 % during the last two years. This is a very low figure compared with other European routes operated by the designated airlines and other European airlines.

The Irish side has indicated that Aer Lingus breakeven load factor is around 40 % thanks to the relatively high yield. This means that no contribution to overhead costs could be obtained from operations at that load factor level.

The actual situation of the two airlines is however somewhat different. Aer Lingus has achieved a load factor of about 48 %, while SABENA'S load factor in the Summertime has been around 28 % and in the Wintertime around 19 %. (If SABENA, like Aer Lingus, had used BAC 111, the Winter load factor would have increased to around 27 % or about the same as in the Summertime). This indicates that SABENA - given even the same breakeven load factor as Aer Lingus - cannot recover all attributable costs from the operation of the route. This situation has lasted for two years and represents are economic hardship to SABENA.

Towards this background I regard the present output of capacity as excessive, which unduly affects SABENA'S operations and probably also prevents optimal operation of Aer Lingus services.

2.2. Forecasts

It is easy to say, in retrospect, that both airlines have overestimated the traffic growth during the last two years.

Excess capacity can be tolerated during a short period of time, if a significant increase of traffic can be expected in the near future. Experts from SABENA and Aer Lingus have as late as in May, 1981 estimated the foreseeable traffic growth to be in the order of 8 %. Judging from revised forecasts of the growth of GNP in Western European countries during the next few years I believe that lower growth of airline traffic can be expected. (The rule of the thumb suggests that the elasticity factor is around 2, which means that an increase in GNP of 2 % will result in an increase in airline traffic of 4 %). Even if the higher growth rate of 8 % were accepted, it would still take too long until the total capacity could be properly adapted to the traffic requirements, so as to arrive at sound economic operations for both airlines.

If the present capacity situation is allowed to continue unchanged, my forecast is that SABENA will be forced out of the market for economic reasons. Such a development cannot be in line with the purpose of the air agreement and the intentions of the Contracting Parties when concluding the agreement.

2.3. The Public Interest

It is important that the air transport system can provide on demand accommodation on reasonably frequent air services, in particular to duty and business travellers. Load factors must therefore not be so high that these demands cannot be met. An average utilisation of more than 65 % has in the past been regarded as a limit that should not be surpassed.

A reduction of the non-stop services during the day is always felt as an inconvenience by the public, but these demands have to be tempered by economic considerations. A volume of traffic of 40,000 or more passengers/year is often regarded as sufficient for economic operation of a daily non-stop route, and the basic need of a daily service on the Brussels-Dublin route can therefore be expected to be safeguarded. I will come back to the question whether the public interest may require specific timings on this route.

2.5. *(sic)* Conclusion

My conclusion is that overcapacity has existed on the Brussels-Dublin route for two years, that future traffic growth is not likely to remedy this situations and that a reduction of capacity is needed as early as possible.

3. Distribution of Capacity

3.1. The Submarkets

In broad terms one can distinguish between the duty and business market, which flows mainly from Sunday evening to Friday evening, and the market for tourist and VFR traffic, which flows mainly on Saturdays and Sundays with some overlap on Fridays and Mondays.

The overcapacity and the zone of conflicting airline interests is at present to be found in the former market and the necessary adjustments of capacity and traffic programs should be made there.

3.2. Scheduling and influence of Aircraft Basing

There is an operational and economic advantage for an airline to avoid the costs for night stopovers for aircraft and crew. However, I do not regard operations with aircraft stationed overnight outside the homebase as irregular, when needed for serving the public properly.

The flight time between Brussels and Dublin is 1 1/2 hours and both SABENA and Aer Lingus should also be able to provide roundtrip services in the mornings and in the evenings from their homebases so as to give the public reasonable timetable satisfaction.

Neither airline has a prerogative of operating its services at a certain time of the day. Due regard should, however, be given to the needs of both airlines to schedule their overall operations so as to achieve optimum utilisation of their aircraft.

3.3. Apportionment of Capacity

In order to reduce overcapacity and to avoid interference it would have been desirable to limit the output of capacity to a daily roundtrip during the Sunday evening - Friday evening period, *i.e.* six roundtrips compared with ten roundtrips at the present time. I realise that adjustments have to

be made with certain caution and with due regard to the now existing proportions between the airlines' total output of capacity on the route.

SABENA is presently operating four roundtrips during the period in question and Aer Lingus six. Both airlines should reduce their present capacity so as to interfere as little as possible with each others services.

Without prejudice to any future proportion, in which capacity might be shared, I deem it appropriate that SABENA yields one roundtrip and Aer Lingus two roundtrips.

3.4. Tourist and « VFR » Markets

I see no need at this time to include specific attention to the provision of capacity for the proper tourist and « VFR » markets in the arbitration. I would like to see the airlines developing their air services for these markets without any further guidance but within the framework of the air agreement.

3.5. Implications

I have been warned that a decrease of frequencies may lead to diversion of traffic to indirect routings. I agree that there will be an increased need for urgent travellers to be routed via London and Amsterdam and the airlines should be ready to assist their clients in finding the best possible substitutes, when a suitable non-stop service is not available. I believe, however, that such diversion will be small compared with the cutback in frequencies.

A cutback in frequencies will also - at least in the short term - delay a development towards a pattern of two roundtrip services a day, which appears to be a common goal for the airlines. Both airlines will have to make considerable efforts to make such a development possible and it can hardly be expected that such efforts will materialise full as long as one of the airlines is in the red on the route. A necessary prerequisite for this development is that both airlines are working from a common platform, where both are making profit and operate within the framework of the principles of the air agreement.

I am confident that a cutback of frequencies as indicated above will produce an average load factor around 50% in the course of the following 12 months. I also consider that the possibility for SABENA to get *de facto* access to some evening slots now operated by Aer Lingus will diminish the gap between the breakeven load factors of the two airlines on the route.

I regard the reduction of total capacity and the apportionment of the remaining capacity as a temporary measure in order to bring the operations of the airlines back within the framework of the air agreement. It is without prejudice to the establishment of the total capacity and the apportionment of capacity in the future within that framework.

The Arbitrator's Decision:

The capacity offered by the designated airlines on the Brussels-Dublin route is in certain respects significantly in excess of traffic requirements, which is in contradiction with the principle of sound economic operations underlying the air agreement. In establishing their traffic programs in this way the airlines have not properly taken into account their mutual interests, which has led to undue effects on their respective services.

A reduction of capacity during the period Sunday evening - Friday evening by two roundtrips for Aer Lingus and one roundtrip for SABENA is required as early as practicable.

Henrik Winberg.