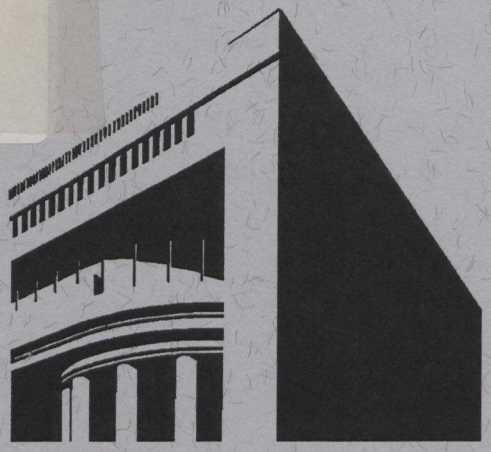

Canadian Studies Grant Programs

An Analysis of Canadian Air Transport Bilateral Agreements

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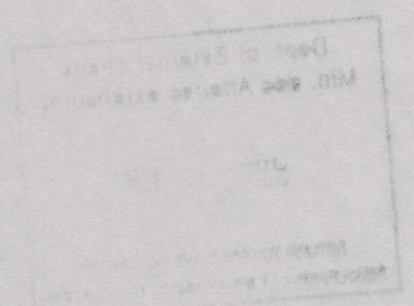

An Analysis of Canadian Air Transport Bilateral Agreements*

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An Analysis of Canadian Air Transport Bilateral Agreements

I. Introduction

On February 24, 1995, after 16 years of negotiations, Canada and the United States agreed to an "open skies" air transport bilateral.[1] After an initial phase-in period, the bilateral removed restrictions to transborder routes by both Canadian and U.S. carriers and effectively eliminated governmental control over pricing.[2] The intent of the agreement was to open transborder routes to greater competition among airlines, reduce prices on transborder routes, and increase the number of services offered. Early results indicate that the open skies agreement has been effective at increasing the number of services available to cross-border travelers.[3]

But what of Canada's other air transport bilateral agreements?[4] Do they promote competition on international air routes, act to reduce prices, and increase services to the traveling public? The bilateral agreement with Canada was just one of a series of open skies agreements

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1 "Air Transport Agreement Between the Government of Canada and the Government of the United States of America", *Canada Treaty Series*, 1995, no. 4.

2 *Ibid.* Annex 5 limited the frequencies U.S. carriers could offer on transborder services into Montreal and Vancouver for a period of two years and on services to Toronto for a period of three years. After this phase-in period, carriers from both countries are free to offer whatever transborder services they choose, subject to gate and slot availability. Article 5(2) on pricing states that without the mutual agreement of the Governments of Canada and the United States, airline prices may "go into effect or continue in effect". In other words, prices determined by carriers may not be disapproved by any single government.

3 Canadian Transport Minister David Anderson reported that the open skies agreement sparked the creation of 102 new scheduled routes between Canada and the U.S. in its first year of existence, 56 of them operated by Canadian carriers and 46 by U.S. carriers. The Canadian government also maintains that transborder air travel is now less expensive. See: "New Routes, Bargain Fares: Consumers Cash In", *The Globe and Mail*, Toronto, April 3, 1996, p. C1.

4 Canada currently has air transport bilateral agreements with about 60 countries. See: Canada, Transport Canada, "Canada's International Air Transportation Policy", statement of the Minister of Transport, December 20, 1994, p. 3.

signed by the United States.[5] But for Canada, the open skies agreement was the first bilateral to provide both unlimited access to routes by carriers of both countries and to effectively remove governmental control over pricing. Unlike the United States, Canada did not actively pursue a liberal or open skies bilateral policy when it deregulated its domestic air transport system.

This paper provides an analysis of Canadian bilateral air transport agreements signed between 1987 and 1993.[6] In particular, an analysis is conducted of those articles relating to the economics of providing air services, including tariff clauses, capacity clauses, carrier designation provisions and annexes outlining the granting of route rights. The purpose of the paper is to determine to what extent the bilateral agreements have restrictions that impede competition. These restrictions have important public policy implications for at least two reasons. First, Canadian consumers may be paying higher ticket prices for international air travel than would be the case under a more liberal international policy.[7] Second, the restrictive agreements may hamper the implementation of Canada's new international air policy with a goal, among others, to "... ensure consumers benefit from increased price and service competition...".[8] Bilateral

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5 Other open skies agreements are with: Austria, Denmark, Finland, Germany, Iceland, Luxembourg, Norway, Sweden, Switzerland, and, most recently, Singapore.

6 There is often a lag of 1 to 2 years before agreements are published in the *Canada Treaty Series*, so that the most recent agreements are not easily obtainable.

7 Economic studies have shown that liberal or open skies bilateral agreements lead to significantly lower prices. One recent study found that U.S. liberal agreements served to divert passengers from Canadian international routes to U.S. international routes. See: Martin Dresner and Michael W. Tretheway, "Modeling and Testing the Effect of Market Structure on Price: The Case of International Air Transport", *Journal of Transport Economics and Policy*, May 1992, pp. 171-184; and, Martin Dresner and Tae Hoon Oum, "The Effect of Liberalized Air Transport Bilaterals on Foreign Visitor Volume and Traffic Diversion: The Case of Canada", working paper of the University of Maryland, September 1996.

8 Canada, Transport Canada, "Canada's International Air Transportation Policy, *op. cit.* p. 4.

agreements may have to be renegotiated before Canada's new international policy can be fully implemented.

The rest of the paper is structured as follows: Section II briefly outlines the Canadian bilateral agreements examined for this study and describes the key components of these agreements. Section III discusses the articles related to "designation" contained in the agreements; that is the number of designated carriers allowed per country to operate under a bilateral agreement. Section IV describes the capacity articles and commercial agreements in the Canadian agreements and how they affect the determination of carrier capacity on Canadian international air routes. Section V analyzes the tariff articles in Canadian international air agreements. Section VI reviews the route annexes in Canadian international agreements, with an emphasis on those clauses related to fifth freedom traffic rights.[9] Finally, Section VII summarizes the main findings from this paper and draws conclusions as to the level of competition permitted under the agreements.

II. Canadian Air Transport Bilaterals 1987 - 1993

Between 1987 and 1993 Canada had 15 air transport agreements enter into force definitively.[10] Table 1 lists the countries with which these agreements were signed, the dates the agreements entered into force (definitively) and the *Canada Treaty Series* number for each agreement. Note that all but three of the agreements were completed by the end of 1990 and that the period 1991 to 1993 represented a slow period for the conclusion of new air transport bilaterals.

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[9] Fifth freedom traffic includes those passenger carried between countries A and B by a carrier based in country C on flights that originate or terminate in country C.

[10] Included are all new agreements reported in the *Canada Treaty Series*. In addition there were several amendments to existing agreements, generally made through a diplomatic exchange of notes.

Although each Canadian bilateral agreement is unique, they generally share a number of common characteristics. All the agreements examined for this study, for example, have an article covering the designation of carriers by governments or "Contracting Parties" to the agreement. This article permits each Contracting Party to designate one or (sometimes) more carriers to operate on the international routes outlined in the agreement. All Canadian agreements have another article covering capacity levels. This article specifies the rules under which the designated carriers may determine the capacity levels to operate on their international routes. All of the agreements also have a pricing or tariff clause stating the preferred way international prices should be determined under the agreement and what role governments have in determining or approving international air prices. All of the agreements also contain an annex in which the routes designated to the Canadian and partner country carriers are stated, outlining permitted intermediate and beyond points on the routes, and specifying operating restrictions, such as limits on capacities, not outlined in the main part of the agreement.

Canadian bilaterals also contain a number of other articles that are not specifically addressed in this paper. Some of these articles fall under the category of "doing business" issues relating to the permitted user fees that carriers can be charged to operate in a country or to the right of a carrier to have access to airport facilities. Some of the articles relate to security issues or to how disputes between the governments are to be addressed. This paper does not address any of these "non-economic" articles but, instead, is confined to discussions of competitive and economic factors related to designation, capacity, tariffs, and route rights.

III. Designation

As outlined above, Canadian bilateral agreements typically contain a clause outlining the number of carriers that may be designated to operate on routes authorized under the agreements. Two common types of designation are single designation, permitting each of the two countries,

party to the agreement, to designate one carrier per route, or multiple designation, permitting each country to designate one *or more* carriers per route. In a study examining the thirteen bilateral agreements entered into force by Canada between January 1978 and April 1986, Dresner and Tretheway found that eight (61 percent of the total) contained single designation clauses while 5 (39 percent) had multiple designation clauses.[11] Of the fifteen more recent agreements examined for this paper, six (40 percent) were single designation, eight (53 percent) were multiple designation and one (7 percent) was dual designation, reflecting a move by Canada away from single designation and towards multiple designation.[12]

However, even the bilateral agreements that permit the multiple designation of carriers may effectively restrict operations to one carrier per country. These restrictions are often contained in the route annex to the agreement, but may also be found in confidential memoranda of understanding attached to the bilaterals.[13] An example of a restriction found in a route annex is in the Canada-Australia bilateral agreement.[14] The designation clause (Article IV) clearly allows multiple designation, stating, "Each Contracting Party shall have the right to designate ... an airline or airlines to operate the agreed services on the specified routes ...". However, the annex

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[11] Martin Dresner and Michael W. Tretheway, "Policy Choices for Canada in International Air Transport", Proceedings of the Administrative Sciences Association of Canada, Toronto, 1987, pp. 83-94.

[12] Of the seven agreements that entered into force between January 1, 1990 and December 31, 1993, only one (the Ivory Coast) was single designation.

[13] See, Donna Mitchell, "Canadian International Air Transport Historical Background and Current Policy", Ministerial Task Force On International Air Policy: Research Reports, Transport Canada, June 1991, p. 41. Mitchell reported that as of 1990, 20 of 60 Canadian agreements contained attached confidential memoranda of understanding. She stated, "Whether confidential or not, the attached instruments for the most part deal with capacity, commercial (pooling) agreements, tariffs, fifth freedom rights, charters, or the clauses on Rules of Commercial Activity."

[14] Canada, "Air Agreement Between Canada and Australia (with Annex)", *Canada Treaty Series*, 1988, No. 2.

to the agreement describes the "Route to be operated in both directions by the designated *airline* of Canada ... [and] by the designated *airline* of Australia" (emphasis added) implying *de facto* single designation.

Wherever the restrictions may occur in the bilateral agreement, single designation clauses may impede the implementation of Canada's new international air transport policy, announced in 1995. Under Canada's previous international air policy, Canada divided the world between Canadian designated carriers.[15] Carriers were allocated exclusive rights to serve certain countries or regions in the world without competition from other Canadian carriers. Therefore, single designation bilateral agreements were appropriate. However, under the new "Second Carrier Designation Policy", specific conditions are outlined that can lead to the designation of two Canadian carriers (and ostensibly two foreign carriers) per route. The policy states:

> Assessment of applications for second designation for scheduled passenger services by a Canadian carrier, large or small, will be guided by market thresholds, as follows:
>
> - In country markets with at least 300,000 one-way origin/destination passengers per year travelling by scheduled air service, second designations will be made.
> - In country markets with origin/destination traffic less than 300,000, second designations will not be made.[16]

Although the 300,000 passenger threshold currently applies only on routes to the United Kingdom, France, Germany, Hong Kong, and Japan,[17] it certainly may apply to many more

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15 See: Canada, Transport Canada, "Allocation of International Airline Routes", Information Bulletin 248/87, October 5, 1987.

16 Canada, Transport Canada, News Release No. 28/95, March 10, 1995.

17 *Ibid.*

markets in the future. Recognizing that Canadian bilateral agreements with single designation clauses cannot support the new dual designation policy, the policy continues that "... Canada will negotiate second designation rights in markets as they mature, whenever practical...".[18] Successful renegotiation, however, depends on the willingness of the bilateral partner to renegotiate the agreement, so there may be a lag before Canada can fully implement its dual designation policy, even on routes where traffic warrants dual designation.

IV. Capacity and Commercial Agreements

Even if bilateral agreements permit competition through the multiple designation of carriers, they may limit competition in other ways, for example by restricting the number of flights that can be operated on designated routes, or by requiring the designated carriers to divide capacity on authorized routes. In their study of thirteen Canadian agreements signed between January 1978 and April 1986, Dresner and Tretheway found that seven (54 percent) required either a carrier or a governmental agreement on capacities.[19] Of the fifteen more recent agreements studied for this paper, eleven (73 percent) required either carrier or government agreement on capacities or both governments to approve capacity levels, indicating that the Canadian government has, if anything, moved towards more restrictive capacity clauses in its bilateral agreements.

The wording of the first four paragraphs of the capacity clause (Article 10) of the bilateral agreement between Canada and Austria, is typical of Canadian agreements.[20] Paragraph 1 states that there "shall be a fair and equal opportunity for the designated airline or airlines of each

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[18] *Ibid.*

[19] Dresner and Tretheway, "Policy Choices for Canada in International Air Transport", *op. cit.*, p. 89.

[20] Canada, "Agreement Between the Government of Canada and the Austrian Federal Government on Air Transport (with Annex)", *Canada Treaty Series*, 1993, No. 19.

Contracting Party to operate the agreed services...".[21] Paragraph 2 provides that the carriers of one country should take into account the interest of the carriers of the other country, "so as not to affect unduly the services which the latter provides on the whole or part of the same route". Paragraphs 3 and 4 allow that the carriers operating under the agreement provide services primarily to meet demand from their home country to the country of final destination. These paragraphs preclude the carriers from carrying excessive fifth and sixth freedom traffic or from operating at "unreasonable" load factors.[22]

The fifth paragraph of Article 10 is the one that varies between those bilaterals that require carriers or governments to agree on capacity levels and those that do not. In the Austrian agreement, "capacity provided ... shall be agreed between the aeronautical authorities of the Contracting Parties, following consultations between the designated airlines ...".

The most liberal capacity article of the fifteen agreements was contained in the Canada-Netherlands bilateral.[23] Paragraph 2 of the agreement states that "appropriate action" should be

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[21] This wording contrasts with the type of wording found in pro-competitive liberal or open skies agreements promoted by the United States and with the wording in the Canada-Netherlands agreement. For example, the pro-competitive agreement between the United States and Canada has a "Fair Competition" article that states:

> Each Party shall allow a fair and equal opportunity for the designated airlines of both Parties to *compete* in providing the international air transportation governed by this Agreement. (emphasis added)

See, Canada, "Air Transport Agreement Between The Government of Canada and The Government of the United States of America", *op. cit.*

[22] Sixth freedom traffic differs from fifth freedom traffic outlined above. Sixth freedom traffic includes those passengers carried from country A to country B with an intermediate stop in country C by a designated carrier of country C.

[23] Canada, "Agreement Between Canada and The Kingdom Of The Netherlands Relating to Air Transport Between Canada and The Netherlands (with Annexes)", *Canada Treaty Series*, 1990, No. 12.

taken to eliminate "all forms of discrimination or unfair competitive practices adversely affecting the competitive position of the airlines of the other Contracting Party". Paragraph 4 states that a designated airline's traffic may *not* be limited or restricted as to "capacity, frequency of service, aircraft type(s), aircraft configuration(s), or rights" by either government or by entities within their jurisdiction.

Capacities are often restricted in the route annexes of Canadian bilateral agreements even if they are not restricted in the body of the bilateral. The bilateral agreement between Canada and Thailand, for example, which does not have restrictive capacity provisions within the main body of the bilateral, specifically outlines permitted capacity levels within the route annex.[24] For example, on the trans-Atlantic route designated to a Thai carrier between Thailand and Canada, the carrier is restricted to three Boeing 747 or four DC 10 flights per week. The designated Canadian carrier is subject to the same restrictions.

Two of the Canadian bilaterals, with Israel[25] and Jordan[26], require commercial agreements among designated carriers on some or all of the routes covered by the agreements.[27] A commercial agreement, sometimes referred to as a "pooling" agreement, differs from a capacity

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[24] Canada, Air Agreement Between the Government of Canada and the Government of the Kingdom of Thailand on Air Services (with Annexes), *Canada Treaty Series*, 1989, No. 16.

[25] Canada, "Air Agreement Between Canada and Israel (with Annex)", *Canada Treaty Series*, 1987, No. 17.

[26] Canada, Agreement Between the Government of Canada and the Government of the Hashemite Kingdom of Jordan on Air Transport (with Annex), *Canada Treaty Series*, 1990, No. 9.

[27] A number of the bilaterals may also have had confidential commercial agreements. As noted above, Donna Mitchell reported that as of 1990, 20 of 60 Canadian agreements had confidential attachments; some of these including commercial agreements. See: Donna Mitchell, *op. cit.*, p. 41.

agreement in that it generally requires a transfer of revenue between carriers. The commercial agreements in the two Canadian bilaterals cover "single track" operations only; single track being when the designated carrier of only one of the two governments operates on a route. The bilaterals require a commercial agreement be in place if a route is to be operated on a single track basis, ostensibly to ensure that the designated carrier not operating on the route also receives some benefits from the service.

As is the case with single designation articles in bilateral agreements, restrictive capacity clauses or commercial agreements may impede the implementation of Canada's new dual designation policy. Certainly, capacity agreements between carriers may have to be re-opened in order to accommodate a second Canadian carrier under the dual designation policy. Re-negotiations over capacity limits may be difficult, given the reluctance of existing carriers to yield flights to potential competitors, especially if they are already operating at the maximum capacity level permitted in the agreement.

V. Tariffs

An important competitive aspect of an international air transport market relates to the ability of an airline to unilaterally establish air fares. The most competitive bilateral agreements have wording in their tariff articles that promote unilateral price-setting and inhibit governmental involvement in the process. An example can be found in the pro forma "post 1977" United States air transport bilateral agreement.[28] Government intervention is limited to the prevention of predatory prices, the protection of consumers from unduly high prices due to the abuse of market power, and the protection of airlines from artificially low prices due to government support or subsidy. In the same vein, paragraph 3 states: "Neither [Governmental] Party shall take unilateral

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[28] Air Transport Association of America, "A U.S. Standard 'Post 1977' Agreement", mimeo, May 15, 1989.

action to prevent the inauguration or continuation of a price proposed ... by an airline of either Party ...". Prices may only be disapproved if *both* governments agree that the prices should not be in effect. This double *disapproval* language contrasts with double *approval* language most commonly found in bilateral agreements, requiring both governments to *approve* a price before it goes into effect.

In their study of bilateral agreements that entered into force between 1978 and 1986, Dresner and Tretheway found that all thirteen agreements contained double approval language.[29] The more recent agreements examined for this paper indicate that double approval remains the norm for Canadian bilateral agreements. All fifteen agreements had double approval wording in the tariff articles. However, two exceptions were made. Annex II of the bilateral agreement between Canada and the United Kingdom contains specific exceptions to the double approval provisions in Article 13.[30] Paragraph 2 of Annex II states that double *dis*approval of fares is allowed if the fares meet the following conditions:

> ... [T]he said tariff is:
>
> (a) at least 60% of the reference level in effect on the date the tariff is filed; or
>
> (b) less than 60% of the reference fare in effect on the date the tariff is filed and subject to each of the following requirements:
>
> (i) a round trip;
> (ii) a minimum stay of at least seven days; and
> (iii) an advance booking of at least seven days ...[31]

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[29] Dresner and Tretheway, "Policy Choices for Canada in International Air Transport", *op. cit.*, p. 89.

[30] Canada, Agreement Between the Government of Canada and the Government of the United Kingdom of Great Britain and Northern Ireland Concerning Air Services, *Canada Treaty Series*, 1988, No. 28.

[31] Appendix B provides some cases when the advance booking requirement can be waived.

The reference fares are set out in Appendix A of the agreement, subject to re-negotiation by the authorities.

The second exception to double approval is contained in the Canada-Netherlands bilateral agreement.[32] Like the Canada-United Kingdom agreement, the Canada-Netherlands bilateral requires double approval of fares except under specified cases. Paragraph 1 of Article XII states the following:

> b) Each designated airline may meet any lawful tariff publicly available from any other airline or charged on charters for air transportation between the territories of the two Contracting Parties.
>
> c) Airlines of each Contracting Party other than designated airlines may meet any publicly available lawful tariff of any designated airline ... on an inter-lining basis over comparable routings ...

Paragraph 9 of the same article states:

> Each designated airline may meet any lawful tariff publicly available for air transportation between the territory of the other Contracting Party and points in third countries over comparable routings ...

In other words, double approval is not required to match competitive fares on routes between Canada and the Netherlands or on routes between Canada or the Netherlands and a third country.

Aside from the issue of governmental approval, a second important component of a tariff clause is the specification of the preferred means for establishing fares. The more liberal agreements affirm that the preferred means of price-setting is to be based on individual carrier

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[32] Canada, "Agreement Between Canada and The Kingdom Of The Netherlands Relating to Air Transport Between Canada and The Netherlands", *op. cit.*, Article XII.

choice and on the carrier's assessment of market conditions. For example, paragraph 1 of the pro forma post 1977 U. S. bilateral agreement clearly states: "Each Party shall allow prices for air transportation to be established by each designated airline based upon commercial considerations in the marketplace".[33] Other, less liberal agreements, state the preferred means of price-setting is by agreement among the designated carriers, or through multilateral tariff coordination, perhaps under the auspices of the International Air Transport Association (IATA). An example of preferred multilateral coordination can be found in Canada's bilateral with Argentina:

> The tariffs ... shall be agreed upon between the designated airlines of the Contracting Parties; such agreement shall be reached, whenever possible, through the rate-setting procedures of the International Air Transport Association.[34]

The preferred means of tariff-setting was examined in the fifteen bilateral agreements entered into force between 1987 and 1993. Five of the agreements specifically mentioned IATA as the preferred forum for establishing prices while three others mentioned the use of an international body or multilateral body as the preferred means for tariff-setting, indicating that a majority of the agreements (53 percent) favor multilateral price-setting. The remaining seven agreements present options to the designated carriers for the preferred price-setting means. The Australian and Saudi Arabian agreements[35] specify mutual agreement among the designated carriers with the option of multilateral coordination as the preferred means. The Jordan

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[33] Air Transport Association of America, *op. cit.*, Article 12, Paragraph 1.

[34] Canada, "Commercial Air Transport Agreement Between the Government of Canada and the Government of the Argentine Republic", *Canada Treaty Series*, 1987, No. 4, Annex Section IV, Paragraph 2.

[35] Canada, "Air Agreement Between Canada and Australia (with Annex), *op. cit.*; Canada, Agreement Between the Government of Canada and the Kingdom of Saudi Arabia on Air Transport (with Annex), *Canada Treaty Series*, 1991, No. 20.

agreement[36] states that tariffs *may* be reached through multilateral coordination. The United Kingdom and Hong Kong bilaterals[37] prefer agreement between the designated carriers with the option of multilateral coordination. Finally, the Austrian and Netherlands agreements[38] specify three preferred options: Tariffs should be set individually by carriers, by mutual agreement among designated carriers, or through multilateral coordination.

The findings on preferred price-setting appear to indicate a movement away from IATA or multilateral coordination as the preferred means for setting prices and a movement towards providing more choices to designated carriers. Dresner and Tretheway[39], in their study of Canadian bilateral agreements signed between January 1978 and April 1986, found that ten of thirteen agreements (77 percent) specified IATA as the preferred means for price-setting and the remaining three (23 percent) specified agreement among designated carriers as the preferred price-setting mechanism. There were no agreements among those studied by Dresner and Tretheway similar to the Austrian and Netherlands bilaterals described above, that specifically mentioned individual carrier choice as a price-setting option. As indicated above, only a bare majority of the recent set of agreements favor (only) multilateral coordination.

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[36] Canada, Agreement Between the Government of Canada and the Government of the Hashemite Kingdom of Jordan on Air Transport (with Annex), *op. cit.*

[37] Canada, "Agreement Between the Government of Canada and the Government of the United Kingdom of Great Britain and Northern Ireland Concerning Air Services", *op. cit.*; Canada, "Air Agreement Between Canada and Hong Kong (with Annex), *Canada Treaty Series*, 1988, No. 16.

[38] Canada, Agreement Between the Government of Canada and the Austrian Federal Government on Air Transport (with Annex), *op. cit.*; Canada, Agreement Between the Government of Canada and the Kingdom of the Netherlands Relating to Air Transport (with Annexes), *op. cit.*

[39] Dresner and Tretheway, "Policy Choices for Canada in International Air Transport", *op. cit.*, p. 89.

Although changes to the tariff clauses in bilateral agreements were not specifically addressed in Canada's new international air policy, it does appear that the movement away from preferred multilateral tariff coordination and towards providing carriers with the option for competitive, market-determined pricing is in keeping with a stated goal of the Canadian policy to ensure Canadians benefit from increased price competition.[40] The same can be said with the decision to allow two exceptions to the double approval policy, in the United Kingdom and Netherlands bilateral agreements. With both of the exceptions, designated carriers were given the latitude to set some international prices without the requiring the approval of both governments, party to the bilateral agreements. In summary, although double approval of tariffs and multilateral price-setting remain key elements of most recent Canadian air bilaterals, there has been a movement away from these restrictive measures to bilateral wording reflecting more market-based price-setting.

VI. Route Schedules

Routes allocated to Canadian carriers and to the carriers of Canada's bilateral partners are outlined in annexes to the bilateral agreements. The route allocations examined for this paper were generally made on the basis of strict reciprocity. If a Canadian carrier is allocated the route: Points in Canada - Intermediate Points - Points in the country of the bilateral partner - Beyond Points; then the bilateral partner carrier is provided a mirror route: Points in the country of the bilateral partner - Intermediate Points - Points in Canada - Beyond Points.[41] If the Canadian carrier is allowed to operate to only one point in the foreign country, then the bilateral partner's carrier is often allowed to operate to only one point in Canada.

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[40] Canada, Transport Canada, "Canada's International Air Transportation Policy", *op. cit.*, p. 4.

[41] See, for example, the route schedule in the bilateral between Canada and Hong Kong; Canada, "Air Agreement Between Canada and Hong Kong (with Annex), *op. cit.*

An exception to the strict reciprocity rule may occur when the foreign country is (geographically) small and contains only one viable international airport, but would like its designated carrier to be permitted to serve more than one Canadian city. For example, in the Canada-Netherlands agreement[42], the designated Dutch carrier is authorized to serve Montreal, Toronto, Halifax, Ottawa, Calgary and Vancouver. While the Canadian carrier may serve Amsterdam plus two other points in the Netherlands, it is unlikely that these other points will ever be served, leaving the Netherlands with seemingly more benefits than Canada. In order to achieve a more equal exchange of benefits, the designated carrier of the Netherlands is limited to two points in the United States, Houston and Orlando, for which it can operate fifth freedom routes from Canada (from Montreal, only). A designated carrier from Canada, on the other hand, has full traffic beyond rights from the Netherlands to other points in Europe, Africa north of the Sahara, the Middle East and Asia.

The bilateral with the Netherlands is, actually, an exception among the agreements studied. It is the only one of the fifteen agreements that does not restrict beyond points to Canadian carriers.[43] Two agreements (with Australia[44] and Saudi Arabia[45]) have no beyond points for designated Canadian carriers, while three others (Hong Kong[46], Brazil[47], and the Ivory

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[42] Canada, "Agreement Between the Government of Canada and the Government of the Kingdom of the Netherlands relating to Air Transport (with Annex), *op. cit.*

[43] If Canada names a second designated carrier to serve routes to the Netherlands, beyond rights for that second carrier are restricted to two points. See *ibid.*

[44] Canada, "Air Agreement Between Canada and Australia (with Annex)", *op. cit.*

[45] Canada, "Agreement Between the Government of Canada and the Government of the Kingdom of Saudi Arabia on Air Transport (with Annex), *op. cit.*

[46] Canada, "Air Agreement Between Canada and Hong Kong (with Annex)", *op. cit.*

Coast[48]) require governmental agreement on beyond points. Two other agreements (Jordan[49] and Austria[50]) provide for no fifth freedom traffic to any beyond points for Canadian carriers. All the other agreements allow a limited number of beyond points for Canadian carriers. Typical of these latter agreements is the Canadian bilateral with Finland.[51] Canadian carriers are limited to a total of four intermediate and beyond points of which no more than two may be beyond points.

The inclusion of fifth freedom routes is important for two reasons. First, a route to a foreign point may not be profitable unless it can be served in combination with another city. For example, a Canadian carrier may only be able to serve Bangkok profitably in combination with service to Tokyo, Singapore or Hong Kong.[52] Second, even if the Canadian carrier does not serve the beyond point, it may want to enter into an alliance with a carrier that does. For example, it may not be profitable for a Canadian carrier to service Moscow itself, but it may be

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47 Canada, "Agreement (and Exchange of Notes) Between the Government of Canada and the Government of the Federative Republic of Brazil on Air Transport (with Annex)", *Canada Treaty Series*, 1990, No. 5.

48 Canada, "Agreement Between the Government of Canada and the Government of the Republic of the Ivory Coast on Air Transport (with Annex and Memorandum of Agreement)", *Canada Treaty Series*, 1990, No. 7.

49 Canada, "Agreement Between the Government of Canada and the Government of the Hashemite Kingdom of Jordan on Air Transport", *op. cit.*

50 Canada, "Agreement Between the Government of Canada and the Austrian Federal Government on Air Transport (with Annex)", *op. cit.*

51 Canada, " Agreement Between the Government of Canada and the Government of Finland for Air Services Between and Beyond their Respective Territories (with Annexes), *Canada Treaty Series*, 1992, No. 4.

52 The new Canadian international policy makes reference to the importance of fifth freedom carriers wishing to serve two international markets on the same flight. The policy recognizes that the fifth freedom rights negotiated in the bilateral agreements often go unused by designated carriers. The policy, therefore, states that "second designated carriers" may apply for unused fifth freedom rights. See, Canada, Transport Canada, "Canada's International Air Transportation Policy", *op. cit.*

profitable for the Canadian carrier to enter into a alliance with a French carrier to transfer Moscow-bound passengers to the French carrier in Paris. Even though the Canadian carrier is not physically serving Moscow, it can sell Canada-Moscow tickets under its own ticket code, if it has the French alliance and if it can legally serve the Paris-Moscow route according to Canada's French and Russian bilaterals. If Moscow is not specified as a beyond point in the French agreement, and Paris is not specified as an intermediate point in the Russian agreement, the Canadian carrier cannot legally sell Canada-Moscow tickets under its own code.

Given the increasing reliance of carriers on international alliances, the limited fifth freedom rights in Canadian bilateral agreements could severely restrict the ability of Canadian carriers to profit from these agreements in the future. It is evident that the Canada-Netherlands model, with unlimited fifth freedom rights for a designated Canadian carrier, best allows Canadian carriers to capitalize on alliance opportunities.

VII. Conclusions

The purpose of this paper was to examine recent Canadian bilateral agreements to determine how well they promote the interest of the traveling public in terms of providing for competitive price-setting and increased international services. These goals were written into Canada's new international air transport policy and form the basis of Canada's recently signed open skies agreement with the United States. Four aspects of Canadian agreements were examined: designation; capacity and commercial clauses; tariffs; and, route rights. Key findings from the study were as follows (see Table 2):

- Seven of the 15 agreements that entered into force between 1987 and 1993 allowed for dual or multiple designation (47 percent) compared to only 5 of 13 (39 percent) signed between 1978 and 1986, reflecting a movement towards allowing more carriers to compete on Canadian international routes. However, the competitive benefits from multiple designation

clauses were negated in some of the bilaterals by designation restrictions in route annexes, effectively limiting the number of designated carriers to one per country.

- A large majority of recent Canadian bilaterals (73 percent) required either carrier or governmental agreement on capacity levels, compared to only 54 percent of agreements signed between 1978 and 1986. The bilateral with the Netherlands, however, contained wording that strictly limited the right of governments to restrict capacity levels. Two of the fifteen agreements studied required commercial agreements for single-track operations.
- All of the recent Canadian agreements require both governments to approve tariffs, with two specific exemptions, one in the agreement with the Netherlands and the other in the United Kingdom bilateral. There were no exceptions to the double approval rule in the group of bilaterals signed between 1978 and 1986.
- Although a majority of the recent Canadian agreements stated that a multilateral forum is the preferred means for price-setting, there has been an increase in the percentage of agreements that provide for preferred price-setting options, including price-setting by individual carriers.
- All but one of the recent Canadian agreements limited or prohibited fifth freedom traffic by Canadian carriers. These limitations and restrictions could impede the ability of Canadian carriers to operate routes profitably either unilaterally or jointly with an alliance partner.

In summary, compared to the Canada-United States open skies agreement, Canadian overseas bilaterals, in general, do not promote competitive pricing and services on Canadian international routes, although there has been some movement towards more competitive pricing and designation arrangements. The vast majority of recent agreements contain designation, capacity, pricing and/or route restrictions that act to severely limit competitive pricing and service outcomes. Clearly, the agreements fall short of the more pro-competitive goals of the new Canadian international air policy.

Table 1
Canadian Air Transport Bilateral Agreements: 1987-1993

Country	Date in Force Definitively	Canada Treaty Series Number
Argentina	February 6, 1987	1987 (4)
Israel	March 24, 1987	1987 (17)
Greece	June 24, 1987	1987 (11)
United Kingdom	June 22, 1988	1988 (28)
Hong Kong	June 24, 1988	1988 (16)
Thailand	June 30, 1989	1989 (16)
Australia	July 5, 1988	1988 (2)
Republic of Korea	September 20, 1989	1989 (50)
Netherlands	February 1, 1990	1990 (12)
Ivory Coast	April 23, 1990	1990 (7)
Jordan	May 10, 1990	1990 (9)
Brazil	July 26, 1990	1990 (5)
Saudi Arabia	June 9, 1991	1991 (20)
Finland	February 21, 1992	1992 (4)
Austria	September 1, 1993	1993 (19)

Table 2
Characteristics of Canadian Bilateral Agreements, 1987-1993

Country	Designation	Required Capacity Agreement	Preferred Price Setting	Fifth Freedom Beyond Routes
Argentina	Single	Yes	IATA	Limited
Israel	Single	No	IATA	Limited
Greece	Single	Yes	IATA	Limited
United Kingdom	Multiple	No	Individual Airline or Airline Agreement	Limited
Hong Kong	Multiple	Yes	Individual Airline or Airline Agreement	With Government Agreement
Thailand	Single	No	Multilateral	Limited
Australia	Multiple	Yes	Airline Agreement or Multilateral	None
Republic of Korea	Single	Yes	IATA	Limited
Netherlands	Multiple	No	Individual, Airline Agreement, or Multilateral	Unlimited
Ivory Coast	Single	Yes	Multilateral	With Government Agreement
Jordan	Multiple	Yes	Airline's Option	None
Brazil	Dual	Yes	IATA	With Government Agreement
Finland	Multiple	Yes	Multilateral	Limited
Austria	Multiple	Yes	Individual, Airline Agreement, or Multilateral	None