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LIBERALIZATION OF RESTRICTIONS ON FOREIGN OWNERSHIP IN U.S. AIR CARRIERS: THE UNITED STATES MUST TAKE THE FIRST STEP IN AVIATION GLOBALIZATION

DAVID T. ARlington

I. INTRODUCTION

THE ORIGINAL proposal of British Airways (BA) to purchase a substantial portion of USAir would have required the Department of Transportation (DOT) to make a decision that would greatly affect international air transportation for many years to come. However, on December 22, 1992, BA decided to withdraw its original offer in the face of almost certain rejection by the DOT.

1 In 1992, USAir originally agreed to sell BA a 44% share of the common equity in the airline in return for a payment of $750 million in cash. James T. McKenna, USAir-BA Pact Will Spark New Transatlantic Battle, AVIATION WK. & SPACE TECH., July 27, 1992, at 26. The deal also provided that BA would hold four seats on USAir's board of directors, which would have been increased from 13 to 16 members, and all key decisions by the USAir board of directors would have to have been approved by a super majority of 80% of the entire board. Id.; Paula Dwyer et al., Air Raid: British Air's Bold Global Push, Bus. WK., Aug. 24, 1992, at 54, 60; see also infra notes 138-57 and accompanying text (discussing in depth the original agreement between BA and USAir).

2 In fact, opponents to the original BA-USAir pact termed the possible DOT decision in that case "[t]he most monumental policy decision since domestic deregulation." American Airlines et al., An Issue of National Policy, Competition and Fairness: The Case Against the British Airways Takeover of USAir, (Aug. 20, 1992) (unpublished position paper, on file with American Airlines, Corporate Communications Department).


BA and USAir later completed a revised investment agreement calling for less controversial levels of voting stock ownership and actual control. Robert L. Rose & Brian Coleman, British Airways Buys Stake in USAir, Drawing Protests from Other Carriers, WALL ST. J., Jan. 22, 1993, at A3. The revised deal calls for a much
One might think that the citizenship requirement of the Federal Aviation Act of 1958, which restricts the level of ownership that a foreign entity may have in a U.S. air carrier, would have been a legal barrier to the proposed BA-USAir alliance. The true cause of the demise of the original smaller ($300 million) investment by BA giving the foreign carrier 19.9% of USAir's voting stock and 24.6% of its total equity. Id. The new agreement eliminated the super majority requirement and gave BA only three seats on USAir's 16 member board. Id. The agreement does, however, provide BA with the option of investing a total of $450 million more into the U.S. carrier. Id. Of course such increased investment would only come in the event that the government liberalizes the citizenship requirement. Id.

In order to implement the first phase of the newly structured alliance, two specific aspects of the deal had to first be approved. Id. First was a provision calling for some code sharing between BA and USAir so that the former could feed USAir's domestic passengers into its own international flights. Id.; see also In re USAir and British Airways D.O.T. Order No. 93-3-17, 1993 WL 75439, *6 (Mar. 15, 1993) (approving of code-sharing arrangements between BA and USAir). The other provision that required approval was the provision calling for BA to rent three USAir planes and crews to fly routes between London and several U.S. cities. Rose & Coleman, supra at A3. Robert Crandall, president of American Airlines, stated that American Airlines "vigorously oppose[d] any attempt to integrate the operations" of the two airlines "whether by code-sharing or any other means." Id. The DOT, however, resisted such opposition and approved both of these aspects of the new deal. See D.O.T. Order No. 93-3-17, 1993 WL 75439 (approving of code-sharing and wet leasing agreements between the two airlines).

It should also be mentioned that the DOT is planning to continue evaluating the citizenship status of USAir after the investment by BA. See id. at *13-14. The DOT already approved of the first phase of the agreement. Id. at *3. However, it has instituted proceedings and called for public comment on the likely status of USAir's citizenship after the second and third phases of the agreement are engaged. See id. at *13-14. As of the date of this publication, the DOT had not yet made a determination.

The DOT has the authority to conduct continuing fitness investigations to
nal deal, however, was actually a conglomeration of many factors having very little to do with the law itself. This analysis clearly demonstrates that the citizenship requirement of the Federal Aviation Act of 1958 is archaic and therefore must be liberalized and adapted to the new world economy if U.S. air carriers are going to survive in the upcoming world of global competition.

Since the deregulation of the airline industry in 1978, U.S. airlines have been struggling to stay in business and if they are fortunate, to maintain profitability. Airlines have consistently reported losses of millions and, in some cases billions of dollars, and are having to find ways to determine if a U.S. carrier in fact remains a U.S. citizen once it has been determined to be such. 49 U.S.C. app. § 1371(r). Under § 204.4 of the DOT's Economic Regulations, carriers undergoing substantial changes in operations are required to provide the DOT with information relevant to their operations. 14 C.F.R. § 204.4 (1992); see also In re Acquisition of Northwest Airlines, Inc., D.O.T. Order No. 89-9-51, at 1 (Sept. 29, 1989) (stating that the DOT considers significant changes in ownership, such as those which would have occurred with USAir, to constitute a substantial change in operations).

See infra notes 268-306 and accompanying text (discussing the failure to liberalize the air services agreement between the U.S. and Great Britain as the most important factor causing the original alliance to go awry).


USAir Group, the parent company of USAir, reported a 1992 net loss of $1.23 billion. Losses for Three Largest U.S. Airlines Approach $2.5 Billion in 1992, AIRPORTS, Feb. 2, 1993, at 46. The airline stated, however, that the majority of this loss could be attributed to a $982 million charge because of a retiree benefits accounting change. Id. Furthermore, UAL, the parent company for United Airlines reported a 1992 net loss of $956.8 million. Id. This figure is nearly 3 times United's 1991 net loss of $331.9 million. Id. Delta also reported a 1992 net loss of $564.8 million that almost doubles the airline's net loss of $239.5 million in 1991. Id. Finally, AMR Corp., parent of American Airlines, reported a 1992 net loss of $935 million which exceeded 4 times its 1991 net loss of $240 million. Id. Additionally AMR and UAL both stated that a large portion of their losses also resulted from "one-time" charges because of a new accounting standard relating to retiree benefits. Id.

After the second-quarter of 1993, it appeared that the airlines were on at least a
cut costs, including massive lay offs and reduction of air services to many marginally profitable destinations. Fare wars during the summer of 1992, typically the airline industry's most profitable season, caused most airlines to report big losses. Furthermore, the end does not appear to be in sight. In fact, one analyst predicted that fare wars will continue during 1993, and that therefore, the airline industry as a whole will not become profitable until at least the end of this year.

The deregulation of the U.S. airline industry, as well as that of the European Community (EC) has also sparked the beginning of airline globalization. As a result, airlines all over the world are joining forces in the hopes of...
being able to compete in the new world market which analysts say is coming within the next ten years. This new market is predicted to consist of only a few mega worldwide airlines that will provide service to all important points of destination.

Extreme limitations on foreign ownership in U.S. carriers, such as those imposed by the Federal Aviation Act of 1958, will inhibit the ability of U.S. airlines to compete. The United States airline industry is virtually unable to profit from its endeavors in the United States. Thus, it is unlikely that U.S. carriers are in a position to globalize alone. The current limitations will also inhibit globalization of the international airline industry as a whole. The United States market is the largest domestic market in the world and is essential to the effort of any foreign air car-

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18 Id. at 28.
19 Id.
20 USAir, The Case For the British Airways Investment in USAir, at 9 (Aug. 28, 1992) (unpublished position paper, on file with USAir, Corporate Communications Department). USAir stated that one of the primary reasons why the DOT should have approved the BA-USAir pact was to promote competition as it was intended to take place under the Airline Deregulation Act. Id. at 5; see also Airline Deregulation Act of 1978, 49 U.S.C. app. § 1302(a)(3), (7)(A) (stating that the act will promote reliance on competition and the prevention of anticompetitive practices). USAir stated specifically:

The only dangerous precedent which could result from this transaction is disapproval. Disapproval would close the door on the only remaining source of capital for U.S.-flag airlines other than the Big Three. It would be a signal that the marketplace can only work if the special interests of American, Delta and United are not threatened by the specter of competition. It would tell other nations that airline deregulation, to borrow from the Big Three, is more a myth than reality and invite a reaction of protectionism. USAir is not asking for affirmative relief. It is not seeking special treatment or federal support. It has only one message: let the marketplace work for USAir as it has worked for American, Delta and United.

USAir, supra, at 9.

21 See Tom Incantalupo, Re-Regulation of Airlines? American's Chairman Says Issue is Sure to Come Up in '93, NEWSDAY, Dec. 17, 1992, at 53. In fact, U.S. carriers have lost approximately $7.5 billion as a whole over the past three years. Id. This figure includes the approximate $2 billion dollars which the airlines lost in 1992, partially as a result of brutal fare wars during the summer season. David Field, Airlines Big Losers in 1992's Fare Wars; Consumers Profited from Many Specials, WASH. TIMES, Dec. 9, 1992, at C1.
rier to provide worldwide air service. Finally, and most importantly, the recent United States insistence on open access to foreign markets before it will liberalize the archaic foreign ownership limitations in U.S. carriers will likely spark protectionist sentiments in countries around the world, thereby preventing market access that is essential to globalization of any airline.

This Comment emphasizes the importance of the liberalization of the citizenship requirement of the 1958 Act as a first step in the process of airline globalization. If the United States decides to participate in world aviation, its laws must keep pace with this policy as well as with the world economy. This Comment begins with a brief discussion of the history of the citizenship requirement in the 1958 Act. Second, it addresses the Civil Aeronautics Board (CAB) and DOT interpretations of this requirement, focusing on the most recent decisions in the area. Third, it discusses the many policy arguments both for and against the original BA-USAir alliance. Fourth, it analyzes the failure of the original alliance, focusing on the roles the 1958 Act and current bilateral issues between the U.S. and the U.K. may have played in that failure. Finally, the Comment discusses the DOT's recent proposal for open skies agreements with European coun-

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22 The failure of the original BA-USAir alliance was viewed as a setback for BA's global plans. Richard W. Stevenson, British Air Halts Plan to Purchase Big Stake in USAir, N.Y. TIMES, Late Ed., Dec. 23, 1992, at A1. Analysts confirmed that for BA to have the global airline it envisions, the U.S. must be a part of its market, and, therefore, BA would not let this setback prevent its effort to achieve some type of alliance with a U.S. carrier. Julie Schmit, USAir Deal in Trouble?, USA TODAY, Dec. 18, 1992, at 2B. After all, the United States domestic airline market constitutes 40% of the whole world market. Richard M. Weintraub, Leveraging An Airline Linkup: U.S. Prepared to Block USAir Deal Unless Britain Opens Market, WASH. TIMES, Dec. 18, 1992, at B9 [hereinafter Leveraging An Airline Linkup]. In fact, BA did not allow this setback to hinder its efforts. See Rose & Coleman, supra note 3, at A3. On January 21, 1993, BA and USAir agreed to a smaller scale alliance that will eventually give BA the option to increase its investment to the originally proposed levels. Id.

23 See, e.g., Bill Poling, France Gives Up Pact with U.S., but Air Services Will Continue; Commercial Aviation Brief Article, TRAVEL WKLY., May 7, 1992, at 39 [hereinafter France Gives Up Pact]; see also infra notes 276-90 and accompanying text (discussing the DOT’s insistence on open skies agreements as a condition for liberalization).
tries and suggests the first step that the United States must take to make true global aviation a reality.

II. ORIGINS OF THE CURRENT CITIZENSHIP REQUIREMENT

A. AIR COMMERCE ACT OF 1926

The Air Commerce Act of 1926 contained the first enacted limitation on foreign ownership of U.S. carriers. The 1926 Act defined a citizen of the United States as an individual who is a U.S. citizen, a partnership composed only of U.S. citizens, or a corporation that was organized in the United States and that fulfilled two further requirements: (1) two-thirds of its board of directors had to be U.S. citizens, and (2) U.S. citizens had to own fifty-one percent of its voting stock. The focus of this discussion will be on the corporate form of ownership.

1. National Security Concerns

In order to understand one of the major arguments that critics later used to attack the original alliance between BA and USAir, it is necessary to discuss the role that national security policy played in the enactment of the citizenship requirement of the 1926 Act. With World War I still fresh in the political arena, concern with the country's security during wartime was pervasive. The primary concern was that U.S. owned aircraft should be available during time of war to serve as an auxiliary air force fleet. The pilots of these aircraft would also serve

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25 Id. § 9(a), 44 Stat. at 573.
26 Id.
27 See, e.g., infra notes 177-81 (discussing national security concerns with regard to the BA-USAir alliance).
28 See Gjerset, supra note 8, at 180-82 (discussing in depth the national security concern and its relation to the citizenship requirement).
30 H.R. REP. No. 1262, 68th Cong., 2d Sess. 2 (1925); see also Stewart, supra note
as auxiliary personnel during wartime.\textsuperscript{31}

To ensure that such aircraft and personnel would be available in the event of an emergency situation, Congress made it clear in a 1925 House Report dealing with the issue of the citizenship requirement that all “[r]egistered aircraft of the United States will serve as an auxiliary air force in time of war.”\textsuperscript{32} The House stated that U.S. citizens should therefore control such aircraft so that the government would have easy access to the fleet in a time of need.\textsuperscript{33} In that report, the House went on to say:

The Secretary of Commerce and representatives of the Secretary of War and Secretary of the Navy agreed that it was desirable, in the case of corporate owners, that at least 75 per cent of interest in the corporation should be held by citizens of the United States, for the reason that corporations created under our laws, but in fact foreign controlled, should not be able to possess craft that fly the United States flag and [craft that] should be a part of our air-fleet auxiliary in time of war.\textsuperscript{34}

Thus were the beginnings of the relationship between the concern for national security and the citizenship requirement contained in the Air Commerce Act of 1926.\textsuperscript{35} When the requirement was finally enacted with the 1926 Act, however, the requirement for corporations was that U.S. citizens hold only fifty-one percent of the carrier’s voting interest.\textsuperscript{36}

2. \textit{Fostering and Protecting the Airline Industry}

The 1926 Act itself was the federal government’s first attempt to regulate the airline industry in the United States.\textsuperscript{37} Although foreign ownership warranted sufficient

\textsuperscript{29}, at 694-95 (discussing the citizenship requirements of those who own such aircraft).
\textsuperscript{32} Id.
\textsuperscript{33} Id. at 26.
\textsuperscript{34} Id.
\textsuperscript{35} Pub. L. No. 69-254, § 9(a), 44 Stat. at 573 (1926).
\textsuperscript{36} Id.
\textsuperscript{37} Stewart, \textit{supra} note 29, at 690.
concern to include it in the 1926 Act, the primary motivation for the regulation of the airline industry as a whole came as a result of the chaotic state of the industry after World War I.\textsuperscript{38} After the war, the airline manufacturing industry had grown to unprecedented levels that the private aviation industry as it stood could not sustain.\textsuperscript{39} Furthermore, those within the airline industry recognized that airline transportation would likely not be successful if the federal government did not step in to foster its development as it had done with the automobile and shipping industries.\textsuperscript{40}

This idea of government regulation with the purpose of fostering development of the airline industry is important in the discussion of the citizenship requirement. One of the primary reasons behind the enactment of the 1926 Act and the citizenship requirement was the "encouragement and protection of civil air navigation."\textsuperscript{41} This policy became even more evident just before the Civil Aeronautics Act of 1938\textsuperscript{42} passed when proponents of the protectionist position called for the government to provide economic support for U.S. carriers who were competing with


\textsuperscript{39} Id. at 11-12. With World War I over, there was a surplus of pilots as well as aircraft on the market. Id. This encouraged former military pilots to buy the airplanes at rock bottom prices and to make a living providing transportation and entertainment to the public. Id. at 12. This situation, however, led to airplanes which were unfit to fly and a general chaos in the unregulated skies. Id. at 7-9. Furthermore, the flood of the aircraft on the market had a devastating effect on the aircraft manufacturing industry. Id. at 12.

\textsuperscript{40} Komons, supra note 38, at 7-9. In fact, the framework and language of the Air Commerce Act of 1926 were in many cases just applications to aviation law of that which had long been a part of the law relating to water transportation. H.R. Rep. No. 1262, 68th Cong., 2d Sess. 2 (1925). The citizenship requirement for corporate owners of aircraft and airlines was modeled after the Shipping Act of 1916. Id. at 6; see Shipping Act of 1916, Pub. L. No. 64-260, § 2, 39 Stat. 728, 729 (1916) (current version codified at 46 U.S.C. § 802(a) (1988)); see also Stewart, supra note 29, at 693-96 (discussing the role of maritime precedent on the Air Commerce Act of 1926 and its continuing influence on aviation law).


\textsuperscript{42} Ch. 601, Pub. L. No. 75-706, 52 Stat. 973 (1938).
foreign carriers in foreign commerce.43

B. CIVIL AERONAUTICS ACT OF 1938 THROUGH FEDERAL AVIATION ACT OF 1958

During the 1930’s, the United States began to reevaluate its international trade policy as a whole.44 The nation had just suffered through the Great Depression and “[p]olicy-makers [began to shift] their economic position from advocating the classical theory of free trade to heavy reliance on governmental intervention.”45 Thus, even stronger cries came to protect and maintain control over the airline industry.46

Continuing to reflect these concerns for protectionism and also the security of the nation, the Civil Aeronautics Act of 193847 accordingly contained an even more restrictive citizenship requirement for U.S. carriers.48 The Act, instead of requiring U.S. citizens to own only fifty-one percent of the voting stock of U.S. air carriers, actually required seventy-five percent ownership.49

This version of the citizenship requirement contained in the 1938 Act survived virtually unchanged and became incorporated into the Federal Aviation Act of 1958.50 The citizenship requirement of the 1958 Act has continued in effect even until today unchanged, at least as far as the written law is concerned.51

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43 See Gjerset, supra note 8, at 183 (citing Aviation: Hearing on H.R. 4652 Before the Comm. on Interstate and Foreign Commerce, 75th Cong., 1st Sess. 72 (1937)).
44 Id. at 182.
45 Id. (citations omitted).
46 Id. at 183-84.
48 Id. § 1(13), 52 Stat. 978.
49 Id.
51 Id. Although the written law has remained unchanged since the 1938 Act, the CAB and the DOT have approached cases involving the citizenship issue on a case by case basis extending the letter of the law to include an actual control test above and beyond the written law itself. See In re Acquisition of Northwest Airlines, Inc., D.O.T. Order No. 89-9-51, at 4-5 (Sept. 29, 1989); see also infra part III (discussing CAB and DOT applications of this actual control test).
III. INTERPRETATION OF THE CITIZENSHIP REQUIREMENT BY THE CAB AND DOT: A LONG HISTORY OF STRICT CONSTRUCTION

So far this discussion has focused on what the citizenship requirement of the Federal Aviation Act of 1958 specifically and explicitly requires. However, the more important aspect is how the CAB and the DOT, the bodies empowered with the authority to decide if particular airlines are complying with the requirement, have interpreted the rule over the years. The following section analyzes the earliest decisions of the CAB regarding the citizenship issue as well as the most recent decisions of the DOT.

A. TRADITIONAL STRICT INTERPRETATION AND IMPOSITION OF THE ACTUAL CONTROL TEST

Traditionally, the CAB and DOT have interpreted the citizenship requirement very strictly, requiring first that the airline in question satisfy the letter of the statute itself. This means U.S. citizens must own seventy-five percent of the stock of the airline. The CAB and DOT have adhered to this interpretation for many years, ensuring that only U.S. citizens are involved in the ownership of airlines.

52 See supra note 5 (quoting the language of the citizenship requirement).
53 The CAB, created under the name "Civil Aeronautics Authority," was originally established under § 201(a) of the Civil Aeronautics Act of 1938. Pub. L. No. 75-706, § 201(a), 52 Stat. 973, 980-81 (1938). The Authority was given power to issue certificates of public convenience and necessity which an air carrier was and still is required to obtain before engaging in any air transportation. Id. § 401(a), 52 Stat. at 987 (current version codified at 49 U.S.C. app. § 1371(a) (1988)). The 1938 Act as well as current law required that such a carrier "must be fit, willing, and able to perform such transportation properly" and must conform to the provisions of the 1958 Act, which include the citizenship requirement. Id. § 401(d)(1), 52 Stat. at 987; see also id. § 101(13), 52 Stat. 978 (stating the definition of a U.S. citizen); 49 U.S.C. app. § 1371(d)(1) (1988) (current version requiring air carriers to conform with all provisions of the 1958 Act). The 1958 Act continued the existence of the Authority, but under the name of the Civil Aeronautics Board. Federal Aviation Act of 1958, Pub. L. No. 85-726, § 201(a), 72 Stat. 731 (1958). The power of the CAB, however, was terminated by the Airline Deregulation Act of 1978, Pub. L. No. 95-504, § 40(a), 92 Stat. 1705, 1744 (1978) (codified at 49 U.S.C. app. § 1551(a) (1988)). At the same time, this power was transferred to the DOT. Id. § 40(a), 92 Stat. 1745 (codified at 49 U.S.C. app. § 1551(b) (1988)).
percent of the airline’s voting stock and that two-thirds of the members of the airline’s board of directors or other managing officers must be U.S. citizens. There is, however, a second part of the citizenship requirement that the statute does not clearly state: The requirement that a non-U.S. citizen cannot actually control the airline.

1. Earliest Interpretations through Daetwyler

The CAB set forth this actual control test early on in a 1940 decision. The CAB and DOT have restated the test many times over the years, and it is clearly still in effect today. One of the most widely cited decisions by the DOT, which thoroughly discusses and applies the actual control test, is Wilby Peter Daetwyler, D.B.A. Interamerican Airfreight Co., Foreign Permit. That case involved the application of Interamerican Airfreight Corporation (Interamerican) requesting that the Board grant the company an operating authorization as a U.S. citizen international airfreight forwarder under part 297 of the Board’s Economic Regulations.

The CAB stated that the issue in that case was “whether Interamerican qualifies as a ‘citizen of the United States’ pursuant to section [101(16)] of the Federal Aviation

55 Id.; see also supra note 5 (citing the actual language of the citizenship requirement as set forth in modern version of the 1958 Act).


57 Id. In that decision, the CAB stated:

[t]he apparent general intent of the statute is to insure that air carriers receiving economic support from the United States and seeking certificates of public convenience and necessity, under section 401 of the Act shall be citizens of the United States in fact, in purpose and in management. The shadow of substantial foreign influence may not exist.

Id. at 337 (emphasis added).

58 See In re Discovery Airways, Inc., D.O.T. Order No. 89-12-41, at 10 (Dec. 21, 1989); In re Acquisition of Northwest Airlines, Inc., D.O.T. Order No. 89-9-51, at 4 (Sept. 29, 1989); In re Intera Arctic Serv., Inc., D.O.T. Order No. 87-8-43, at 5 (Aug. 18, 1987); In re Page Avjet Corp., C.A.B. Order No. 83-7-5, at 2 (July 1, 1983); Premiere Airlines, Fitness Investigation, C.A.B. Order No. 82-5-11, at 103 (May 5, 1982); Daetwyler, 58 C.A.B. at 119.


Act." There was no question that U.S. citizens owned seventy-five percent of the voting stock of Interamerican or that two-thirds of its board of directors consisted of U.S. citizens. The question was whether Daetwyler, a non-U.S. citizen of Swiss nationality and twenty-five percent stockholder, exhibited actual control over the airline. The CAB found that in fact he did. Although Interamerican met the "bare minimum" standards of the citizenship requirement, the CAB focused on both the close personal relationships between Daetwyler and the other stockholders of Interamerican and the fact that many of those same stockholders were actually employees of other Daetwyler-owned companies. As a result of Daetwyler's actual control over Interamerican, the CAB found that the airline did not qualify as a U.S. citizen and therefore did not meet the requirements of a U.S. citizen airfreight forwarder under the Board's regulations.

2. Premiere

The CAB once again addressed the issue of actual control in *Premiere Airlines, Fitness Investigation*. This case involved Premiere Airlines' (Premiere) application for a certificate to engage in scheduled interstate air transportation. Such a certificate required that Premiere be fit, willing, and able to perform the services in question and

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61 Daetwyler, 58 C.A.B. at 119 (citation omitted).
62 Id.
63 Id.
64 Id. at 120.
65 Id. at 121.
66 Id. at 120-21. In making this finding, the CAB argued that the intent of Congress in enacting the citizenship requirement was to "insure that air carriers issued licenses by the United States as U.S. carriers would be owned and controlled by citizens of the United States." Id. (citations omitted) (emphasis added). The Board insisted that the notion that Congress might have intended the phrase to be read disjunctively, in other words, owned or controlled, was completely illogical and would totally undermine the purpose of the citizenship requirement. Id. at 121. Under such a reading, the Board stated, Interamerican could clearly be deemed a U.S. citizen despite the fact that it is subject to extensive if not complete foreign control. Id.
67 C.A.B. Order No. 82-5-11 (May 5, 1982). The Board stated that "as a factual matter, the carrier must actually be controlled by U.S. citizens." Id. at 103.
to comply with the Act and any other applicable rules or regulations. The more important requirement in relation to this discussion was that Premiere be a U.S. citizen as defined in the 1958 Act.68

Originally an administrative law judge who examined the case recommended to the CAB that Premiere had failed to establish that it was a U.S. citizen pursuant to section 101(16) of the 1958 Act.69 The problem as determined by the judge was that Joseph Cicippio, a co-founder of Premiere, had borrowed $2.5 million from his Saudi Arabian employer to invest in the venture.70 The judge found that Cicippio, as a result of this loan, was under the control of his Saudi Arabian employer and that the latter had a substantial interest in the successful operation of the airline.71

Despite this clear control by a non-U.S. citizen, the CAB agreed to stay its final decision on the issue of Premiere's citizenship status72 and allowed Premiere the opportunity to reorganize with the hope that such a restructuring would eliminate the CAB's concern over foreign control.73 In reconsidering Premiere's application, the CAB once again focused on the issue of actual control in determining citizenship.74 As in Daetwyler, the CAB stated that there had never been any question that

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68 Id. at 101-02; see supra note 5 (quoting the exact language of the citizenship requirement).
69 C.A.B. Order No. 82-5-11, at 102.
70 Id.
71 Id.
73 C.A.B. Order No. 82-5-11, at 102. The CAB stated:
[T]he applicant reorganized itself to nullify any control the Sheikh may exercise through Mr. Cicippio. According to [the administrative law judge], it took the following steps: (1) Mr. Cicippio resigned from the applicant's management and board of directors; (2) Mr. Cicippio's voting interest in the applicant has been transferred to an independent third-party voting trustee, the Bank of America; (3) a new senior financial officer has been hired to replace Mr. Cicippio; and (4) Premier [sic] will pursue equity capital from sources other than Mr. Cicippio and the Sheikh.
74 Id. at 103.
Premiere met the statutory requirements that U.S. citizens own seventy-five percent of its voting stock and that at least two-thirds of its board of directors or other managing officers be U.S. citizens.\textsuperscript{75} The CAB agreed with the administrative law judge that after Premiere's reorganization, the airline had successfully stripped Cicippio of his control over the airline and had thus eliminated any concerns over actual control which the CAB may have had.\textsuperscript{76}

3. \textit{Page Avjet}

Following the \textit{Premiere} decision, the CAB again addressed the issue of foreign control in \textit{In re Page Avjet}.\textsuperscript{77} For a brief period it appeared that the CAB, through this decision, had begun to liberalize its past strict interpretation of the citizenship requirement.\textsuperscript{78} However, as will be discussed, this apparent liberalization was short lived.\textsuperscript{79}

\textsuperscript{75} Id.
\textsuperscript{76} Id. In an attempt to strictly monitor Premiere's citizenship status, the CAB imposed the following condition in Premiere's certificate:

\textbf{(4)} Prior to the inauguration of service under this certificate and thereafter, on August 10th and February 10th of each year, the holder shall file with the Director of the Bureau of Domestic Aviation a report, in narrative form, describing any changes in its officers or directors and a current financial statement which includes the identification of all persons who hold more than five percent of its equity and the amount held by each. The report shall include the citizenship and residence of all creditors holding in excess of five percent of the total outstanding debt. If any debt or equity interest in excess of five percent is held directly or indirectly on behalf of some other person, the report shall include the citizenship and residence of the beneficial owner together with the full text of any written agreement or a summary of any oral agreement between the parties pertaining to such interest; \textit{provided} that this requirement will be terminated upon Board approval of the termination of the Voting Trust Agreement dated as of December 16, 1981 entered into by and between Mr. Joseph J. Cicippio and Bank of America NT & SA as voting trustee, unless the board determines at that time that the public interest requires continuation of this reporting requirement.

\textit{Id.} at 106.
\textsuperscript{77} C.A.B. Order No. 83-7-5, at 5 (July 1, 1983); C.A.B. Order No. 84-8-12 (Aug. 2, 1984).
\textsuperscript{78} See C.A.B. Order No. 84-8-12, at 2 (allowing airline to maintain its citizenship status despite the appearance of foreign control through a buy-out provision).
\textsuperscript{79} See \textit{In re} Intera Arctic Services, Inc., D.O.T. Order No. 87-8-43, at 11 (Aug. 18, 1987) (stating that the decision in \textit{Page Avjet} constitutes the outer limits of the
In the Page Avjet case, the CAB first applied its strict interpretation of the actual control test and determined that U.S. citizens did not actually control the carrier. To the contrary, the CAB stated that the nonvoting stockholders in Page Avjet (Page), who were not U.S. citizens, actually had power to control the airline. The CAB supported its determination by pointing out the specific methods of control that the nonvoting stockholders had:

In Page's proposal, the nonvoting stockholders do not have day to day operational control; however, they have the right to influence many of the crucial decisions of the company. They have the power to block any proposal by the voting stockholders for a company consolidation, merger or acquisition. Similarly, they have the power to dissolve the company and liquidate its assets. If the nonvoting stockholders disapprove of the way that the officers and director conduct the company's affairs, they can vote for dissolution of the company.

The CAB concluded by saying that considering the level of power of the nonvoting stockholders, it was clear that the officers of the company would follow their wishes.

The CAB, however, agreed to give Page the opportunity to restructure its ownership in the hopes of obtaining citizenship status under the Act. In restructuring the organization, Page submitted a plan that called for the creation of a new corporation that would have two classes of stockholders. The plan stated that Page would own one class of stock which would be nonvoting common stock. The second class of stock would be owned by U.S. citizens and this class would be voting preferred stock. One of the more interesting aspects of this plan was that it contained a buy-out provision which stated that if certain events

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citizenship requirement); see also Stewart, supra note 29, at 709 (questioning the validity of the Page Avjet decision).

80 C.A.B. Order No. 83-7-5, at 5.
81 Id. at 3.
82 Id. at 4 (citations omitted).
83 Id.
84 Id. at 5.
were to occur, U.S. citizen stockholders would agree to purchase Page's nonvoting stock owned by foreign citizens at its "fair market value."\textsuperscript{85}

The CAB did not elaborate on exactly how it came to its decision, but it determined that effective control no longer rested in the hands of the nonvoting shareholders.\textsuperscript{86} However, the buy-out provision still appeared to restrict the activity of the airline significantly. The conditions of the buy-out provision were sufficiently ambiguous to allow nonvoting, non-U.S. citizen stockholders a significant amount of leverage. The conditions stated that U.S. citizen shareholders agreed to purchase Page's stock in the event of:

1. consolidation, merger or acquisition of control by another entity;
2. sale of its assets other than in the ordinary course of business;
3. issuance of additional stock;
4. "waste" of corporate assets or payment of unreasonable compensation to management or key personnel; or
5. "self dealing" by management or key personnel that may be detrimental to Page's investment.\textsuperscript{87}

The first three conditions were very specific events. The conditions in themselves were quite restrictive and certainly would have influenced management decisions on a regular, if not day to day, basis. More importantly, however, the final two provisions for the U.S. stockholder buy-out (prohibitions against the wasting of corporate assets or payment of unreasonable compensation and against self-dealing by management or key personnel) seemed to leave a great deal of room for interpretation and discretion for the nonvoting stockholders regarding exactly when one of these conditions would be violated.

These provisions seemed to have provided Page with an escape hatch in case they felt that the company was not being run according to its wishes. Thus, to maintain the non-voting stockholder's investment, the company's man-

\textsuperscript{85} C.A.B. Order No. 84-8-12, at 1.
\textsuperscript{86} See id. at 2.
\textsuperscript{87} Id. at 1 n.3.
agement was likely to defer to their requests, and this certainly appeared to be a case of actual control. However, the CAB allowed an apparent relaxation of the actual control test and permitted the airline to maintain its citizenship.88

4. Intera

Nevertheless, in In re Intera Arctic Services,89 the DOT indicated that the apparent liberalization of the interpretation of the citizenship requirement by its predecessor, the CAB, should not concern us for long.90 Specifically, the DOT stated that the Page Avjet case represented the extreme outer limits of the interpretation of the citizenship requirement.91 In making this statement, however, the DOT stated that there were enough significant differences between Page Avjet and Intera to avoid the question of whether the DOT would have decided Page Avjet in the same way as did its predecessor.92

Intera involved a foreign entity's (IT) creation of the company Intera Arctic Services (IAS). This undertaking was an attempt to obtain U.S. citizen status in order to carry out IT's operations in the United States. In creating IAS, IT patterned its structure on what the CAB had recently approved in its Page Avjet decision. Thus, IAS consisted of two classes of stock: "voting preferred, of which no more than 25 percent [was to] be held by non-U.S. citizens; and nonvoting common stock, which [was] held by IT."93 The company's articles of incorporation also required that its president and two-thirds of its board of directors and management officials be U.S. citizens. Furthermore, and more importantly under the actual control analysis, there was a buy-out provision which IAS contended was very similar to that in Page Avjet.

88 See id. at 2.
89 D.O.T. Order No. 87-8-43 (Aug. 18, 1987).
90 Id. at 11.
91 Id.
92 Id.
93 Id. at 6.
In distinguishing *Intera* from the CAB's decision in *Page Avjet*, the DOT noted differences in the buy-out provisions which seemed to leave IT with more effective control in IAS than non-U.S. citizens had in *Page Avjet*. The most significant difference between the cases, according to the DOT, was the total level of ownership which the foreign entity had in the U.S. air carrier. For example, the DOT pointed out that in *Page Avjet* the non-U.S. citizen stockholders "held only about 9% of the issued and outstanding stock of all classes," and therefore, the buy-out provision would not be extremely burdensome on the U.S. citizen shareholders should a buy-out come to pass. In contrast, however, the foreign stockholders in IAS held almost eighty-two percent of the issued and outstanding stock of all classes. Therefore, the DOT concluded that the burden would be much higher on U.S. citizen shareholders than was the case in *Page Avjet*. Thus, foreign citizens had much more influence in *Intera* than such persons had in *Page Avjet*.

Next, the DOT stated the most important reason for

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94 Id. at 11. Specifically, the DOT stated that:

The *Page Avjet* buy-out provision set a price of one-half of the net tangible book value per common share (after allowance for liquidation preference of preferred shares), plus six times earnings per common share. The IAS provision sets a price of full net tangible book value per common share (after allowance for liquidation preference of preferred shares). Thus, in the *Page* situation, the buy-out price would be lower if the company was not profitable and, therefore, an unprofitable company would be better able to afford the necessary payment than it would under the IAS buy-out provision.

95 Id. at 12.

96 Id.

97 Id.

98 See id. The DOT considered the liquidation provision in the agreement between IAS and IT as another indicia of control. Id. The DOT pointed out that the liquidation provisions were "such that the U.S. citizen voting shareholders bear little risk in the event of failure and would reap little reward if the company were dissolved." Id. The DOT stated that instead, the "risks and rewards lie with the non-U.S. citizen owners." Id. In other words, it was clear to the DOT that the person or shareholders who would incur the most risk in the event of a liquidation would clearly have a vested interest in guaranteeing that such a liquidation did not occur; therefore, it is likely that such a party would assert or at least attempt to assert control over the U.S. carrier in order to avoid the liquidation. See id.
deciding against IAS on the actual control test and citizenship question: "Finally, and most importantly, our show cause order found that Messrs. Lantz and Grandia, upon whom IAS relies to establish its citizenship, are key employees of IT and therefore 'ready conduits for the exercise by [IT] of control over IAS, Inc.'" Lantz and Grandia, who were both U.S. citizen directors and management officials of IAS, were also officers of IT, the foreign entity that created IAS. The DOT went on to say:

The fact that these gentlemen are U.S. citizens and major shareholders in IAS's non-U.S. citizen affiliates does not negate foreign control. To the contrary, as major stockholders, they have far more at stake in seeing to it that IT and ITC are successful in carrying out their various activities than a "mere" employer-employee relationship. Thus, we conclude that the potential for foreign influence and control by these gentlemen is far greater than that found to be decisive in Daetwyler, which IAS seeks to distinguish.

The Interar decision sent a vivid message to future applicants that the DOT would scrutinize any case in which the parties have apparently organized themselves in an attempt to meet only the explicit statutory requirements of the 1958 Act and not necessarily the spirit of the law.

5. Northwest I

In September 1989, the DOT handed down yet another decision reinforcing its intolerance for foreign control of U.S. air carriers. In Northwest I the DOT once again focused on the actual control that foreign interests had over Northwest Airlines. In Northwest I, the DOT was con-

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99 Id.
100 Id. at 13 (citation omitted).
101 Id. at 11.
102 In re Acquisition of Northwest Airlines, Inc., D.O.T. Order No. 89-9-51 (Sept. 29, 1989) [hereinafter Northwest I].
103 Id. at 4. As was the case in many of the decisions already set forth in this Comment, the DOT specifically stated that the facts in this case clearly satisfied the letter of the law set forth in § 101(16) of the Federal Aviation Act of 1958. Id.; see 49 U.S.C. app. § 1301(16).
cerned with Koninklijke Luchtvaart Maasschappij (KLM), a Dutch citizen and foreign air carrier. The concern arose out of KLM's ownership of 56.74 percent of the equity in Wings Holdings, Inc. (Wings), a company created for the purpose of purchasing Northwest Airlines. Although KLM claimed it was going to own less than five percent of the voting interest in Northwest, the DOT countered this argument by stating that "it is clear from our precedent that a large share in a carrier's equity poses citizenship problems, even where the interest does not take the form of voting stock, particularly if there are other ties to the foreign entity." The DOT also concluded that due to its lack of voting stock, KLM would have a large incentive to participate in the business of the U.S. airline in a significant way in order to protect its business investment.

The DOT did not, however, rest its decision solely on the high level of equity interest KLM had in Wings (and therefore Northwest). Instead, the DOT examined other links between the two entities and decided that KLM was in a de facto position of control. First of all, KLM was allowed to name one person to the Wings twelve-member board of directors. Second, KLM had the right to organize a three member committee which would advise Northwest in the area of financial affairs. The DOT, in light of this information, concluded that it was likely that KLM would use these methods to control Northwest in a way which would protect the former's $400 million interest.

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104 Northwest I, D.O.T. Order No. 89-9-51, at 6 (citation omitted).
105 Id.
106 Id. at 7.
107 The DOT also pointed out that "[t]here [were] no restrictions on the KLM board member's participation in Northwest's decisionmaking." Id.
108 There were also no limits placed on the advisory committee's authority or scope of advice. Id.
109 Id. at 7. The DOT was also very concerned by the fact that KLM was not simply a foreign citizen but that it was also an air carrier. Id. at 8. The concern becomes much stronger when the foreign carrier in question actually competes in certain routes with the entity it is trying to invest in and control, as such a situation could easily destroy all advantages of competition. Id. The DOT found that
In its decision in *Northwest I*, however, the DOT was not forced to declare that Northwest would no longer be a U.S. citizen. Instead, Northwest and Wings agreed to take steps that substantially eliminated the foreign control concerns of the DOT.\(^{110}\) First, Northwest and KLM agreed to reduce KLM's share of Wing's equity to no more than twenty-five percent within six months from the date of the consent order.\(^{111}\) Until that time, the parties agreed to place KLM's interest that exceeded twenty-five percent into a voting trust free from KLM's control.\(^{112}\) The parties also agreed to eliminate the ability of KLM to create a financial advisory committee to Northwest and that KLM's member of the board of directors would be recused under certain circumstances.\(^{113}\) Finally, Northwest agreed to make reports to the DOT concerning any agreements or change in ownership that might effect the airline's citizenship status.\(^{114}\) Thus, the DOT was able to allow Wings and Northwest to restructure and avoid an adverse decision.\(^{115}\)

6. *Discovery*

Just months after the decision was handed down in the consent order of *Northwest I*, the DOT once again had the opportunity to address the issue of actual control in *In re Discovery Airways, Inc.*\(^{116}\) The DOT in this case, however, focused more on the issue of foreign control over members of the board of directors.\(^{117}\) The Discovery board of directors consisted of seven members, four of whom were alleged to be foreign citizens or controlled by foreign entities. The first member in question, Franco Mancassola,

\(^{110}\) *Id.*

\(^{111}\) *Id.*

\(^{112}\) *Id.*

\(^{113}\) *Id.* at 9.

\(^{114}\) *Id.*

\(^{115}\) *Id.*

\(^{116}\) D.O.T. Order No. 89-12-41, at 10 (Dec. 21, 1989).

\(^{117}\) *Id.* at 10-11.
was an Italian citizen and served as the vice-chairman of the board as well as the board's representative to Discovery's management. The DOT was concerned that Mancassola was essentially serving the function of president and thus ordered his removal from his liaison position.

The other board members in question, Phillip Ho, Daryl H.W. Johnston and Barbara Tanabe were all U.S. citizens. Mr. Ho was also the president of a wholly owned subsidiary of a Japanese company. The DOT felt that Ho's connections with this foreign entity, as well as many other foreign corporations, effectively provided for foreign control over Mr. Ho's actions. Therefore, the DOT called for his removal from the board of directors and for all of his voting stock to be placed in a voting trust. Similarly, because of Mr. Johnston's and Ms. Tanabe's connections with Mr. Ho and the same Japanese company, the DOT also called for their removal in order to completely eliminate that aspect of control.

As the preceding examples illustrate, the DOT and its predecessor, the CAB, have consistently and strictly construed the citizenship requirement in the 1958 Act. The DOT has focused on the actual control element that developed shortly after the passage of the Civil Aeronautics Act of 1938. It has looked closely not only at how investment in carriers allow foreign control, but also how personal relationships between U.S. citizens and foreign entities may provide a more subtle method of influence. As will be discussed, however, if the United States intends to participate in global aviation, Congress and the DOT will have to take the first step by liberalizing both this citizenship requirement and the DOT's corresponding inter-

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118 Id. at 14-15.
120 D.O.T. Order No. 89-12-41, at 13-14.
121 D.O.T. Order No. 90-1-60, at 14.
122 Id.
pretations and applications.\textsuperscript{124}

\textbf{B. APPARENT LIBERALIZATION OF THE CITIZENSHIP REQUIREMENT IN THE DOT's RECONSIDERATION OF THE NORTHWEST-KLM ALLIANCE}

In a revisit by the DOT into the KLM-Northwest alliance (\textit{Northwest II}), it appeared that the DOT had made a commitment to the liberalization of its interpretation of the citizenship requirement, at least as it relates to equity ownership.\textsuperscript{125} On January 15, 1991, Northwest filed another petition requesting that the DOT modify the existing consent order enacted in 1989.\textsuperscript{126} Specifically the petition asked the DOT to:

1. terminate the requirement of Order 89-9-51 that KLM's total equity investment in Wings be reduced to 25 percent;
2. permit KLM to hold 49 percent of the equity in Wings, including 10.544 percent of the voting interest, free of the voting trust required by the Order, with any equity in excess of 49 percent to continue to be held in the trust;
3. permit KLM to designate three members of the Wings board of directors after that board has been increased from 12 to 15 members; and
4. remove the financial reporting conditions contained in the order.\textsuperscript{127}

In its reconsideration, the DOT stated explicitly that it had reevaluated the relationship between voting equity and nonvoting equity and would now allow up to forty-nine percent foreign equity investment in a U.S. carrier.\textsuperscript{128} The DOT stated that although it would continue to examine all avenues of foreign control over a U.S. air carrier, "as a general matter, [the DOT] would not construe foreign equity investment up to these limits, taken alone

\textsuperscript{124} See infra part VII(C).
\textsuperscript{125} See In re Acquisition of Northwest Airlines, Inc. D.O.T. Order No. 91-1-41 (Jan. 23, 1991) [hereinafter Northwest II].
\textsuperscript{126} Id. at 4; see also D.O.T. Order No. 89-9-51 (consent order enacted in 1989).
\textsuperscript{127} D. O. T. Order No. 91-1-41, at 4 (citation omitted).
\textsuperscript{128} Id. at 9. The DOT made it clear that in allowing 49% foreign equity ownership in a U.S. carrier, it was referring to the total foreign equity ownership in Northwest. Thus, if one foreign entity owns the entire 49 percent, then no other foreign entity would be allowed to own a portion of the U.S. carrier. \textit{Id.}
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as indicative of foreign control." Furthermore, the DOT stated that such a standard would not be limited to the Northwest-KLM situation alone and that "[a]s with all decisions in this area, the decision in this order [would] constitute a part of the body of [the DOT's] precedent to be considered in the disposition of future cases as appropriate." The DOT also addressed in depth the issue of the increase of Northwest's board of directors from twelve to fifteen members and the increase of KLM's number of representatives on the board from one to three. The DOT granted the request, noting that the three KLM members would be more than offset by the twelve other directors on the board, eleven of whom were U.S. citizens. The DOT went on to say, however, that because the level of control of each board member is not always equal, "as a general rule, [it] would not allow a foreign citizen to hold the position of Chairman of the Board." Nor would the DOT allow a disproportionate number of foreign directors to hold positions on important corporate committees because this would be another avenue for actual control. Finally, the DOT maintained the requirement found in the earlier consent order that the KLM representatives on the board of directors recuse themselves under certain circumstances.

Overall, the decision by the DOT in Northwest II appeared to be the beginning of an era where the DOT would adapt the U.S. airline industry to the international industry as a whole. In fact the DOT stated in its decision in Northwest II that the decision itself was partly based on the Department's "reassessment of the complexities of to-

129 Id.
130 Id. at 9 n.22. The DOT made this statement partially in response to a request by Delta that the DOT state that any decision reached in this case not serve as precedent. Id. at 6.
131 Id. at 10-11.
132 Id. at 11.
133 Id.
134 Id.
135 Id.
day's corporate and financial environment." Moreover, the DOT looked closely at the liberalized aviation relationship between the United States and the Netherlands, the homeland of KLM, and decided partly in light of this situation, that there was justification to allow KLM to invest heavily through both money and directors in the business of Northwest.

IV. BRITISH AIRWAYS’ PROPOSED PURCHASE OF USAIR - THE AGREEMENT ITSELF

With the DOT’s apparent liberalization of its interpretation of the citizenship requirement of a U.S. air carrier, it appeared the legal door was open to form airline alliances that would take carriers not only to many different parts of the world but also into the next generation of international aviation. As this situation evolved, British Airways (BA) emerged as an airline with a desire to have a U.S. connection. As a result, USAir, Northwest Airlines, Continental Airlines and Trans World Airlines all attempted to attract the capital of BA. Ironically enough, BA originally focused its attention primarily on the KLM-Northwest alliance. However, when the talks between these airlines failed in March, 1992, USAir became a strong contender. BA and USAir began talks regarding the original agreement in June, 1992.

BA came to the negotiations with a clear idea of the type of relationship it was looking for. It was not only looking for “economic and operational compatibility” but it was also looking for a “cultural fit.” Finding that

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136 Id. at 7.
137 Id. at 7-8; see also infra notes 277-90 and accompanying text (discussing the DOT’s open skies initiative and the open skies agreement between the U.S. and the Netherlands).
138 Id.
139 Id.
140 Id.
141 Id.
142 Id.
143 Id.
144 Id.
145 McKenna, supra note 1, at 26.
USAir met these standards, the two airlines signed a final agreement on July 20, 1992 calling for a major investment in USAir by BA. On July 21, 1992, the parties announced the agreement, claiming that it would "form the world's largest airline alliance that [would] strengthen both carriers and provide substantial increases in benefits to the customers, shareholders and employees of both airlines."146

Under the original agreement, British Airways was to invest $750 million in USAir and would receive in return a forty-four percent share in the overall airline equity and four representatives on the USAir board of directors.147 Specifically concerning the investment by BA, the agreement provided that $520 million of the investment would have purchased seven percent of the Series "C" Convertible Preferred shares in USAir, which would have been convertible to common stock at $20.50 per share.148 This part of the investment would have represented twenty-one percent of the voting stock of USAir,149 strictly within the twenty-five percent limit of the Federal Aviation Act of 1958.150 The remainder of the $750 million investment would have been in the form of Series "E" Convertible Preferred shares which would also have been convertible

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145 Id.; see also infra notes 147-56 and accompanying text (discussing the original proposal in detail).
146 USAir, British Airways to Invest $750 Million in USAir, First Step in Creation of World's Largest Airline Alliance (July 21, 1992) (News Release, on file with USAir, Corporate Communications Department) [hereinafter USAir News Release].
147 Id. at 2. At the time of the negotiations, there were 13 members on the USAir board of directors, but through the agreement, the board size would have increased from 13 to 16 members. Id.
148 Id. at 1.
149 Id. Twenty-one percent of the voting stock was the maximum amount of voting stock that BA could purchase at the time of the original agreement because other foreign interests owned four percent of the voting stock in USAir, and as discussed in previous sections, the limit of total foreign ownership of voting stock in a U.S. air carrier is 25%. Id. at 1-2; see 49 U.S.C. app. § 1301(16) (1988). Thus, BA's voting stock would have been able to increase as other foreign voting interests diminished, but it would not have been allowed to exceed 25%. USAir News Release, supra note 146, at 1-2.
to USAir common voting stock at $20.50 per share.\footnote{USAir News Release, supra note 146, at 2. USAir stated in its news release that "[n]o conversion can take place within the first four years. After five years USAir has, under certain circumstances, the ability to require conversion of all the outstanding preferred shares, both Series C and E, to either common stock or to non-voting common stock according to the regulatory framework in place at that time." \textit{Id.}}

The most controversial aspect of the original agreement between USAir and BA called for a major expansion of the USAir board of directors so that BA could have placed a sizable representation on the board.\footnote{\textit{Id. at 2.}} Specifically, the agreement called for an expansion of the USAir board from 13 to 16 members, four positions of which would have been occupied by representatives of BA.\footnote{\textit{Id.}} Furthermore, up to two other directors would have been "interlocking independent directors" serving on both the USAir and BA boards of directors.\footnote{\textit{Id.}} The most important part of the changes in store for the board of directors was the fact that many key decisions\footnote{\textit{Id.}} of the USAir board of directors would have to have been approved by a super majority, consisting of eighty percent of the board’s members.\footnote{\textit{Id.}} As will be discussed shortly, if the DOT had evaluated the alliance on legal grounds, this provision could have been a major factor in the failure of the original agreement.\footnote{\textit{See infra} notes 236-67 and accompanying text (discussing how veto power actually played almost no role in the failure of proposed alliance).}

V. SHOULD THE DEAL HAVE SUCCEEDED?

Before considering how the original agreement between BA and USAir eventually failed, one should under-
stand the domestic policy arguments that were made and continue to be made both for and against the alliance. The following discussion focuses on the policy discussions that took place between the time of the announcement of the original deal and its failure on December 22, 1992. The next section discusses the legal and bilateral issues involved in the alliance.

A. NATIONAL SECURITY

Although national security may no longer be a great concern of the DOT, at least as it relates to air carrier ownership, it must be addressed here for two reasons. First, opponents of the original deal between BA and USAir did raise such concerns. Second, it is necessary to recognize the historical importance of national security concerns. As mentioned earlier, national security interests have always been a concern of opponents to foreign investment in U.S. air carriers. Such concerns were once again confirmed during the Persian Gulf War when U.S. carriers were called upon by the military to aid in transporting troops and equipment to the Persian Gulf.

154 See British Airways Terminates Plan to Invest in USAir, supra note 3.
155 See infra part VI.
156 See infra notes 165-76 and accompanying text (referring to evolution of the opinion of former U.S. Secretary of Transportation Skinner on the issue of national security).
157 See infra note 174 and accompanying text (discussing concern for national security as it related to the proposed BA-USAir alliance).
158 See supra notes 28-36 and accompanying text (discussing the national security concerns which were partially responsible for the original implementation of limitations on foreign ownership of U.S. air carriers).
159 Id.
160 Under the Civil Reserve Air Fleet ("CRAF") program, developed during the Korean War and not activated until 38 years later during the Persian Gulf War, U.S. carriers voluntarily contract to supply a certain number of aircraft to the military when called upon to do so. Lester Reingold, CRAF A "Qualified" Success: Civil Reserve Air Fleet, AIR TRANSP. WORLD, Aug. 1991, at 24. Once the Airline volunteers, however, it is contractually bound to provide the craft. Id. Stage I of the CRAF program was activated on August 18, 1990 after the government discovered that the military airlift alone would be unable to transport the necessary troops and equipment to Saudi Arabia in a timely enough manner. Id. Stage I consisted of 38 aircraft representing 16 carriers. Id. Stage II of the program was engaged on January 16, 1991 and made a total of 187 aircraft available
It appears, however, that such concerns may have subsided or were virtually ignored by the DOT as they related to the BA infusion of capital into USAir.

I. Evolution of DOT Position on National Security

On September 19, 1989, only ten days before the original consent order was handed down in the KLM-Northwest Airlines alliance, Samuel Skinner, then U.S. Transportation Secretary, expressed his concerns over heavy foreign investment in U.S. carriers by foreign entities. One of his primary concerns at that time was national security. In essence, Secretary Skinner stated that national defense would certainly be jeopardized if the U.S. government could not call upon U.S. airlines in times of military crisis to participate in the Civil Reserve Air Fleet (CRAF) program. Some concluded that national security concerns played a significant role in the DOT’s forcing of KLM to reduce its investment in Northwest Airlines and in eliminating other methods of control that KLM might have exercised had the deal gone through as originally planned. Skinner received heavy criticism for this reasoning. The critics stated that the national security argument was not relevant to the case of KLM-Northwest because there was no question that in a time of crisis “the U.S. government could simply commandeer

for the use by the military. Id. Although the government later considered activating stage III, the last stage of the program, which would have made an additional 217 cargo and 258 passenger planes available, it ultimately decided not to do so. Transcom Considering CRAF Stage III Activation, 157 Aerospace Daily 181 (1991).

Before the CRAF deployment was deactivated on May 24, 1991, the civilian aircraft had carried over 310,000 troops and 150,000 tons of cargo. Reingold, supra, at 24. A total of 110 civil aircraft had flown more than 4,700 missions, including an average of 23.4 missions per day per carrier during the war’s peak months of January and February of 1991. Id. Overall, the program was termed a success. Id.

167 See id.
168 Id.
169 Id.
the civilian planes it need[ed].’’

The other argument facing Secretary Skinner was that U.S. carriers needed foreign investment to give them the necessary funds to survive and expand. One commentator expressed his frustration with the DOT’s apparent nationalistic and protectionist views by stating that “[i]t doesn’t matter whether the shareholders of a U.S. airline reside in London, England, or London, Ohio . . . . They are going to want something—profits—and they are going to manage their investment to maximize their profits.’’ This would in turn benefit the U.S. carriers.

This argument eventually caught the attention of Secretary Skinner. In January, 1991, after releasing the modified order in the KLM-Northwest alliance, Skinner indicated that there was a need for foreign investment in U.S. airlines if the latter would be expected to survive. Despite some public support for his old arguments against foreign ownership due to possible threats to national security, Skinner actually made a complete turn around and stated that allowing U.S. carriers to attract

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170 Id. The same critics noted that this is exactly what the U.S. government did during World War II when it took over the U.S. assets of German firms. Storch and Jouzaitis, supra note 165, at C1.

171 Id. Such arguments have also been made in support of the BA-USAir alliance. See USAir, supra note 20, at 7.

172 Storch & Jouzaitis, supra note 165, at C1.


174 Paul S. Dempsey, The Sky Ought to be the Limit, N.Y. TIMES, Jan. 26, 1991, § 1, at 25. This editorial by Paul S. Dempsey, then director of the University of Denver transportation law program, articulates a portion of the national security concern over allowing foreign entities to invest in U.S. airlines:

Foreign ownership restrictions have long existed for many of our essential infrastructure industries—airlines, intercostal and inland shipping, telecommunications, broadcasting, electric power production and nuclear energy. These restrictions were added to our law, not because of blind xenophobia but because of national security considerations.

Aviation is essential to national security, as Operation Desert Storm confirms. The Air Force simply doesn’t have enough C-5A’s to do the job. We maintain a federally subsidized U.S.-flag fleet of ocean carriers because of the lesson we learned in World War I—when we looked around for essential ships to ferry troops and supplies across the Atlantic, there were nearly none. Not that long ago,
foreign capital up to the limits stated in the new *Northwest II* decision “[would] not compromise national security.” Skinner speculated that the decision would instead attract foreign capital into U.S. air carriers and help the airlines recover from a year of record losses.

2. National Security Issues in the BA-USAir Alliance

Concerning the BA-USAir alliance, USAir maintained throughout that there was no national security concern arising from BA’s proposed investment. In support of this argument the airline stated:

There are no foreign policy or national security considerations that should stand in the way of this transaction. U.S. and British firms have had close investment relationships for generations. Capital flows freely between the two countries. With regard to national defense, USAir is a minor participant (two airplanes) in the Civil Reserve Air Fleet program. Moreover, the United Kingdom is, and has for many years been, a close ally of the United States. There could be no more ideal investment partner for a U.S. airline.

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the Government bailed out a collapsing Conrail and Lockheed, in part, because of their importance to national security.

Of course we could commandeer the aircraft of foreign airlines if we needed them—seize the property of foreign companies as other nations have done to American firms. But acquisition of capacity is not the only problem. Those who argue for foreign ownership of domestic airlines forget that most of the technological breakthroughs of aviation were inspired by military applications—proficiency in delivering troops and bombs.

Imagine a world where we had never prohibited foreign ownership or foreign airline competition. How many Pearl Harbors would we have suffered if the dominant domestic airlines in 1940 had been Lufthansa and Japan Airlines? Although we fought wars with Britain in two centuries, British Airways doesn’t look like much of a national security threat these days. Neither did Iran Air before the fall of the Shah.

*Id.*

175 Stewart & Gellene, *supra* note 173, at D3.

176 *Id.*

177 USAir, The British Airways - USAir Investment 2 (undated and unpublished position paper, on file with USAir, Corporate Communications Department) [hereinafter BA-USAir Investment].

178 *Id.*
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Thus, there appeared to be no legitimate national security concern with the original BA investment in USAir. USAir stated that it participated only minimally in the CRAF program, and even if this were not the case, there was absolutely no indication that USAir would cease to participate in the CRAF program as a result of an alliance with BA. Furthermore, it appeared that the DOT was changing its opinion and realizing that foreign capital was a necessary part of the future aviation industry of this country. Finally, as has been indicated above, there seemed to be no lower risk partner than BA, considering the U.S.'s close relationship with Great Britain in recent history.

B. JOB SECURITY

An issue over which there has been much debate is how the original BA-USAir alliance would have effected jobs of both USAir employees and airline employees in general. American, United and Delta Airlines (the Big Three) claimed that USAir jobs would be in jeopardy as a result of the British Airways investment in USAir. Although the jobs might have been secure for the short term, the long term threat would have come from a possible BA takeover of the entire operations of USAir if the DOT eventually allowed BA to do so. In such a situation, the Big Three claimed, "[economic logic dictates that integration of [USAir] operations with larger British
Airways [would have lead] to consolidations resulting in a loss of USAir jobs."\textsuperscript{185}

USAir, on the other hand, argued that the infusion of capital by British Airways into USAir would clearly have had the opposite effect of ensuring the jobs of the approximately 46,000 employees of USAir.\textsuperscript{186} The airline stated specifically that "[t]he alliance [would] strengthen USAir and thus assure the employment future of 46,000 USAir employees and the economic contribution that they make to the cities in which they work and live."\textsuperscript{187} It is clear that USAir does not have the financial resources with which the Big Three are operating and thus cannot continue to absorb the losses that the airline has suffered consistently over the past two years and still sustain its work force.\textsuperscript{188} USAir claimed that one of the most logical sources of badly needed income or capital for the airline is that which can come only from a foreign carrier.\textsuperscript{189} A foreign carrier would be the investor most likely to achieve equal benefits from such an arrangement.\textsuperscript{190} Thus, BA appeared and still appears to be a logical conduit through which USAir can maintain its viability and thereby secure the jobs of its employees.

The Big Three also argued, however, that USAir jobs

\textsuperscript{185} Id.

\textsuperscript{186} USAir, The Alliance Should be Approved Because: (undated and unpublished position paper, on file with USAir, Corporate Communications Department) [hereinafter Alliance Should be Approved].

\textsuperscript{187} Id. at 1. USAir also stated unequivocally that "USAir, and the 45,000 jobs it represents [would] not 'cease to exist.' The investment [would have] permit[ted] USAir to survive and prosper as an independent U.S.-flag airline. The investment [would have] create[d] U.S. jobs and enhance[d] airline competition. This is why the investment [was] enthusiastically supported by USAir's employees." USAir, supra note 20, at 2.

\textsuperscript{188} See supra notes 9-16 (discussing the recent losses of the airline industry as well as grim prospects for immediate improvement).

\textsuperscript{189} USAir, supra note 20, at 7.

\textsuperscript{190} Id. For an airline such as USAir, which has a lower investment grade than some of its competitors, particularly the Big Three, the only way to attract an investor is to offer the investor the ability to gain from the transaction. Id. Thus, logic points to a foreign airline who could invest a substantial amount in the airline and receive a major return on its investment through an alliance with a U.S. carrier. See id.
were not the only ones that would have been in jeopardy if the original transaction between BA and USAir had been approved. In fact, they argued that the approval of the alliance might also jeopardize the jobs held at other U.S. carriers. The Big Three's reasoning was basically that approval by the DOT of the original BA-USAir deal would have set a dangerous precedent and allowed other foreign airlines to "violate U.S. law, buy their way into the U.S. market and place U.S. international [and domestic] carriers at a serious competitive disadvantage." 

The Big Three argued that allowing foreign air carriers such a large stake in the U.S. domestic market would effect jobs at these other U.S. airlines in very serious ways. First, they claimed that U.S. airline jobs would be transferred overseas as foreign air carriers bought larger and larger shares of the U.S. airlines and consolidated their operations in locations other than the United States. Second, others claimed that with greater competition within the United States from foreign carriers, pure U.S. carriers would not be able to effectively com-

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191 American Airlines et al., supra note 2, at 10.
192 Id.
193 Id.
194 See id.
195 Id. The Big Three further warned that if large amounts of U.S. airline jobs were transferred overseas as they predicted, the U.S. airline industry would soon find itself in the same weak position as the U.S. steel and auto industries find themselves today. Id. at 5.

Several unions whose members work in the aviation industry urged the DOT to disapprove of the BA-USAir deal or to at least scrutinize heavily the effects which the original alliance would have had on U.S. jobs. Labor Groups Weigh Their Future Against BA/USAir Transaction, AVIATION DAILY, Dec. 3, 1992, at 368. One union in particular, Transport Workers of America (TWU) urged this position to the DOT but felt the administration was unwilling to take on such a scrutiny. Id. The union's fears stemmed from the fact that Northwest and Continental both were well on their ways to being controlled by foreign entities, and if the original BA-USAir deal had been approved, they claimed that "almost 30% of the U.S. commercial aviation [would have been] controlled by foreigners." Id.

TWU also states that the DOT will not be able to save U.S. jobs if these foreign partners decide to transport the jobs to their own countries. Id. Additionally, TWU contends that there is good reason to believe that the foreign carriers will have the incentive "to transfer functions, such as heavy maintenance and dispatch of U.S. aircraft, to facilities in their home countries." Id. The union predicts catastrophic results if such a situation were to occur. Id.
pete in their own marketplace. A partial reason for such an inability to compete would be that a large portion of foreign governments either own or heavily subsidize their airlines. It would be virtually impossible for privately-owned U.S. airlines to compete against foreign government-owned (or subsidized) airlines, unconcerned about short term losses. Therefore, airline jobs indus-

197 *Id.* at 33-34.
198 *Id.* Duane Woerth raised the issue of national airlines in the context of cabotage, but the possible problem of U.S. carriers competing with foreign government owned airlines applies equally to issues of foreign control and ownership of U.S. airlines considering that the U.S. carriers that would conceivably be under foreign control would be competing directly with other U.S. air carriers in their own marketplace. To illustrate how serious the problem of government ownership of foreign airlines may be, the following data indicates the extent to which foreign airlines were owned by their governments as of August, 1992:

**Percentage of Government Ownership of the Top 16 European Airlines:**

<table>
<thead>
<tr>
<th>Airline</th>
<th>Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Air France</td>
<td>100%</td>
</tr>
<tr>
<td>Iberia</td>
<td>100%</td>
</tr>
<tr>
<td>Olympic</td>
<td>100%</td>
</tr>
<tr>
<td>TAP-Air Portugal</td>
<td>100%</td>
</tr>
<tr>
<td>JAT-Yugoslav</td>
<td>100%</td>
</tr>
<tr>
<td>Air Lingus</td>
<td>100%</td>
</tr>
<tr>
<td>Alitalia</td>
<td>83%</td>
</tr>
<tr>
<td>Austrian</td>
<td>75.8%</td>
</tr>
<tr>
<td>Finnair</td>
<td>70%</td>
</tr>
<tr>
<td>Sabena</td>
<td>55%</td>
</tr>
<tr>
<td>SAS</td>
<td>50%</td>
</tr>
<tr>
<td>Lufthansa</td>
<td>48%</td>
</tr>
<tr>
<td>KLM</td>
<td>39%</td>
</tr>
<tr>
<td>Swissair</td>
<td>25%</td>
</tr>
<tr>
<td>British Airways</td>
<td>0%</td>
</tr>
<tr>
<td>Icelandair</td>
<td>0%</td>
</tr>
</tbody>
</table>

**Percentage of Government Ownership of the Top 12 Asian Airlines:**

<table>
<thead>
<tr>
<th>Airline</th>
<th>Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Air India</td>
<td>100%</td>
</tr>
<tr>
<td>Air China Int'l</td>
<td>100%</td>
</tr>
<tr>
<td>China Airlines</td>
<td>100%</td>
</tr>
<tr>
<td>Garuda Indonesia</td>
<td>100%</td>
</tr>
<tr>
<td>Philippine Air</td>
<td>100%</td>
</tr>
<tr>
<td>Thai Airways</td>
<td>100%</td>
</tr>
<tr>
<td>Vietnam Airlines</td>
<td>100%</td>
</tr>
<tr>
<td>Singapore</td>
<td>55%</td>
</tr>
<tr>
<td>Malaysia</td>
<td>52%</td>
</tr>
<tr>
<td>Korean Air</td>
<td>0%</td>
</tr>
<tr>
<td>All Nippon</td>
<td>0%</td>
</tr>
<tr>
<td>Japan Airlines</td>
<td>0%</td>
</tr>
</tbody>
</table>
try-wide would conceivably be in jeopardy.

C. LOCAL ECONOMIES IN USAIR SERVED CITIES\textsuperscript{199}

Despite assurances from the U.S. Secretary of Transportation and airline analysts that USAir would not be seriously endangered even without the $750 million BA investment,\textsuperscript{200} there was some concern for the viability of the airline if the original investment proposal failed.\textsuperscript{201} One of the primary voices of concern was that of Robert P. Casey, Governor of Pennsylvania.\textsuperscript{202}

Before the deal failed, Governor Casey expressed his support to the DOT for the BA-USAir alliance.\textsuperscript{203} In a letter to the DOT, Casey stated that the BA-USAir venture "was essential to the economic future of Pennsylvania."\textsuperscript{204} Casey noted that USAir contributes to the Pennsylvania economy in many important ways.\textsuperscript{205} The

\textsuperscript{199}There is also some concern that the national economy will suffer substantial negative effects from the failure of the original deal. \textit{See Boeing Link, SEATTLE TIMES}, Dec. 14, 1992, at F1. BA stated before the deal failed that regardless of whether the alliance was successful, the airline intended to spend $6.5 billion dollars in the United States on Boeing aircraft in the next five years and has the option to purchase more jets worth the same amount. \textit{Id.} The airline has further stated that it intends to pump a total of over $20 billion into the U.S. economy by 1997 including the aircraft purchases already mentioned. \textit{Id.} The other money would come in the form of spare parts, fuel, salaries, commissions and other fees related to its operation in the United States. \textit{Id.}

Furthermore, if this $20 billion were to be combined with USAir's projected spending, the total would be over $60 billion. Carole A. Shifrin, \textit{British Airways, USAir Escalate Offensive Against Dissenters}, AV. WK. & SPACE TECH., Dec. 14-21, 1992, at 30. There is, however, some concern that, without the full $750 million investment, USAir will not be in a position to make such expenditures thereby having substantial effects on the national economy. \textit{Id.}

\textsuperscript{200}Jeff Pelline, \textit{British Airways-USAir Deal is Dead}, S.F. CHRON., Dec. 23, 1992, at C1; Julie Schmit, \textit{Airline Still has Hope for British Air}, USA TODAY, Dec. 23, 1992, at 1B.

\textsuperscript{201}USAir has an accrued debt of approximately $2.3 billion. Schmit, \textit{supra} note 200, at 1B.


\textsuperscript{203}Casey Urges Approval, \textit{supra} note 202; Casey Supports Agreement, \textit{supra} note 202.

\textsuperscript{204}Casey Urges Approval, \textit{supra} note 202.

\textsuperscript{205}Id.
airline is the second largest private employer in the southwestern part of the state and as a result, the salaries the airline pays to its employees give the airline a "major economic presence" in the state. USAir has its largest hub in Pittsburgh with 347 daily nonstop departures to eighty-seven destinations. Casey's letter also stated that "eighty-nine percent of the total passengers who board[ed] airplanes in Pittsburgh in 1991 boarded either USAir or USAir Express." Furthermore, USAir had just made an enormous investment in a new terminal at the Pittsburgh International Airport which provides state-of-the-art transportation services to the western region of the state. Thus, it is clear that USAir plays a large role.

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206 Id. Casey's letter to Secretary Card specifically stated that:
Of course, Pennsylvania has an enormous stake in USAir's success and vitality. USAir is the second largest private employer in southwestern Pennsylvania, employing 12,020 full- and part-time employees. Its operations generate over $1.1 billion through payroll, fuel, food, taxes, landing fees and other expenditures.
The airline is an important state-wide presence, with an additional 2,300 employees in the Philadelphia region and a total Pennsylvania work force of about 15,000. By ensuring a strong and successful company, the agreement will help secure these high paying jobs and the continued stability of a major economic presence in Pennsylvania.

207 Id.

208 Id. USAir Express is a commuter airline which also belongs to the USAir parent company, USAir Group, Inc. Id. The airline as of September, 1992 ran 147 daily commuter flights to 33 destinations. Id.

209 Id. Governor Casey's letter continued:
Pennsylvania has undertaken an unprecedented infrastructure investment in and around the airport. Federal funds have made a substantial contribution. The economic growth resulting from this investment will be strengthened by a successful and thriving USAir.
As you know, the new Midfield Terminal was recently completed in October, the first new airport construction in this country in the last twenty years. The $766 million partnership among the Commonwealth, the federal government, Allegheny County and USAir produced a state-of-the-art air terminal that now serves as a regional hub for air, highway and rail transportation.
This hub is linked to all of Western Pennsylvania, through a $400 million investment in the Southern Expressway, the Beaver Valley Expressway and the Moon Township Interchange highway improvement and construction prospects.

Planning is underway, financed with $2.3 million in state funds
in the overall economy of Pennsylvania, and the airline’s viability is vital if the state is to maintain and fully utilize its recent infrastructure investments.\textsuperscript{210}

Although Pennsylvania may be where USAir has its largest presence,\textsuperscript{211} it is certainly not unrealistic to assume that the airline is important to many of the other local economies that it serves.\textsuperscript{212} USAir dominates a large portion of the airline market share on the East Coast,\textsuperscript{213} and its employees live all over the country. Because the original alliance between USAir and BA would have allowed USAir to substantially reduce its debt\textsuperscript{214} and increase its standing for long term competition,\textsuperscript{215} the alliance would have therefore had a positive effect on the cities where USAir employees work, live, and contribute to the local economies.\textsuperscript{216}

\section*{D. Consumer Benefits}

Just as the long term viability of USAir would greatly benefit the economies of the cities that the airline serves, the original alliance would have also benefitted consum-

\begin{itemize}
\item and $500,000 in federal funds, for a proposed magnetic levitation demonstration project to run from the airport to downtown Pittsburgh.
\item Approval of the USAir/British Airways alliances will reinforce these investments to ensure southwest Pennsylvania’s place as a true world-class transportation “hub,” and ensure continued growth in high-paying jobs for our people.
\item \textit{Id.}
\item \textit{Id.}
\item \textit{Id.}
\item \textit{Id.}
\item \textit{USAir Sees the Demise of Second-Tier Carriers Without Investment, Av. Daily, Dec. 1, 1992, at 352 [hereinafter Demise of Second-Tier Carriers]. Pennsylvania is not the only area which has expressed support for the BA/USAir alliance for economic reasons. See id. For example, many businesses and civic organizations in Charlotte, North Carolina have “implored the DOT to allow the investment to go through because of USAir’s impact on the local economies and their business transportation and shipping needs.” Id.}
\item \textit{Id.}
\item \textit{Id.}
\item \textit{Id.}
\item \textit{BA-USAir Investment, supra note 177, at 2.}
\item \textit{Id.}
\end{itemize}
ers of USAir's and BA's air services. The benefits would have come through more effective competition that USAir could have provided against the Big Three airlines in the United States and internationally. The proposed alliance would have served destinations in 71 countries throughout the world. The British carrier, through its investment, was hoping to create a "'seamless' global airline network that would link its London-based international flights with USAir's large system in the United States." The goal of the companies was to provide uniform air services throughout the world, which they believed would be very important to the consumer.

Opponents of the deal, however, stated that the alliance under any circumstances would benefit the customers only very modestly. In fact, they claimed that instead of benefitting consumers, the alliance between BA and USAir could possibly have led to monopolistic practices. Such a situation would have had detrimental effects on the consumers.

The stronger and more logical argument, however, appears to be that it would be better to have five or six major airlines, one being the alliance between BA and USAir,

217 Shifrin, supra note 199, at 30. U.S. Secretary of Transportation Andrew Card also supports the view that the deal would have been "very good for American consumers." David Field, Open-Skies Failure Kills BA-USAir Deal, WASH. TIMES, Dec. 23, 1992, at C1. Card added, however, that he could not approve the deal even with such benefits if the U.S.-U.K. landing rights treaty could not be changed. Id.

218 Demise of Second-Tier Carriers, supra note 212, at 352.


221 Pact Will Help Consumers, supra note 219, at B5. When asked why customers should care about the alliance between BA and USAir, Seth Schofield, CEO of USAir, responded that "[i]t is very important from a consumer point of view that he or she get the same service whether flying from Allentown to Pittsburgh or from London to Paris." Id.


223 Demise of Second-Tier Carriers, supra note 212, at 352.
who compete effectively in this country.\textsuperscript{224} Certainly the U.S. market alone, which consists of approximately forty percent of the entire world market,\textsuperscript{225} is large enough to support more than only the Big Three.\textsuperscript{226} With the failure of the original deal between BA and USAir, it appeared that the Big Three had achieved what they wanted: maintenance of an oligopoly without major competition from USAir or British Airways.\textsuperscript{227} This oligopoly currently controls about sixty percent of the international and domestic market.\textsuperscript{228} It is difficult to see how this situation can benefit the consumer.

VI. WHY THE AGREEMENT ACTUALLY FAILED

The relatively strong arguments outlined above favoring the original alliance between BA and USAir and former Secretary Card's belief "that (1) carriers from everywhere would benefit from a loosening of restrictions, which would feed competition, and (2) that U.S. carriers certainly could benefit from more foreign investments"\textsuperscript{229} lead to the overarching question of why the original deal did not succeed. Clearly the arguments concerning national security,\textsuperscript{230} job security,\textsuperscript{231} faltering local economies,\textsuperscript{232} and consumer benefits\textsuperscript{233} should play a role in the decisions and policy that the DOT sets forth for the airline industry. Certainly such concerns were not far away from the mind of Secretary Card as he began to evaluate the possible original alliance between BA and USAir; however, it appears that such concerns were only secondary to the DOT when it made the final indication that it

\begin{itemize}
\item \textsuperscript{224} See generally Shifrin, supra note 199, at 30.
\item \textsuperscript{225} Leveraging an Airline Linkup, supra note 22, at B9.
\item \textsuperscript{226} Shifrin, supra note 199, at 30.
\item \textsuperscript{227} A Setback for Competition in the Skies, CHI. TRIB., Dec. 24, 1992, at 14.
\item \textsuperscript{228} Pact Will Help Consumers, supra note 219, at B5.
\item \textsuperscript{229} A Loss for USAir—and the Public, WASH. POST, Dec. 24, 1992, at A12 (editorial).
\item \textsuperscript{230} See supra notes 160-81 and accompanying text.
\item \textsuperscript{231} See supra notes 182-98 and accompanying text.
\item \textsuperscript{232} See supra notes 199-216 and accompanying text.
\item \textsuperscript{233} See supra notes 217-28 and accompanying text.
\end{itemize}
would not approve of the alliance between BA and USAir.\textsuperscript{234} The following discussion also shows that despite the DOT’s role of applying the citizenship requirement of the 1958 Act, the alliance did not fail due to any such application or any legal reason at all, but instead from pressure applied by the Big Three to use the BA-USAir pact as leverage to gain a stronger hold on the international airline market.\textsuperscript{235}

A. The Issue of Control

Although this Comment concludes that the DOT was concerned more with politics than with the law when it made its indication, it is still useful to discuss the original agreement in the context of the citizenship requirement. From a legal perspective, the issue of the control that BA would have exercised over USAir did cause some concern.\textsuperscript{236} As was discussed earlier in this Comment, the DOT not only applies the letter of the law, that U.S. citizens must own seventy-five percent of the voting stock of all U.S. carriers and that the president and two-thirds of the board of directors of such carriers must be U.S. citizens,\textsuperscript{237} but it also applies an actual control test.\textsuperscript{238} Such a test requires that regardless of the fact that an airline may meet the above requirements set forth by the 1958 Act, it must also in fact be controlled by U.S. citizens.\textsuperscript{239}

\begin{itemize}
\item \textsuperscript{234} British Airways stated, in withdrawing from the agreement with USAir, that BA had received a clear indication from the U.S. government that the deal as it stood would not be approved. Pelline, \textit{supra} note 200, at C1; \textit{see also infra} notes 236-306 and accompanying text (discussing the determinative factors which caused the DOT to attack the BA-USAir alliance).
\item \textsuperscript{235} \textit{See infra} notes 268-306 and accompanying text (discussing the effect of the Big Three’s emphasis on the bilateral agreement between the U.S. and Great Britain).
\item \textsuperscript{236} Pelline, \textit{supra} note 200, at C1.
\item \textsuperscript{237} 49 U.S.C. app. § 1301(16) (1988); \textit{see also supra} note 5 (setting forth the exact language of the citizenship requirement under current law).
\item \textsuperscript{238} \textit{See supra} notes 52-137 and accompanying text for an in depth discussion of the control test applied first by the CAB and now by the DOT. \textit{But see In re Acquisition of Northwest Airlines, Inc.}, D.O.T. Order No. 91-1-41 (Jan. 23, 1991) (indicating that the DOT was willing to loosen some restrictions on actual control by allowing KLM to own up to 49% of the common equity in Northwest Airlines).
\item \textsuperscript{239} \textit{In re Discovery Airways, Inc.}, D.O.T. Order No. 89-12-41, at 10 (Dec. 21,
First of all, there is no question that the original BA-USAir agreement satisfied the explicit standards in the 1958 Act. In the deal, BA would have invested $750 million in USAir, purchasing only twenty-one percent of USAir's voting stock. This figure is well within the twenty-five percent limit contained in the 1958 Act. Furthermore, the agreement provided that BA could not have elected more than twenty-five percent of USAir's board of directors and that USAir's current management would stay in place, also satisfying the requirements of the 1958 Act.

Furthermore, the amount of USAir's total equity that BA would have gained in its investment was also within the limits recently allowed by the DOT. Had the original deal between BA and USAir succeeded, BA would have owned forty-four percent of USAir's total equity, well within the forty-nine percent parameter.

BA and USAir both claimed that their agreement complied fully with U.S. law, and USAir was very careful to insist that it would remain under the control of U.S. citizens. USAir stated specifically that it was aware the DOT not only looks at the strict requirements of the law, but also at the overall effect of the agreement on the airline industry. USAir also noted that the deal had already received antitrust clearance in the U.S.

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USAir, supra note 20, at 3. See also British Airways Terminates Plan to Invest in USAir, supra note 3 (stating that the deal between the two airlines was constructed to comply completely with U.S. law). BA also noted that the deal had already received antitrust clearance in the U.S. Id.
but "also reads a 'control' requirement into the definition, requiring that 'control' be in the hands of U.S. citizens."248 The airline still insisted, however, that it would remain "an American company run by Americans."249

The Big Three and others argued just the opposite.250 They claimed that the terms of the agreement between USAir and BA would have given the latter effective control over USAir.251 Thus, despite the agreement's compliance with other aspects of the citizenship requirement, there has been much argument over whether the foreign-owned BA would have actually controlled USAir had the original deal succeeded.

The problem with the agreement between the two airlines pertained to BA's presence on USAir's board of directors.252 As discussed earlier, the agreement provided that USAir's board of directors would have been increased from thirteen to sixteen members of which BA would have gained four seats.253 Although this would have given BA only twenty-five percent of the USAir board of directors, within the limits stated in the 1958 Act,254 the real problem was the control over key decisions that BA would have had.255 The agreement specifically provided that key decisions such as major financial

248 USAir, supra note 20, at 3. USAir, however, went on to qualify its interpretation of the control requirement as follows:

The "control" requirement, a concept developed in the days of heavy-handed federal regulation, is subjective and decided on a case-by-case analysis, but there are guidelines. First, the requirement does not reflect any protectionist sentiment. Second, it is subject to change as the forms of investment change. Third, and most important, it is motivated primarily by the pro-competition policies of airline deregulation, including the statutory mandate "to attract capital" to a competitive U.S. airline industry.

Id.

249 Id. at 4.

250 See American Airlines et al., supra note 2, at 3.

251 Id.

252 See supra notes 152-57 and accompanying text (introducing the topic of the super majority provision contained in the agreement between BA and USAir).

253 McKenna, supra note 1, at 26.


255 See McKenna, supra note 1, at 26.
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investments, appointment or dismissal of senior USAir executives or any other major business decision not common to the airline's daily operations, would have to be approved by a super majority (eighty percent) of USAir's board of directors.256

The Big Three were very quick to condemn this aspect of the deal and argued that such control over USAir by BA would have been overtly illegal.257 They noted that "all critical business decisions affecting the business affairs of USAir would [have] require[d] agreement of at least [eighty] percent of its Board of Directors."258 The Big Three then claimed that since BA would have controlled twenty-five percent of that board, BA would have consequently maintained veto power over the most important decisions of USAir.259

USAir, on the other hand, argued that the super majority requirement was a common right conceded in such investments and would not subject USAir to illegal control by their British partner.260 USAir stated instead that the super majority provision was not an unusual concept for corporate boards of directors and that the provision simply provided for a system of "management by consensus."261 The airline argued that such an arrangement is commonly used to protect minority investment interests.262 Finally, the airline stated that despite this negative veto power, BA in no way could affirmatively control USAir's board of directors.263

It would appear at first glance that despite USAir's forceful arguments, the issue of control could have been a deal breaker for the BA-USAir pact. In fact, there are indications that the DOT did raise some concerns regarding

256 Id.; see also Tait, supra note 155, at 22 (listing decisions that would be subject to super majority approval).
257 American Airlines et al., supra note 2, at 3.
258 Id.
259 Id.
260 USAir, supra note 20, at 3.
261 Alliance Should be Approved, supra note 186, at 1.
262 BA-USAir Investment, supra note 177, at 1.
263 Id. at 2.
the veto provision.\textsuperscript{264} If, however, the super majority provision did cause the deal to fail, it certainly appears that there could have been a workable solution. The DOT had earlier dealt with arrangements between foreign and U.S. carriers where the foreign carrier exercised too much control over decisions of the U.S. airline.\textsuperscript{265} The DOT had also successfully encouraged the partners to restructure their arrangements so as to allow the deal to comply fully with U.S. law.\textsuperscript{266} Such a solution probably could have been achieved here, but BA withdrew before such negotiations even began. As this situation and the following discussion indicate, the reason for BA's withdrawal was not in fact the DOT's legal concern over control; instead, BA withdrew because the DOT would have rejected the agreement on completely different grounds.\textsuperscript{267}

\textbf{B. BREAKDOWN IN BILATERAL TALKS WITH UK AND BIG THREE'S POLITICIZATION OF THE DEAL}

1. \textit{Big Three Connect Issues of Foreign Ownership and Bilateral Liberalization with the U.K.}

From the moment USAir announced BA's plans to invest $750 million into the airline, the Big Three adamantly opposed the original alliance.\textsuperscript{268} It might seem logical that the Big Three would have opposed the deal because an alliance between BA and USAir would pose a major competitive threat to them in their own market.\textsuperscript{269} In a time when the airlines are reporting record losses,\textsuperscript{270}

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\textsuperscript{264} Pelline, \textit{supra} note 200, at C1.
\textsuperscript{265} See \textit{In re} Acquisition of Northwest Airlines, Inc., D.O.T. Order No. 89-9-51, at 7 (Sept. 29, 1989) (discussing KLM's proposal to appoint a three-member advisory committee with the purpose of advising Northwest in its financial and other affairs).
\textsuperscript{266} Id. at 9 (discussing KLM's agreement to discard plans to appoint an advisory committee).
\textsuperscript{267} See infra notes 268-306 and accompanying text (discussing the politicization of the deal between BA and USAir).
\textsuperscript{268} See generally American Airlines et al., \textit{supra} note 2.
\textsuperscript{269} \textit{A Loss for USAir and the Public}, \textit{supra} note 229, at A12.
\textsuperscript{270} See \textit{supra} note 11 (for an in depth discussion of recent losses by the airlines).
\end{flushleft}
their reluctance to open the market to a foreign carrier is understandable.

The Big Three, however, claimed that their opposition was based on completely different grounds.\(^\text{271}\) In fact, they stated that they did not fear competition; they feared that approval of this ownership arrangement between BA and USAir would effectively destroy the ability of U.S. carriers to compete.\(^\text{272}\) The Big Three accused BA of seeking backdoor access to the domestic U.S. market and effectively avoiding U.S. laws against cabotage.\(^\text{275}\) They concluded that if the alliance had been allowed to succeed without concessions granted to U.S. carriers by the U.K., the alliance would have been a direct assault on the U.S. airline industry, leaving U.S. carriers with no means to compete and the U.S. government with no leverage to gain access to the British market.\(^\text{274}\) Thus, the Big Three claimed that their only problem with the proposed alliance between BA and USAir was set in the context of the current strict air transport agreement between the U.S. and the U.K.\(^\text{275}\)

2. DOT Calls for Open Skies - Cites U.S. Netherlands Agreement

The Big Three focused on the DOT’s policy to “permit limited ownership flexibility only in cases where the United States has a liberalized aviation relationship with the country of the foreign investor.”\(^\text{276}\) On March 31, 1992, former Secretary of Transportation, Andrew Card, announced the DOT’s so-called open skies initiative.\(^\text{277}\) The initiative is directed toward European countries and

\(^{271}\) American Airlines et al., supra note 2, at 5.

\(^{272}\) Id.

\(^{273}\) Id. at 3.

\(^{274}\) Id. at 5.

\(^{275}\) American Airlines et al., supra note 2, at 5. The Big Three in fact claimed that they would wholeheartedly support an alliance between BA and USAir if only equal concessions could be won from Great Britain. Julie Schmit, Rivals Seek Reciprocity, USA TODAY, July 22, 1992, at B1.

\(^{276}\) American Airlines et al., supra note 2, at 4.

\(^{277}\) U.S. to Explore Open Skies Agreements with European Nations Offering Free Access, PR
basically states that the U.S. would offer to negotiate "open-skies agreements" with any European country that is willing to offer U.S. air carriers unlimited access to their respective airline markets.\textsuperscript{278} Subsequently, after calling for public comment to aid in formulating an official definition of open skies,\textsuperscript{279} the DOT issued an order stating the final definition of open skies. This definition focused on "(1) [o]pen entry on all routes; (2) [u]nrestricted capacity and frequency on all routes; [and] (3) [u]nrestricted route and traffic rights, that is, the right to operate service between any point in the United States and any point in the European country."\textsuperscript{280}

A key example of the type of agreement the DOT is seeking with European countries is the recent agreement

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\item \textsuperscript{278} In re Defining Open Skies, D.O.T. Order No. 92-4-53 (Apr. 29, 1992) (requesting public comment on definition of open skies).
\item \textsuperscript{279} In re Defining Open Skies, D.O.T. Order No. 92-8-13 app. (Aug. 5, 1992).
\item \textsuperscript{280} Newswire, March 31, 1992, available in LEXIS, Tran Library, Air File [hereinafter U.S. to Explore Open Skies Agreements].
\end{itemize}
\end{footnotesize}
signed between the United States and the Netherlands.\textsuperscript{281} The agreement, signed on September 4, 1992, will allow any U.S. carrier to provide service from any point in the United States to any point in the Netherlands and vice-versa.\textsuperscript{282} The deal also allows the freedom to carry both passengers and cargo, places no limitations on the number of flights or types of planes used, grants the freedom to form any aviation related businesses, and grants the freedom for U.S. and Dutch carriers to work together on any route between the two countries.\textsuperscript{283} In fact, Secretary Card stated that the agreement embraces all elements of the definition of open skies that the DOT published in August of 1992.\textsuperscript{284}

The agreement further provides for "cooperation and integration of commercial operations between airlines of the U.S. and the Netherlands," and the DOT agreed to give "fair and expeditious" evaluations of such agreements and antitrust immunity requests.\textsuperscript{285} Northwest Air-

\begin{itemize}
  \item \textsuperscript{281} The Turbulent Travel Industry; U.S., Netherlands Sign "Open Skies" Pact; Aviation: The Agreement Allows Airlines from the Two Countries Unrestricted Access to Each Other's Airports, L.A. TIMES, Sept. 5, 1992, at D1 [hereinafter U.S., Netherlands Sign "Open Skies" Pact].
  \item \textsuperscript{282} Joint Application of Northwest Airlines, Inc. and KLM Royal Dutch Airlines for Approval and Antitrust Immunity of an Agreement Pursuant to Sections 412 and 414 of the Federal Aviation Act, as Amended, D.O.T. Order No. 92-11-27, at 3 (Nov. 16, 1992).
  \item \textsuperscript{283} David Phelps & Josephine Marcotty, Northwest, KLM begin 'Open Skies' Agreement; As a Result, Both Carriers Will Have Unlimited Access to United States, Netherlands, STAR TRIB., Sept. 5, 1992, at D1.
  \item \textsuperscript{284} U.S., Netherlands Sign "Open Skies" Pact, supra note 281, at D1; see D.O.T. Order No. 92-8-13 app.; see also supra note 280 (setting forth the complete definition of open skies as stated by the DOT in its order).
  \item \textsuperscript{285} Bill Poling, Northwest, KLM Seek to Operate as 'Single Firm' Under New Pact; Northwest Airlines and KLM Royal Dutch Airlines, TRAVEL WkLY., Sept. 14, 1992, at 1.
\end{itemize}
lines and KLM Royal Dutch Airlines have subsequently taken advantage of this liberalization and have won the DOT's approval for a new Commercial Cooperation and Integration Agreement and antitrust immunity. According to the agreement, Northwest and KLM intend to operate all of their services as if they were a single airline. Furthermore, the KLM-Northwest alliance was able to convince the DOT to further liberalize the requirements that it had earlier imposed upon the airlines in order to ensure compliance with the citizenship requirement of the 1958 Act. The DOT allowed such liberalization and ruled that the alliance would remain under the control of U.S. citizens. Thus, with this approval and with the comments of former Secretary Card stating that the open skies agreement between the U.S. and the Netherlands should be a model for future agreements with other European countries, it is becoming clear that the DOT is doing exactly what the Big Three would hope: placing emphasis on the need for such open skies agreements before allowing significant foreign ownership liberalization to take place.

286 Joint Application of Northwest Airlines, Inc. and KLM Royal Dutch Airlines for Approval and Antitrust Immunity of an Agreement Pursuant to Sections 412 and 414 of the Federal Aviation Act, as Amended, D.O.T. Order No. 93-1-11, at 1 (Jan. 11, 1993).


288 See supra notes 125-37 (discussing the final DOT order with regards to the original KLM/Northwest alliance). The DOT concluded that nothing in the new agreement will cause Northwest to cease being a U.S. citizen. D.O.T. Order No. 93-1-11, at 16-17. The DOT did, however, retain the reporting requirement that it had earlier imposed. Id. at 17; see also D.O.T. Order No. 89-9-51, at 9 (original imposition of reporting requirement). In its approval of the new agreement, the DOT eliminated the recusal requirement for members of the board of Northwest who represented KLM in matters of finance or competition. D.O.T. Order No. 93-1-11, at 17. The order did, however, impose a new recusal requirement in matters related to Northwest's decision to terminate or maintain the agreement and in matters regarding U.S. negotiations with the EC and the Netherlands. Id.

289 Id. at 16.

290 U.S., Netherlands Sign "Open Skies" Pact, supra note 281, at D1.
3. USAir's Plea for Disconnection of Issues of Foreign Ownership and Bilateral Liberalization

USAir recognized that the Big Three appeared to be using the prospects of a similar open skies agreement with the U.K. to gain more route authority into the British market. USAir argued, however, that this line of reasoning was misleading and that the Big Three neither needed nor wanted additional authority, but simply wanted to connect the issues of foreign ownership and an open skies agreement because they knew that any negotiations with the U.K. for liberalization would last beyond the deadline for approval of the deal set in the agreement between the airlines. Thus, they simply were looking for a way to kill the alliance and prevent the birth of a powerful competitor.

USAir urged the DOT to focus its attention on the facts of the case and on the law, thus separating the alliance from claims for open skies by the Big Three. USAir stated that the deal, as it stood, complied strictly with U.S. law, including the Federal Aviation Act and the case-by-case analysis undertaken by the DOT in such matters. The airline requested the DOT not to focus on the bilateral issues but to follow the policy encouraging foreign investment and the open investment policy set forth by the Bush administration. Without such a commitment,

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291 USAir, supra note 20, at 6.
292 Id. The Big Three argued that they are denied large amounts of the European market share because they lack the authority to operate between the U.K. and Continental Europe. Id. at 6. They further claimed that such rights would be comparable to what BA would have gained through its alliance with USAir. Id. USAir claimed, however, that although British Airways flies some routes between the U.S. and U.K. and then to other European countries, the majority of air travel between the U.S. and Europe consists of non-stop flying, and the Big Three dominate this market. Id. Thus, the Big Three's argument that they need more authority from Great Britain to establish themselves in the U.S.-Europe market seems to have been a shield covering their underlying motives of delaying the approval of the BA-USAir alliance until after the deadline had passed. Id.
293 Id. at 2.
294 Id. at 1.
295 Id.
296 Id. at 4-5.
USAir stated, the airlines will be unable to realize the true gains of free competition as envisioned in the concept of deregulation.297

4. DOT Failed to Take First Step in Global Aviation

Early on, the Big Three, in a rare period of cooperation, utilized all resources to ensure that the DOT did not separate the issue of the alliance from that of bilateral liberalization between the U.S. and its British counterpart.298 They believe that it would have been a mistake fatal to the U.S. airline industry for the DOT to have failed to see the connection between the two issues.299 The Big Three, and in fact both coalitions, hired some of the most powerful lobbyists to represent their views in Washington.300

The Big Three called for open skies immediately after the announcement of the original deal.301 The DOT, however, was quick to state that it would not relate the issues of bilateral liberalization and the BA-USAir alliance, and it would therefore not require a quid pro quo from the U.K. "as the price of approval" for the alliance.302 It was soon clear, however, that the Big Three had gained an upper hand and had motivated the Bush Administration to start talks with the U.K. on the liberali-

298 Andrews, supra note 220, at D1.
299 See American Airlines et al., supra note 2, at 5 (claiming that the alliance would have been a "direct assault" on the U.S. airline industry). Their concern stated basically that BA would obtain control over USAir and thus maintain a global franchise while being served by the alleged protectionist policies of its own country. Id. Beyond the immediate circumstances, the Big Three also feared that this alliance would have set a precedent for other foreign carriers to enter and gain great benefits from the U.S. markets while their governments refuse reciprocal treatment of U.S. carriers, thus destroying the latter's ability to compete. Id.
300 Andrews, supra note 220, at D1. Airlines on both sides of the deal hired top lobbyists. The Big Three were represented by the firm of William E. Brock, who was the U.S. trade representative and later Secretary of Labor under President Ronald Reagan. Id. Howard H. Baker, Jr., former White House Chief of Staff under Ronald Reagan represented USAir and BA in Washington. Id.
301 Schmit, supra note 275, at B1.
zation of the air services agreement between the two countries.\textsuperscript{303} Despite the efforts of top government officials in both countries, the original talks ended in failure.\textsuperscript{304}

In the end, it was clear that as a result of the extreme politicization of the alliance, the DOT changed its position and hinged its approval or lack thereof on the liberalization of the air services agreement between the two countries.\textsuperscript{305} Former Secretary Card, in fact, stated that he might have even been willing to overlook the veto power that BA would have had over the decisions of the USAir board of directors; however, with the current state of the agreement between the two countries, he claimed he would have been unable to approve the deal.\textsuperscript{306} The DOT compelled BA to withdraw its offer and thus faded an opportunity for the DOT to take the first step in showing the world that the U.S. would be a leader in global aviation.

VII. FINAL ANALYSIS - WHERE DOES THE ISSUE OF FOREIGN OWNERSHIP LAND?

In a final analysis of the issue of the antiquated citizenship requirement in the Federal Aviation Act of 1958 and the effect of the DOT’s original informal rejection of foreign investment into USAir, three points must be made. First, the DOT’s open skies initiative would give U.S. carriers a stranglehold on small foreign domestic markets and is unlikely to gain wide support throughout Europe. Second, the politicization of the issue of foreign ownership requirements and the DOT’s connection of the liberalization of such requirements to the issue of open skies agreements will ultimately be detrimental to global avia-

\textsuperscript{303} Card Flies to London for Talks; Majors Remain Critical of DOT, AVIATION DAILY, Oct. 21, 1992, at 115.

\textsuperscript{304} Weintraub, supra note 214, at A4.

\textsuperscript{305} USAir Pilots Disappointed by British Air Decision, PR Newswire, Dec. 22, 1992, available in LEXIS, Tran Library, Air File.

tion. Finally, if the U.S. truly wishes to participate in global aviation, the current inconsistent position of the DOT on the issue of foreign ownership is unacceptable. The situation requires the DOT and Congress to liberalize the citizenship requirement in order to take the first step in this globalization process.

A. WILL THE OPEN SKIES INITIATIVE FLY?

It is important to carefully scrutinize the invitation to negotiate open skies agreements that the DOT recently proposed to European countries. On the face of the proposal, it makes sense that in order to have true global air carriers or any real global aviation opportunities, U.S. air carriers must have access to the domestic markets of European countries. The open skies initiative would certainly provide this access. There remains, however, the question of whether European countries will value the benefits of unrestricted access to the U.S. markets as highly as the DOT seems to believe.

For foreign carriers such as British Airways, it seems quite clear that free access to the U.S. domestic market would mean the addition of a major piece to its global aviation puzzle. We have already seen, however, that the U.K. does not deem such benefits sufficient to open up its market and give U.S. carriers free access under an

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307 U.S. to Explore Open Skies Agreements, supra note 277.
309 See Richard W. Stevenson, British Air's World is Growing, N.Y. TIMES, Dec. 18, 1992, at D1. BA is currently in the process of positioning itself as a true global airline. Id. The airline's recent alliances and deals around the world include the following:

(1) a 25% stake in Australia's Qantas Airlines for $450 million giving BA access to South Pacific routes;
(2) a 49.9% stake in France's TAT European Airways for $108 million;
(3) a 49% stake in Germany's domestic carrier, Deutsche BA;
(4) a proposed joint venture with Aeroflot in Russia to create a new airline, Air Russia, that will serve Europe, the U.S. and Asia from Moscow.

Id.
open skies initiative.\textsuperscript{310} Furthermore, British Airways itself stood by its government's decision to refuse such access.\textsuperscript{311} It seems extremely likely that if a country with such a powerful air carrier as BA would not see fit to open its routes to U.S. carriers in return for the benefit which an alliance with a U.S. carrier would give BA, other smaller European countries will not rush to take advantage of the DOT's proposal for free access.

It seems more logical, however, that European countries will be extremely reluctant to open their markets completely to U.S. carriers. Although access to U.S. markets might initially appear to benefit European carriers, they will likely be unable to stand the competition from U.S. carriers in their own countries, much less be able to compete with the Big Three on a global scale.

While it is true that many foreign carriers are owned wholly or partially by their home governments,\textsuperscript{312} this does not necessarily indicate that they would be more able or willing to accept the open skies initiative. France's recent renunciation of its air transport agreement with the U.S.\textsuperscript{313} serves as a good example. France owns and operates Air France.\textsuperscript{314} While the 40-year-old agreement between France and the U.S. placed "no firm limit on U.S. carrier capacity,"\textsuperscript{315} U.S. carriers have offered extensive service to Paris over the last decade, including service from secondary points within the U.S. As a result, Air France's market share in France dropped from forty-five percent to thirty percent.\textsuperscript{316} It is certainly easy to see how the financially capable U.S. carriers could have this effect on local air carriers in other foreign countries, thus making the prospect of open skies very unappealing.


\textsuperscript{311} Id.

\textsuperscript{312} See Woerth, \textit{supra} note 196, at 34 (chart 1) (listing level of government ownership in many foreign carriers).

\textsuperscript{313} France Gives Up Pact, \textit{supra} note 23, at 39.

\textsuperscript{314} See Woerth, \textit{supra} note 196, at 32 (chart 1).

\textsuperscript{315} France Gives Up Pact, \textit{supra} note 23, at 39.

\textsuperscript{316} Id.
B. The DOT Must Play the Global Aviation Game Fairly

Even though a complete open skies policy is unlikely to achieve wide success, this fact is not an indication that we should not attempt to liberalize, to some degree, our aviation agreements around the world. It is a strong reason, however, not to hinge the assimilation of the U.S. airline industry into the global market on the willingness of other countries to grant free access to U.S. carriers. In other words, the DOT should not hinge approval of such alliances as that between BA and USAir on open skies agreements with the country of the foreign air carrier involved. The DOT must show its foreign counterparts that it is willing to approach global aviation on fair terms.

If the DOT continues to insist that foreign countries open their skies before it liberalizes foreign ownership policies, it will send a negative signal to other countries concerning the United States' commitment, or lack thereof, to participating fairly in future global aviation. By insisting that carriers such as the Big Three gain virtually free access to domestic markets of foreign carriers attempting to participate in the U.S. market, the United States is implying that it will only participate in world aviation if it can have the upper hand and be virtually guaranteed success. Despite recent losses, the Big Three appear to have the ability to infiltrate virtually any European Market that opens its skies. This is in contrast to the inability that a foreign carrier would have to enter the U.S. market which is already under the tight control of the oligopoly.

C. The United States Must Take the First Step in Globalization

The foregoing analysis leads to the suggestion that to realize world aviation, the United States must take the first step to show that it is in fact willing to do so fairly. I

317 See supra note 11 (discussing recent losses of U.S. airlines).
would suggest that this step is composed of two parts. The first part, discussed above, is to depoliticize the issue of foreign ownership of U.S. carriers and to focus instead on the law itself. This means, at least for the time being, that the DOT should separate the issues of foreign ownership and open skies or liberalization agreements. This would allow foreign carriers both the time and an avenue to assess whether access to the U.S. market would be beneficial. Such a step would in effect liberalize the citizenship requirement in the U.S. because by allowing significant foreign ownership without bilateral liberalization first, the DOT will be eliminating a threshold test that it has previously imposed on other airlines.

Secondly, the United States should liberalize the outdated language of the citizenship requirement so that the law can adapt to the quickly developing world economy. The current law, which derives from the Federal Aviation Act of 1958, states among other things that in order for a carrier to be a U.S. citizen, two-thirds of its board of directors and other managing officers must be U.S. citizens, and U.S. citizens must also own seventy-five percent of its voting stock. This law limits any one foreign entity to ownership of only twenty-five percent of the voting stock minus any percentage of voting stock that other foreign entities might already own. Such a limit inhibits the ability of large investors to have any influence on the performance of their investments.

With this in mind, this Comment suggests the following change in the statute. The current language of the statute is as follows:

"Citizen of the United States" means . . . (c) a corporation

See supra part VI(B).

See supra note 306 and accompanying text (Secretary Card stating that he would have liberalized the actual control test in BA-USAir alliance but for the current state of air services agreement between U.S. and U.K.).


See McKenna, supra note 1, at 26. In the original alliance with USAir, it was noted that at least at the outset, BA could only buy up to 21% because other foreign interests already owned four percent of the voting stock of USAir. Id.
or association created or organized under the laws of the United States or of any state, territory, or possession of the United States, of which . . . at least 75 per centum of the voting interest is owned or controlled by persons who are citizens of the United States or of one of its possessions.

The statute should be changed to read:

"Citizen of the United States" means . . . (c) a corporation or association created or organized under the laws of the United States or of any state, territory, or possession of the United States, of which . . . at least 51 per centum of the voting interest is owned or controlled by persons who are citizens of the United States or of one of its possessions.

The change in the percentage of voting stock allowed to be owned by foreign entities to forty-nine percent is certainly not a new idea. However, it is an idea that Congress must seriously consider again after the failure of the original proposed alliance between BA and USAir. The change in the percentage of voting stock allowed to be owned by foreign entities to forty-nine percent is certainly not a new idea. However, it is an idea that Congress must seriously consider again after the failure of the original proposed alliance between BA and USAir.

See Stewart, supra note 29, at 716-18.

In fact, immediately prior to the publication of this Comment, the National Commission to Ensure a Strong Competitive Airline Industry recently released its report recommending to the President and Congress that the citizenship requirement be changed to allow foreign ownership of U.S. airlines up to 49% of voting equity. The National Commission to Ensure a Strong Competitive Airline Industry, A Report to the President and Congress 22 (1993). The Commission emphasized that although such liberalization in the long term should be contained with broad-based multi-national agreements, in the short term Congress should allow larger investments under the current bilateral system. Id. The Commission stated specifically:

The Commission appreciates that conclusion of such multi-national agreements will take time, perhaps several years. We believe it is critical, however, for the United States to see the future and shape its strategy today.

While we envision a future in which cross-border airline investment would flow more freely in a more open system, we also believe there is an opportunity today to permit expanded access to international capital markets by allowing larger investments from foreign investors under the current bilateral system. The United States should approve foreign investment of up to 49 percent voting equity in U.S. airlines, in the context of bilateral agreements which are reciprocal and enhance the prospects of securing the ultimate goal of pre-competitive, multi-national agreements. The Commission also believes that in any such 49 percent or other sizable ownership situa-
change will in effect serve two purposes. First, the increased level of voting stock ownership will allow foreign investors to have a higher level of control in the performance of their investments without allowing them to control a majority of a U.S. airline’s voting shares. Thus, foreign interests should be more willing to invest in U.S. carriers that are desperately in need of capital.

Secondly, the change will send a strong message to the rest of the aviation world that the U.S. is ready to truly participate in world aviation and that it is ready to do so fairly. This message should be sent in the hopes that foreign countries will ultimately allow U.S. carriers to access their markets at a significant level. If foreign carriers discover that they can truly benefit from increased alliances with U.S. carriers without losing a foothold in their own markets, they will be less likely to oppose liberalization of bilateral aviation agreements. With such liberalization will come the ever awaited world global aviation industry.

VIII. CONCLUSION

The strict citizenship requirement of the Federal Aviation Act of 1958 must be liberalized. The requirement originated out of the protectionist policies of a U.S. government that had just suffered through World War I. Af-

tion, adequate safeguards should be in place to protect the rights of the remaining shareholders.

*Id.* The Commission then made the following qualified recommendation to change the citizenship requirement:

*We recommend:*

- The Federal Aviation Act be amended to allow the U.S. to negotiate bilateral agreements that permit foreign investors to hold up to 49 percent voting equity in U.S. airlines, providing those bilateral agreements are liberal and contain equivalent opportunities for U.S. airlines; the foreign investor is not government-owned; there are reciprocal investment rights for U.S. airlines, and the investment will advance the national interest and the development of a liberal global regime for air services.

The Commission considers it essential to enforce our currently held rights, particularly when so many of our trading partners are aggressively defending their flagg carriers against our more efficient airlines.

*Id.* at 22–23.
ter the Great Depression, Congress set the requirement at the current level. However, the world economy and the nature of the aviation industry have changed significantly, and global aviation appears to be on the horizon. While the U.S. has a vested interest in being a major player in world aviation, the government and the airline industry as a whole must realize that other countries are essential to the globalization process. The United States, therefore, must adopt both policies and laws that will make it beneficial for other countries to shed their own protectionist policies and participate in the new world market. The first key step which the United States must take is to liberalize the citizenship requirement both in the written law and the DOT application of that law. Once foreign carriers determine they can compete against the U.S. carriers and benefit from U.S. market access through foreign ownership, foreign countries will let down their barriers and open the gateway to true global aviation.