NOTES

TURBULENCE IN THE AIRLINE INDUSTRY: RETHINKING AMERICA’S FOREIGN OWNERSHIP RESTRICTIONS

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I. INTRODUCTION

The dawn of the twenty-first century has proven to be one of the most tumultuous times for the U.S. airline industry. Industry losses have soared past a staggering $40 billion since 2001, sending four of the top seven airlines—United, Northwest, Delta, and USAirways—into bankruptcy protection with others, such as American, narrowly averting the same fate. One estimate put half of all seats on U.S. airlines as belonging to bankrupt carriers. At a time of relative economic growth for the economy as a whole, the airline industry has weathered massive layoffs and pension

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3. See Katie Fairbank, Airline’s Overhaul Almost Certain: Even if It Avoids Chapter 11, Future Will Be Tough, Experts Say, DALLAS MORNING NEWS, Apr. 25, 2003, at 1D; Eric Torbenson, AMR’s Carty Resigns as Union Deal Stalls; Bankruptcy Filing Could Come Today, DALLAS MORNING NEWS, Apr. 25, 2003, at 1A.

fund defaults, including United’s record $9.8 billion pension default in 2005.⁵ As several airlines are seeking new sources of capital as one way to help regain the posture of the aviation industry as a global leader, a law restricting foreign sources of capital continues to hamper their ability to do so. This law requires that U.S. airlines be controlled and owned by U.S. citizens and prohibits foreign investors from owning 25 percent or more of the voting stock of any such airline.⁶ Tracing its roots back to when Calvin Coolidge was president, and strengthened during the presidency of Franklin Delano Roosevelt, the law, which was originally designed to protect an infant industry, has now hamstrung an ailing industry from seeking vital sources of capital. A rethinking of this restriction seems particularly ripe for discussion.

As many in the airline industry push for further liberalization, debate over the law restricting ownership has become more contentious, with labor concerns and protectionist sentiments joining national security concerns to support maintaining the status quo while, on the other hand, commercial interests and various governmental agencies join a global push for liberalization.

Restriction on foreign ownership “appears both in bilateral air transport treaties (whereby each party requires that the other party’s airlines must be majority owned and effectively controlled by the other party’s citizens), and under similarly minded domestic laws (requiring citizens to own and control the State’s airlines).”⁷ This Note focuses primarily on the latter restriction on foreign ownership under domestic laws, but an understanding of the restriction in bilateral agreements is necessary as recent political developments and increasing liberalization efforts in the international realm have shined a critical spotlight on domestic restrictions.

This Note will analyze a recent failed attempt by the Department of Transportation to relax the law’s interpretation, and will recommend an alternative way to modify the law that would ensure transparency while balancing the needs of the industry with the concerns of Congress. Part II provides background on U.S. aviation policy in general, and the law restricting foreign ownership in particular. It provides a history of the U.S. law and describes the significant liberalization of the industry through

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⁶. See infra Part II.A.
Open Skies agreements in recent years. This Note will also discuss the Department of Transportation’s failed attempt to modify its interpretation of the law, coinciding with a widespread backlash against foreign investment in the wake of the Dubai Ports World controversy. It then outlines the Civil Reserve Air Fleet, one of the main national-security-related concerns in any discussion of relaxation of foreign ownership of U.S. airlines, and goes on to describe the Committee on Foreign Investment in the United States ("CFIUS"), which is essential to understanding any potential foreign acquisition that has national security implications.

Part III details a potential solution that would allow the industry to tap into much-needed foreign capital, but in a way that addresses national security concerns and congressional criticisms. This Note proposes that Congress should relax the foreign ownership restrictions on U.S. airlines, but not remove them completely. Rather, it should allow foreign ownership if three conditions are met. The first two conditions favor countries with Open Skies and reciprocal investment opportunities for U.S. citizens, and countries that hold a mutual protection pact with the United States. The third condition seeks to ensure a thorough CFIUS review of any potential acquisition that allows Congress to be kept adequately informed and allows any national security concerns to be effectively addressed. Part III concludes by addressing various uncertainties that may arise in implementing such a solution.

Relaxation of foreign ownership restrictions has been heavily debated in recent years in the aviation industry, the government, and the academic community. Requiring investment reciprocity was identified as one criterion by the Department of Transportation in its failed proposal, while a more transparent CFIUS review process has been increasingly insisted upon by members of Congress. The combination of these two conditions, together with the additional requirement of a mutual protection pact, however, has not been recommended before, and therefore, represents a unique solution tailored to the demands and concerns of the various parties involved.

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8. See infra Part II.C.
9. See infra Part II.E.
II. BACKGROUND ON U.S. AVIATION POLICY AND FOREIGN
OWNERSHIP RESTRICTIONS

A. HISTORY OF THE LAW

Regulation of foreign ownership of U.S. airlines dates back to 1926
with the passage of the Air Commerce Act.\(^{10}\) Under that law, in order for
an aircraft to be registered, the owner must be a “citizen of the United
States,” defined as either a U.S. citizen, a partnership in which all partners
are U.S. citizens, or a U.S. corporation of which the president and at least
two-thirds of the board are U.S. citizens and at least 51 percent of the
voting shares are controlled by U.S. citizens.\(^{11}\) The citizenship requirement
arose from the post-WWI fear of Congress that foreign countries could
control U.S. airlines to the detriment of national security.\(^{12}\)

In the wake of the Great Depression, national security concerns were
supplemented by economic concerns as the chief justifications for the
citizenship requirement,\(^{13}\) eventually codified in the Civil Aeronautics Act
of 1938.\(^{14}\) Much of the focus was on protecting what Congress viewed as
an infant aviation industry that required extensive regulation.\(^{15}\) The
corporate citizenship provision was strengthened to require that at least 75
percent of the voting shares be “owned or controlled by persons who are

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\(^{10}\) Air Commerce Act of 1926, ch. 344, 44 Stat. 568 (1926).
\(^{11}\) Id. §§ 3, 9, 44 Stat. at 569, 573.
\(^{12}\) See Kirsten Böhmann, The Ownership and Control Requirement in U.S. and European
Union Air Law and U.S. Maritime Law—Policy; Consideration; Comparison, 66 J. AIR L. & COM.
\(^{13}\) Id. at 696–97. “Congress intended to support the economic welfare of U.S. air carriers and to
protect the aviation industry from foreign competition. The citizenship requirement was a subtle way to
pursue that goal . . . .” Id. at 697 (internal footnote omitted). See also Isabelle Leleur, LAW AND
POLICY OF SUBSTANTIAL OWNERSHIP AND EFFECTIVE CONTROL OF AIRLINES: PROSPECTS FOR
CHANGE 32 (2003) (“After the Great Depression . . . the state of the economy took its place as a major
element of US national security and law-makers chose ‘protectionism’ as the primary means of
safeguarding the nation’s airline industry.”).
\(^{14}\) Civil Aeronautics Act of 1938, ch. 601, 52 Stat. 973 (1938). The Civil Aeronautics Act,
which also imposed significant regulations on domestic airlines and their routes and fares that lasted
until deregulation in 1978, had a heavy economic focus. See Paul Stephen Dempsey & Andrew R.
Goetz, AIRLINE Deregulation and Laissez-Faire Mythology 163 (1992) (“Among the essential
purposes of the Civil Aeronautics Act was to shield the air transport industry from the hostile economic
forces prevalent in an unregulated economic environment so that the industry could enjoy the stability
required for the acquisition of capital and long-term growth.”).
\(^{15}\) See Dempsey & Goetz, supra note 14, at 160 (stating that “the air transportation industry
was perceived to be in its infancy”); U.S. GEN. ACCOUNTING OFFICE, GAO/RCED-93-7, AIRLINE
COMPETITION: IMPACT OF CHANGING FOREIGN INVESTMENT AND CONTROL LIMITS ON U.S.
AIRLINES 12 (1992) (identifying “protection of the heavily subsidized fledgling airline industry” as a primary
reason why foreign investment and control restrictions were initially placed on airlines).
citizens of the United States," thereby following the precedent set by restrictions on water carriers. The Civil Aeronautics Board, charged with reviewing the citizenship of prospective air carriers, later held in a famous case denying certification to an air carrier that air carriers “shall be citizens of the United States in fact, in purpose, and in management,” and that “[t]he shadow of substantial foreign influence may not exist.”

The Federal Aviation Act of 1958 retained these restrictions, and the Civil Aeronautics Board continued to closely scrutinize air carrier citizenship, holding in another case that it “must look at the substance of a transaction, rather than its form,” and that the applicant bears the burden of showing that the “substance of the transaction is . . . in accordance with the policy, as well as the literal terms of the specific statutory requirements.”

The citizenship requirement was amended in 2003 to reflect the long-standing practice of certifying only those carriers that are both owned and controlled by U.S. citizens. Today, in order to provide air transportation, an air carrier must hold a certificate of public convenience, which can only be issued to a citizen of the United States. The crucial inquiry rests on who or what is considered a “citizen of the United States,” defined in the current statute as:

(A) an individual who is a citizen of the United States;

16. § 1(13)(c), 52 Stat. at 978.
17. Officials in the Department of Commerce had argued before Congress that “serious consideration should be given to the water-carrier precedent of requiring at least a 75-percent ownership, on the part of our nationals, before engaging in certain kinds of commercial enterprise.” Regulation of Transportation of Passengers and Property by Aircraft: Hearing on S. 2 and S. 1760 Before a Subcomm. of the S. Comm. on Interstate Commerce, 75th Cong. 79 (1937) (statement of J.M. Johnson, Office of the Assistant Secretary, Dep’t of Commerce). See also Aviation: Hearing on H.R. 5234 and H.R. 4652 Before the H. Comm. on Interstate and Foreign Commerce, 75th Cong. 261 (1937) (statement of Dennis Mulligan, Office of the Solicitor, Dep’t of Commerce) (providing a nearly identical statement).
18. The Civil Aeronautics Board was the agency charged with reviewing air carrier certificate applications until it was disbanded by Congress in 1984 with airline deregulation; since that time, the Federal Aviation Administration has conducted the review process. See Civil Aeronautics Board Sunset Act of 1984, Pub. L. No. 98-443, § 8, 98 Stat. 1703, 1706 (1984).
24. Id. §§ 41102(a), 40102(a)(2).
(B) a partnership each of whose partners is an individual who is a citizen of the United States; or

(C) a corporation or association organized under the laws of the United States or a State . . . of the United States, of which the president and at least two-thirds of the board of directors and other managing officers are citizens of the United States, which is under the actual control of citizens of the United States, and in which at least 75 percent of the voting interest is owned or controlled by persons that are citizens of the United States.\(^\text{25}\)

Under this definition, foreign persons and corporations can hold no more than 25 percent of the voting shares of a U.S. airline (the ownership requirement),\(^\text{26}\) and the transaction will be further scrutinized to ensure that foreign citizens do not have de facto control of the airline (the control requirement), independent of their actual ownership share.\(^\text{27}\)

**B. OPEN SKIES**

In September 1992 the United States signed the first Open Skies agreement with the Netherlands, representing a major policy shift toward liberalization of air travel.\(^\text{28}\) The agreement removed restrictions on route designations, capacity and frequency controls, and lifted the limit on the number of airlines that could be designated by each country.\(^\text{29}\) This agreement marshaled in a new era of bilateral and multilateral agreements, so that through the end of 2006, there were close to eighty countries with

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25. Id. § 40102(a)(15).
27. See id. at 67; Böhmann, supra note 12, at 698; Office of the Sec’y, U.S. DOT, Docket OST-2005-23307, Order 2006-12-23, Application of Virgin America, Inc. for a Certificate of Public Convenience and Necessity, Order to Show Cause 1, 13 (2006) (denying a certificate to an air carrier because it was found that less than 75 percent of the equity was held by US citizens and that a foreign citizen had actual control, thereby failing both the ownership and control requirements). That airline, Virgin America Inc., was later granted DOT approval following “fundamental and highly constructive changes in its application,” including amending loan and aircraft lease agreements, replacing its CEO, restructuring its board of directors, and establishing a voting trust to administer the 25 percent voting interest held by Virgin Group. Office of the Sec’y, U.S. DOT, Docket OST-2005-23307, Order 2007-3-16, Application of Virgin America, Inc. for a Certificate of Public Convenience and Necessity, Order to Show Cause 1–2 (2007); Office of the Sec’y, U.S. DOT, Docket OST-2005-23307, Order 2007-5-11, Application of Virgin America, Inc. for a Certificate of Public Convenience and Necessity, Final Order 1 (2007).
some form of Open Skies agreement with the United States.\footnote{30}

An important restriction remained with the bilateral Open Skies agreements, however: the nationality clause.\footnote{31} The nationality clause, similar to rules of origins provisions in trade agreements, limits the “right to provide nonstop service between a point of origin in one nation and a destination in a second nation . . . to airlines that are owned and controlled by citizens of the two nations signing the agreement.”\footnote{32} For example, KLM, the main Dutch carrier, could fly from Amsterdam to New York, but not from Belgium to the United States. Further, a non-Dutch carrier was barred from serving the Amsterdam-U.S. route because the airline would not be a “designated” air carrier under the agreement. So while the bilateral Open Skies agreements lifted many restrictions between the United States and the individual countries, the nationality clause contained in the agreements served as a barrier to industry consolidation, while hindering internal liberalization and integration efforts in the European Union (“EU”).\footnote{33}

As the EU pursued greater internal economic and political integration, the nationality clauses of the bilateral treaties signed by several Member States with the United States became increasingly at odds with EU foundational principles of national treatment and freedom of


\footnote{33. Robyn et al., \textit{supra} note 32, at 56. The nationality clause, and ownership restrictions in general, have had wide-ranging implications for the aviation industry, according to one aviation industry expert. Brian F. Havel, \textit{A New Approach to Foreign Ownership of National Airlines}, \textit{in} ISSUES IN AVIATION LAW AND POLICY 13.201, 13.209 (CCH 2003) [hereinafter Havel, \textit{A New Approach}] (“Its cumulative decades-long impact on passenger and cargo costs can scarcely be imagined. It has trapped the air transport industry inside an impenetrable commercial bubble, unable to provide services (and to seize strategic opportunities) with the operational and structural flexibility that is automatically assumed in virtually all other major industries and services.”).}
establishment. In other words, since a main goal of European integration was to remove barriers among its Member States, any agreement between, for example, Belgium and the United States that restricted direct flights from Belgium to the United States to just Belgian air carriers effectively created an additional barrier to political integration on a macro level and to integration of individual European air carriers on a micro level.

As a result, the European Commission challenged several of the bilateral agreements in cases brought before the European Court of Justice (“ECJ”). On November 5, 2002, the ECJ ruled that the bilateral agreements violated foundational principles of the EU: the concept that external agreements are to be negotiated at the European level and freedom of establishment. In particular, the ECJ ruled that the nationality clauses “violate a central treaty principle of freedom of establishment of corporations, in that they provide for the designation only of airlines subject to the ownership and control of the signatory state or its nationals.” In effect the ECJ was saying that this restriction was illegal because it discriminated on the grounds of nationality.

In the aftermath of the rulings, the European Commission stated that the “European Union must urgently agree [to] a mandate for negotiations to replace the existing bilateral [agreements] with the United States with an agreement” at the European, rather than Member State, level. In June, 2003, this mandate to renegotiate an agreement that fully liberalized air travel between the EU and the United States was granted by the Council of Transport Ministers. Daniel Calleja, head of the EU Air Transport Directorate, outlined the bold EU objectives in seeking an agreement by

35. See id. at 23. Cases were brought against Belgium, Denmark, Sweden, Finland, Luxembourg, Austria and Germany, and against the United Kingdom, although the latter had a different type of agreement. Id. at 23 n.1.
36. Id. at 24.
37. Id. For an example of the Court’s ruling that the nationality clause in the bilateral agreements violates European law, see Case C-471/98, Comm’n v. Kingdom of Belgium, 2002 E.C.R. I-9681, ¶¶ 131–45.
38. Doganis, supra note 29, at 63.
calling for removal of restrictions on market access between the United States and the EU and, most strikingly, by calling for a complete relaxation of the foreign ownership restrictions on both sides of the Atlantic in an “Open Aviation Area.” He blasted the current foreign ownership restrictions as “serv[ing] no purpose other than to constrain the normal development of the industry,” and justified their removal by arguing that “the [airline] industry is in crisis [and] we need to rethink our regulatory model. It is an unsustainable situation that in this business, with its impressive growth potential, its fundamentally international character and its high capital needs, [that] access to capital is restricted by government regulation.”

On November 18, 2005, the United States and EU agreed on the preliminary text of a comprehensive air transport agreement, subject to final agreement. The agreement would replace all of the existing bilateral agreements and extend removal of all restrictions on international routes between the United States and EU to all of the Member States, including those with whom the United States currently does not have an Open Skies agreement. While the agreement covered market access and regulatory cooperation provisions, a main sticking point was relaxing foreign ownership restrictions. The EU had identified foreign ownership relaxation as a key priority, while for various reasons to be discussed later, the U.S. position was more complicated.

In negotiating the agreement, the Department of Transportation (“DOT”) sought to relax the restrictions, but the U.S. law itself could only be changed by an act of Congress. A potential solution, on which the EU would temporarily condition its acceptance of the U.S.-EU agreement, was identified by the DOT. The proposal was to change the interpretation of

41. Calleja, supra note 40.
42. Id.
44. Id.
47. See Odessey, supra note 46.
48. See id. The EU ultimately agreed to a First Stage Air Transport Agreement with the United States that did not include an outright removal of the ownership and control restrictions. U.S.-EU Air Transport Agreement, Annex 4, arts. 1, 3, 2007 O.J. (L 134) 4, 28, 29. Rather, the Agreement included a provision that “ownership by nationals of a Member State or States of 50% or more of the total equity
the regulation that defined actual control of U.S. airlines by allowing foreign citizens to invest in U.S. airlines and make certain economic decisions, while safety, security, and other politically sensitive decisions would be reserved for U.S. citizens.49 Jeffrey Shane, Under Secretary for Policy of the DOT, reflected on the proposal that:

Rather than trying to amend the numerical limits in the legislation we would instead address the wholly administrative constraints that, by our assessment, unnecessarily and excessively restrict the activities even of those foreign investors who fully comply with the stringent statutory limits. We thought we were pursuing a far more moderate and evolutionary approach. . . .

Piece o’cake we thought.

... But none of us guessed how much controversy there would be.50

The proposal was immediately controversial and attracted a chorus of supporters pushing for change on the one hand, and a hailstorm of criticism on the other, as it tortuously traversed the political landscape in the following months.

C. DOT’S FAILED ATTEMPT TO RELAX THE RESTRICTIONS: EXECUTIVE BRANCH ACTION WITH EXECUTIVE BRANCH OVERSIGHT

On November 7, 2005, less than two weeks before the United States and EU reached the tentative air transport agreement, the DOT issued a notice of proposed rulemaking seeking to modify the interpretation of “actual control” in its evaluations of air carrier certificates.51 The DOT


49. See Odessy, supra note 46.


argued for the necessity of such a change by stating:

[A]n interpretation of “actual control” that does not recognize the global and structural changes in international finance and thereby take into account new avenues for investment, potentially excludes billions of dollars of foreign investment from airline capitalization sources. Reducing unnecessary regulatory obstacles to the use of cross-border investment will allow U.S. carriers to become more efficient economically, and allow them to continue to be a major presence in the global aviation marketplace. . . .

. . . The industry’s ongoing financial difficulties highlight the need to ensure that our actual control policies do not unnecessarily constrain aviation access to capital.52

The DOT stated that the statutory requirements for determining air carrier citizenship—75 percent voting interest held by U.S. citizens, and president and two-thirds of the Board of Directors are U.S. citizens—would be unchanged.53 Rather, the interpretation of whether the airline was under the “actual control” of U.S. citizens, routinely made by the DOT on a case-by-case basis taking into account the totality of the circumstances, would be modified to allow foreign citizens control over certain aspects of the airline’s operations.54 The DOT proposed that where foreign citizens are significantly involved in an airline and “where their home country does not deny citizens of the United States reciprocal access to investment in their carriers and does not deny U.S. carriers full and fair access to their air services market, as evidenced by an Open Skies agreement,” actual control can be satisfied when U.S. citizens remain in control of “[a]ll necessary organizational documentation,” and in control of decisions relating to the Civil Reserve Air Fleet, Transportation Security Administration requirements, and FAA safety requirements.55

The Aviation Subcommittee of the House of Representatives held a hearing in February 2006, focusing on the DOT’s proposed rulemaking.56

52. Id. at 67,393. Some academic commentators go even further in calling for a complete removal of the foreign ownership restrictions. See HAVEL, supra note 26, at 63 (commenting that the “chauvinistic preference for national ownership has had a significant corollary that sets airlines apart from most other transnational economic enterprises: they have not become multinational corporations”); LELIEUR, supra note 13, at 40 (arguing that “it has become clear that the time has come to drop national restrictions on ownership and control of airlines altogether”).
54. Id. at 67,390, 67,394.
55. Id. at 67,396.
Many of the Representatives voiced their opposition to the proposal, arguing that the DOT did not have the authority to modify its interpretation of “actual control” and that more foreign investment in U.S. airlines would be detrimental to the industry and to the country. The sentiments that only Congress had the authority to change the regulations or laws of foreign ownership echoed some views emanating from other commentators. Some members of the industry, including those representing the Air Line Pilots Association and the AFL-CIO, as well as the head of Continental Airlines, also voiced their opposition to the DOT proposal.

There was considerable support for the proposal, however, coming from representatives of executive branch agencies. Jeffrey Shane, Under Secretary for Policy of the DOT, defended the proposal by arguing that “we felt an absolute obligation, given the amount of change that has taken place in the airline industry [in the past sixty-five years], both here and abroad, to reexamine that interpretation and see whether or not, in fact, it continued to have relevance to today’s circumstances.” John Byerly, representing the Department of State, reminded the Subcommittee of the importance of the U.S.-EU Open Skies Agreement as a way for the United States and Europe to “send a message to all the world that the days of protectionist bilateral agreements are drawing to a close, and that open markets and airline

[hereinafter House Hearing].

57. See, e.g., id. at 3 (testimony of Rep. Costello) (expressing serious concerns about allowing greater control and stating that Congress “should have the authority to issue a final opinion and to legislate on this matter”); id. at 5 (testimony of Rep. Oberstar) (“[I]ts purpose is to hand over U.S. airlines at their most vulnerable moment to their international trade competitors.”); id. at 8 (testimony of Rep. Poe) (“We do not need foreign investment in U.S. air carriers. Do we really want foreign countries controlling the American skies?”).

58. See Kamen, supra note 22, at 17 (“DOT cannot change this fundamental policy by rulemaking. . . . If DOT continues its rulemaking and attempts to usurp the powers of Congress, opponents are certain to petition for review of the DOT decision.”). But see Havel, Portents of Change, supra note 7, at 13,216–18 (recognizing that the proposal could be subject to judicial challenge but arguing that it would likely survive any such challenge).

59. See House Hearing, supra note 56, at 51–53 (testimony of Captain Duane Woerth, President, Air Line Pilots Ass’n) (supporting the Open Skies Agreement with Europe, but opposing the DOT’s NPRM); id. at 53–55 (testimony of Edward Wytkind, President, Transp. Trades Dep’t, AFL-CIO) (opposing the DOT’s NPRM as detrimental to the industry and its workforce).

60. See id. at 49–51 (testimony of Jeffrey Smisek, President, Continental Airlines, Inc.) (arguing that the proposal is unlawful, unworkable, and would not increase foreign capital). In addition, Hershel Kamen, Continental’s Staff Vice President wrote an article in which he argues that “[i]ronically, DOT’s willingness to attempt a rulemaking to override Congress has turned the law on its head and confused potential foreign investors rather than assured them, which will guarantee the continued lack of the foreign investment that DOT is advocating.” Kamen, supra note 22, at 19.

competition represent the future.”

Various industry leaders also voiced their support for the proposal, with FedEx’s Rush O’Keefe, Jr. arguing that “[t]o withdraw the policy carrot of the NPRM would . . . signal an acquiescence to protectionism at a time when U.S. carriers want more and not less international opportunities,” and Michael Whitaker, Vice President of United Airlines, contending that “[w]e are looking for opportunities to compete more effectively in that world market, not for regulatory protection against foreign competition or foreign investment.” The head of Hawaiian Airlines also chimed in with support for the proposal calling it “good public policy” given Hawaiian Airlines’ recent experience trying to attract capital as it emerged from bankruptcy.

As the DOT proposed its changes and the House hearing discussed their relative merits, a separate political controversy erupted over the sale of P&O, a British-owned port management company that managed several U.S. ports, to Dubai Ports World. A political firestorm ensued against foreign ownership of U.S. assets that likely doomed the DOT proposal. Many in Congress sought to block the deal and to ratchet up the scrutiny of transactions involving foreign companies. The U.S. political climate had become increasingly hostile to foreign ownership, with calls for relaxing restrictions on such ownership being drowned out by politicians clamoring to assert their national security credentials in advance of midterm elections.

In the wake of the Dubai Ports World imbroglio, the DOT attempted to salvage its proposal and deflect some of the criticism by issuing a supplemental notice of proposed rulemaking. In particular, the DOT

62. Id. at 20–21 (testimony of John R. Byerly, Deputy Assistant Sec’y for Transp. Affairs, U.S. Dep’t of State).
63. Id. at 46 (testimony of M. Rush O’Keefe, Jr., Senior V.P. & Gen. Counsel, FedEx Corp.).
64. Id. at 47 (testimony of Michael G. Whitaker, V.P., Alliances Int’l & Regulatory Affairs, United Airlines).
65. Id. at 48 (testimony of Mark B. Dunkerley, President & CEO, Hawaiian Airlines).
proposed to maintain the reciprocity requirement while “broaden[ing] the scope of the decision-making that must remain under the actual control of U.S. citizens” to include all defense airlift commitments, and all issues related to safety and security.70 If U.S. citizens controlled decisions relating to those three areas, in addition to controlling the adoption and modifications of any organizational documents, “the requirements of our citizenship review would have been met.”71 This interpretation of actual control would therefore allow foreign citizens to manage other parts of carriers’ operations, such as scheduling, branding, and determination of airfares, which would give foreign citizens more say over the commercial aspects of their investments and would therefore, the theory goes, make them more willing to invest in and inject capital into the U.S. airline industry.72

The DOT warned that “competition itself will be thwarted, and thus the public interest disserved, if we were to restrict capital and management from flowing to the airline industry,” and that “our past interpretations of the citizenship requirement have imposed unnecessary and harmful burdens on U.S. carrier access to investment capital.”73 The DOT substantiated its proposal by stating that “[i]f the U.S. domestic airline industry is to regain its global leadership position, artificial limitations on the ability of long-term strategic investors, regardless of nationality, to participate in the industry and earn adequate returns on their investment need to be removed.”74

The original proposal had ignited intense public interest, as the DOT had received roughly thirty comments from carriers, unions, and industry associations and over 3000 comments from others by the time it issued the supplemental notice of proposed rulemaking.75 Further, members of the House introduced a bill that sought to delay the DOT’s rulemaking process, claiming that the “proposed new interpretation that ‘actual control’ does not require control of significant portions of an airline’s operation is contrary to the plain language of the statute.”76 The DOT had attempted to

71. Id. at 26,430.
72. See id. at 26,426, 26,430.
73. Id. at 26,428.
74. Id. (quoting Comments of United Air Lines, Inc., Notice of Proposed Rulemaking Actual Control of U.S. Carriers, Before the Dep’t of Transportation, Docket No.OST-03-15759, at 4 (Jan. 6, 2006)).
75. Id. at 26,427.
address this criticism by arguing that it was the agency responsible for promoting competition and access to capital and encouraging efficiency in the industry under 49 U.S.C. § 40101(a)(6), (e)(1). The Congressional bill also challenged the Department’s authority by claiming that “[a]ny major change in the definition of ‘actual control’ should only be accomplished through the legislative process and should not be unilaterally imposed by the executive branch.”

Next, it was the Senate’s turn to discuss the DOT proposal, which it did by holding a hearing in May 2006 to discuss the supplemental notice of proposed rulemaking. Senator John McCain voiced his support for the proposal while expressing a sense of resignation by stating that “we’re back to the old protectionist issue again, and since we made so little progress . . . we will probably continue these protectionist policies . . . to the detriment of [the] American economy, to the detriment of the American airlines, and certainly to the detriment of the airline passenger.” Representative John Mica, who chaired the House hearing, also testified to his support of the proposal, pointing to the “economic benefits to consumers, economic opportunities, jobs, [and] creation of new opportunity for some of our struggling carriers in our industry.” Many of the same panelists from the House hearing were present at the Senate hearing and echoed their earlier sentiments, both for and against the proposal.

In the face of substantial opposition, the DOT eventually withdrew its proposal in December 2006. The DOT continued to view the existing

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77. Actual Control of U.S. Air Carriers: Notice of Proposed Rulemaking, 70 Fed. Reg. 67,389, 67,393–94 (Nov. 7, 2005) (to be codified at 14 C.F.R. pts. 204 & 399). See also 49 U.S.C. § 40101(a), (a)(6) (2000) (“T]he Secretary of Transportation shall consider the following matters, among others, as being in the public interest and consistent with public convenience and necessity: . . . placing maximum reliance on competitive market forces and on actual and potential competition . . . to encourage efficient and well-managed air carriers to earn adequate profits and attract capital.”); id. § 40101(e), (e)(1) (“T]he Secretaries of State and Transportation shall develop a negotiating policy emphasizing . . . strengthening the competitive position of air carriers to ensure at least equality with foreign air carriers, including the attainment of the opportunity for air carriers to maintain and increase their profitability in foreign air transportation.”).

78. H.R. 4542 § 1(9). The bill had 198 cosponsors and paralleled a bill in the Senate. H.R. 4542; S. 2135, 109th Cong. (2005). While neither bill was passed, their introduction showed that many in Congress were antagonistic toward the DOT rulemaking proposal.


81. See id.

rules on actual control as “unduly complex and burdensome” and noted that “antiquated notions . . . continue[d] to apply to the airline industry.”\footnote{Actual Control of U.S. Air Carriers: Withdrawal of Certain Proposed Amendments, 71 Fed. Reg. 71,106, 71,106 (Dec. 8, 2006).} Further, the DOT lamented that “retention of the anachronistic administrative standard for determining actual control serves no discernible policy interest of the United States,”\footnote{Id. at 71,108.} but recognized that “more public discussion of the underlying issues is warranted,” and that it would be more capable of advocating its policy objectives outside the “constraints of a specific rulemaking proposal.”\footnote{Id. at 71,109.}

Some members of Congress immediately welcomed the withdrawal, including Representative Oberstar, who declared that the rulemaking proposal would have allowed foreign investors and governments control over the U.S. airline industry and that any such change should come through congressional legislation, not from the rulemaking process.\footnote{Press Release, Rep. Jim Oberstar, T&I Members Praise DOT Move on Airline Ownership Rules (Dec. 5, 2006) (on file with author).}

John Byerly of the State Department summarized that the proposed rulemaking:

ran into a firestorm of opposition in the United States, based on national security concerns and homeland security concerns. It was eventually melded into the huge battle over the Dubai Ports controversy in the United States. And after a full year and plenty of battle scars to show for it, the Administration has decided this is simply not going to work . . . . It’s not politically possible at this time.\footnote{John Byerly, Deputy Assistant Sec’y of State for Transp. Affairs, U.S.’s Byerly Reaffirms Commitment to Finalizing Transatlantic Air Services Accord, Media Roundtable at Brussels (Jan 9, 2007) (transcript available at http://useu.usmission.gov/Dossiers/Open_Skies/Jan1109_Byerly_Roundtable.asp). Given that the EU had linked a decision on the Open Skies agreement to the passage of the DOT’s rulemaking change, the prospects of the agreement going forward were dealt a blow with the DOT’s withdrawal. \textit{See id.} Both sides did, however, “reaffirm[ ] their commitment to the goal of concluding an EU-U.S. agreement.” \textit{Press Release, Delegations of the United States and of the European Community and Its Member States, U.S.-EU Joint Statement on Air Transport Talks} (Jan. 11, 2007) (on file with author). Further, the EU did eventually agree to a First Stage Air Transport Agreement in March 2007 (signed in April 2007) despite the United States maintaining the foreign ownership restrictions of voting stock on its airlines. \textit{See supra note 48 and accompanying text.}}
modify the law and its interpretation, Congress itself had concerns about
the viability of the Civil Reserve Air Fleet and about the CFIUS review
process.

D. THE CIVIL RESERVE AIR FLEET

1. The Primary Concern of Ensuring Program Viability

One of the main concerns in relaxing ownership restrictions on U.S.
airlines is the continued reliability of the Civil Reserve Air Fleet
(“CRAF”). 88 The CRAF is a voluntary Department of Defense (“DoD”)
administered airlift program designed to assist in the movement of military
cargo and personnel during emergencies. 89 CRAF carriers must be U.S.
carriers and must commit 30 percent of its passenger fleet and 15 percent of
its cargo fleet to the program, in addition to at least four crews for each
aircraft. 90

The CRAF program was authorized in 1951 by President Truman 91
and established the following year, after the Korean War, the Berlin Airlift,
and World War II convinced the U.S. military that it would need to turn to
civilian aircraft to augment its own capabilities. 92

In exchange for committing aircraft to the program, certain peacetime
governmental airlift contracts are restricted to CRAF carriers: the
International Airlift Services Contract (military), the Domestic Small
Package Delivery Services program (government cargo), and the General
Services Administration’s City Pairs program (government employees). 93
Of these programs, the City Pairs program is the “prime incentive for major
carriers to participate in CRAF” and represents approximately one-and-a-

88. See, e.g., House Hearing, supra note 56, at 8 (testimony of Rep. Ney) (asking whether the
DOT proposal could “jeopardize” the CRAF program); id. at 10 (testimony of Rep. Pascrell) (citing
“legitimate questions and concerns about the Civil Reserve Air Fleet”); Actual Control of U.S.
to be codified at 14 C.F.R. pts. 204 & 399 (outlining concerns from various comments on the CRAF
program).
89. Ira Lewis, The Civil Reserve Air Fleet: Balancing Risks and Incentives, TRANSP. J., Winter
1998, at 32, 32.
90. CHRISTOPHER BOLKCOM, CONG. RESEARCH SERV., NO. RL3692, CIVIL RESERVE AIR
FLEET (CRAF) 1 (2006).
92. THE BRATTLE GROUP, THE ECONOMIC IMPACT OF AN EU-US OPEN AVIATION AREA 7-1,
93. Lewis, supra note 89, at 36; Factsheet: Civil Reserve Air Fleet, United States Air Force,
half percent of the carrier’s annual passenger revenue.\textsuperscript{94}

The CRAF program is identified as “highly cost-effective” as it provides more than half of the military’s airlift needs by relying on civilian aircraft and the military need only pay for the program if activated.\textsuperscript{95}

The program is activated according to three stages which represent increasing degrees of commitment by the participating carriers: Stage I representing minor regional crises, Stage II representing a major regional war, and Stage III representing a presidentially declared national emergency.\textsuperscript{96} CRAF has been activated only twice since its founding more than fifty years ago: a Stage II activation during Operation Desert Shield/Storm in 1991 to 92 and a Stage I activation during Operation Iraqi Freedom in 2003.\textsuperscript{97}

Thirty-seven carriers were enrolled in CRAF in 2007 and committed a total of approximately 1360 aircraft.\textsuperscript{98} As of 2002 the program was oversubscribed with committed cargo and passenger aircraft far exceeding program requirements.\textsuperscript{99} There have been some warning signs, however, that some carriers may be either unable or unwilling to continue participation in the program. For example, a government report states that “[o]ne of the key stated incentives of the CRAF program—the ability to bid on peacetime government business—may be losing its effectiveness because DOD uses almost exclusively one type of aircraft, the B-747, for its peacetime cargo missions.”\textsuperscript{100} In the first ten months of 2002, the B-747 represented over 94 percent of the missions flown, meaning that some “major CRAF participants who do not have B-747s . . . might reduce or end their participation in the program if they do not receive any business in return for their commitment.”\textsuperscript{101} Another study found that while the airline industry would meet the CRAF needs in the near future, incentives could

\textsuperscript{94} The Brattle Group, supra note 92, at 7-4.  
\textsuperscript{95} Id. at 7-2.  
\textsuperscript{96} Id. at 7-3.  
\textsuperscript{97} Bolkcom, supra note 90, at 3.  
\textsuperscript{98} Factsheet, supra note 93. Many of the major passenger carriers are enrolled in the CRAF, including American Airlines, Continental Airlines, Delta Air Lines, Northwest Airlines, Southwest Airlines, United Airlines, and USAirways. Id. Many cargo operators are also involved, including FedEx Express Airlines and United Parcel Service Airlines. Id.  
\textsuperscript{99} U.S. Gen. Accounting Office, GAO-03-278, Military Readiness: Civil Reserve Air Fleet Can Respond as Planned, but Incentives May Need Revamping 5 (2002) [hereinafter Military Readiness]; Bolkcom, supra note 90, at 7. For example, there were nearly double the cargo wide-body aircraft committed than was required, and more than double the passenger wide-body aircraft committed than was required. See Military Readiness, supra, at 5.  
\textsuperscript{100} Military Readiness, supra note 99, at 7.  
\textsuperscript{101} Id. at 7–8.
be undermined “to the point where participation will fall below needed levels.”

Further, the airline industry’s financial woes, coupled with many carriers’ move toward using smaller planes to trim overall costs, have caused military officials to worry about the reliability of air carriers in the CRAF program. Lieutenant General John Baker stated that he was “concerned about the number of viable, in-business American airlines that are capable,” and that “if the airline industry goes to smaller and smaller airplanes no longer capable of long ranges, we’re going to be in an interesting dilemma when it comes to CRAF.” The worry about the financial stability of program participants was echoed by U.S. Transportation Command Chief General Norton Schwartz, who told the Senate Armed Services Seapower Subcommittee in 2006 that “[w]e depend heavily on [CRAF] on the air side just as we do on the maritime side with our commercial partners. The airline industry is in distress. Three of my [CRAF] carriers are currently in bankruptcy.” While some in the military have argued for a revamped incentive system, more peacetime business for CRAF participants, and even a new military aircraft design, others have suggested allowing foreign carriers to provide airlift capabilities.

2. The Debate Over Foreign Involvement in the CRAF

A report analyzing the U.S. transportation system prepared by several active and retired military members and some civilians found that “[i]n planning for use of the CRAF to supplement military airlift capacity, policymakers will need to consider issues posed by US air carriers entering into long-term alliances with foreign carriers. It may well be time to consider allowing foreign carriers to participate in CRAF.” The report

104. *Id.*
107. See Bennett, *supra* note 105.
108. See *id.*
110. *Id.* at 17.
goes on to find that “[f]oreign carriers already seek participation in US Government travel contracts and chafe under the linkage to CRAF participation. . . . [I]t is appropriate to begin considering means to permit selected foreign carriers to participate in government travel in exchange for contractual commitments to support their . . . partners in CRAF activations.”

A study commissioned by the Office of the Secretary of Defense outlined the potential benefits and risks to CRAF resulting from a relaxation of foreign investment rules, stating that:

liberalizing foreign investment or foreign entry into U.S. markets may be expected to increase available capital and competition in U.S. markets. As a customer of aviation services, DoD should benefit in peacetime and may benefit in wartime from any such changes that contribute to the economic vitality of the industry. Added competition can be expected to strengthen incentives for efficiencies, cost reductions, and service innovations. On the other hand . . . [s]tronger foreign influence increases the risk that international political developments could create conflicts of interest that undermine an airline’s commitments to CRAF.

The study went on to recommend various approaches the DoD could implement to address a change in the ownership laws, including modifying eligibility criteria depending on the amount of foreign ownership and control of a CRAF-participating airline, and codifying a national security review process.

Some of the main worries about a foreign airline participating in CRAF are that a foreign-controlled board of directors might be less reliable, and less likely to honor CRAF commitments in the case of a controversial U.S. military campaign, that foreign crews might be reluctant to fly into hostile areas, and that foreign investors might be subject to pressure, legal and otherwise, from their home governments to withdraw airlift support. These concerns rely on the assumption that U.S. airlines are more dependable to provide CRAF commitments than foreign

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111. *Id.* at 19.
113. *Id.* at 44–50. Some of the proposed eligibility criteria include U.S. registration of aircraft subject to seizure under the Defense Production Act, performance bonds, financial and legal penalties, and assurances from other governments. *Id.* at 45.
114. *The Brattle Group, supra note 92, at 7–7 to 7–8 (quoting an American Bar Association paper on international investment in airlines).*
Given the legal, regulatory, and economic mechanisms available against U.S. carriers, “non-compliance with CRAF contractual commitments is not an option.” A foreign airline, however, is less subject to these mechanisms, and further, “could be compelled by its national government to not comply, and that ‘sovereign compulsion’ could then provide a legal [defense] for the carrier’s conduct.” Adding to the mix the inherently mobile nature of airline assets—namely that an aircraft can be quickly sent outside the U.S. jurisdiction—raises additional questions of reliability of a foreign airline’s involvement in CRAF.

These concerns are mitigated somewhat by the probability that for business and legal reasons, a “foreign owner would want to maintain the airline’s status as a U.S. corporation.” This would make the airline a U.S.-incorporated entity with a U.S. certificate and subject to all U.S. laws and regulations, thereby “giving the US government the same legal control over a [foreign]-owned airline that it has over a US-owned airline.” Therefore, should the foreign-owned, U.S.-registered airline fail to honor its CRAF commitments, the government could seize its aircraft under the Defense Production Act and could revoke its operating certificate. In addition, the “sovereign compulsion” concept would no longer represent a valid defense as the airline would be a registered U.S. corporation subject to the sovereign authority of the U.S. government, not a foreign government.

An important safeguard for ensuring national security concerns are addressed is the CFIUS review process. Understanding the process illuminates how CRAF safeguards could be strengthened and program risks mitigated in any foreign acquisition.

E. THE COMMITTEE ON FOREIGN INVESTMENT IN THE UNITED STATES

An important component of governmental review of foreign
investment in the United States is provided by the Committee on Foreign Investment in the United States ("CFIUS"). Created by an Executive Order under President Ford in 1975, the CFIUS was originally established to serve an advisory role to the president to analyze trends and developments in foreign investments.\textsuperscript{123} Concerned with the rise of Japanese acquisitions in U.S. industries in the 1980s, Congress passed the Exon-Florio provision to grant authority to the president to block acquisitions that threaten national security.\textsuperscript{124} Congress sought to "strengthen the President’s hand in conducting foreign investment policy, while providing a cursory role for itself as a means of emphasizing that, as much as possible, the commercial nature of investment transactions should be free from political considerations."\textsuperscript{125} In response, President Reagan delegated this new authority to the CFIUS, thereby transforming the committee’s role from advisory to supervisory and consequently strengthening the committee’s mandate to review, and even to recommend blocking transactions by foreign investors.\textsuperscript{126}

The Exon-Florio provision, currently codified at 50 U.S.C. app. § 2170, states that the president “may make an investigation to determine the effects on national security of mergers, acquisitions, and takeovers” by “foreign persons which could result in foreign control.”\textsuperscript{127} An investigation is mandatory, however, where any entity controlled by a foreign government attempts to acquire a U.S. company that “could affect the national security of the United States.”\textsuperscript{128} The statute intentionally does not define “national security” so that the term can “be interpreted broadly and without limitation to particular industries.”\textsuperscript{129} The president may take into account the following, among other factors:

1. domestic production needed for projected national defense requirements,
2. the capability and capacity of domestic industries to meet national defense requirements . . . , and
3. the control of domestic industries and commercial activity by foreign

\textsuperscript{125.} \textit{Id.} at 5.
\textsuperscript{128.} \textit{Id.} § 2170(b).
citizens as it affects the capability and capacity of the United States to meet the requirements of national security.  

Notification by companies of potential foreign acquisitions to CFIUS is largely voluntary; however, CFIUS and the president have *indefinite* discretion to review and even enforce divestment of any transaction that did not go through a review. Therefore, any potential acquirer faces a strong incentive to submit a notification in any transaction that might have national security implications, or risk facing significant scrutiny well into the future.

There is also a confidentiality provision in the statute, so that no information regarding the CFIUS review can be disclosed to the public. Interestingly, Congress exempted itself from the confidentiality restriction, leaving open the possibility of keeping Congress informed. In fact, the president must provide Congress with a written report, including detailed findings, of the president’s determination of whether to take action following a CFIUS review.

The CFIUS is chaired by the Secretary of Treasury and is comprised of representatives from several executive agencies, including the Secretaries of State, Defense, Commerce, and Homeland Security, and the Attorney General, among others. The committee members represent diverse interests and concerns, thereby causing a degree of tension; however, “[t]his tension among member agencies is designed to elicit carefully considered judgments that account for a myriad of economic and security considerations.”

There has been considerable debate as to what is perceived as a lack of transparency in the CFIUS review process, particularly with what is shared with Congress. In fact, the CFIUS was heavily criticized for not

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130. 50 U.S.C. app. § 2170(f).
131. See Jackson, supra note 124, at 8–9.
132. 50 U.S.C. app. § 2170(c).
133. Id. (“Nothing in this subsection shall be construed to prevent disclosure to either House of Congress or to any duly authorized committee or subcommittee of the Congress.”).
134. Id. § 2170(g). The CFIUS review process involves an initial thirty-day review, with a forty-five-day extended review for those few transactions that are deemed to require an additional review. Edward M. Graham & David M. Marchick, U.S. National Security and Foreign Direct Investment 35 (2006). There has been disagreement between Congress and the executive branch on the reporting requirements, with the former arguing that a report was required any time a transaction was investigated and the latter arguing that a report was only required when the president decides on a transaction. See id. at 153.
136. Id.
137. See id. at 52.
notifying Congress of its review of the Dubai Ports World transaction.\(^{138}\)

While the president may block a potential transaction, “in practice, CFIUS has focused on mitigating the national security impact of a particular foreign acquisition, as opposed to blocking acquisitions altogether.”\(^ {139}\) Through early 2006, the CFIUS has reviewed a total of 1604 foreign acquisitions, resulting in twenty-five investigations, of which twelve reached the president.\(^ {140}\) Of the twelve that the president decided, only one was blocked.\(^ {141}\) However, such statistics do not give an accurate account of the power of the CFIUS.

A number of transactions were abandoned after informal consultations with CFIUS led the parties to conclude that CFIUS approval would not be forthcoming. . . . Others were withdrawn within the first 30 days of the review process, [which are not reflected in the data]. Even more important, CFIUS has used its power to review transactions to impose strict conditions on foreign acquisitions to mitigate national security concerns.\(^ {142}\)

Robert Kimmitt, Deputy Secretary of the Treasury Department, testified before Congress that “[i]n some cases, CFIUS members negotiate security agreements before a filing is made. In addition, the pre-filing consultation may lead the parties to conclude that a transaction will not pass CFIUS review, in which case they may restructure their transaction to address national security issues or abandon it entirely.”\(^ {143}\)

Before a hearing of the House Financial Services Committee, David Marchick, former official in the State and Commerce Departments and Office of the U.S. Trade Representative, testified that “in the past few years, CFIUS’s scrutiny of transactions has increased, security agreements have become tougher and enforcement and monitoring has been more rigorous.”\(^ {144}\) The stricter scrutiny can be attributed to a heightened sense of national security since the terrorist attacks of September 11, 2001, and also

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138. *Id.* For more discussion on the Dubai Ports World controversy, see *supra* notes 66–69 and accompanying text.


141. See *id.* at 115–16 (statement of Robert M. Kimmitt, Deputy Sec’y, U.S. Dep’t of the Treasury).


143. *House CFIUS Hearing, supra* note 140, at 114 (statement of Robert M. Kimmitt, Deputy Sec’y, U.S. Dep’t of the Treasury).

144. *Id.* at 133 (statement of David Marchick, Partner, Covington & Burling).
to the adding of the Secretary of the Department of Homeland Security to the CFIUS, thereby “shifting the committee’s balance of power significantly in favor of agencies prioritizing security over economic policy considerations.”

The CFIUS, through its various members representing security-related interests, routinely institutes “mitigation measures” to lessen the risk of a foreign acquisition on U.S. national security. These measures “vary in scope and purpose, and are negotiated on a case by case basis to address the particular concerns raised by an individual transaction.”

The DoD, in particular, weighs several factors in its role on the CFIUS, including the importance of the firm to the U.S. defense industrial base, whether the firm is part of the critical infrastructure upon which the DoD relies, and whether national security concerns can be managed through risk mitigation measures, implemented either through regulation or negotiation. Given that the CFIUS operates by consensus, all members must sign off on the transaction and must be satisfied that any mitigation measures effectively address their concerns.

Examples of such measures include negotiation of Network Security Agreements for those transactions involving telecommunications companies; board resolutions, security agreements, and voting trusts and proxy agreements for transactions involving defense contractors; geographic restrictions for transactions involving manufacturing companies; and reassignment of classified contracts to U.S. corporate divisions for transactions involving government contractors.

Despite the increasing rigor with which the CFIUS has scrutinized transactions, and given the controversy over Dubai Ports World, several proposals were introduced in both the House and Senate in recent years to reform the CFIUS. They ranged from: strengthening Congressional oversight of the CFIUS; to heightening reporting requirements to Congress;

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145. See Graham & Marchick, supra note 134, at 58.
146. House CFIUS Hearing, supra note 140, at 114 (statement of Robert M. Kimmitt, Deputy Sec’y, U.S. Dep’t of the Treasury).
147. Id. at 84–85 (statement of Eric S. Edelman, Under Sec’y of Defense for Pol’y, U.S. Dep’t of Defense).
148. See id. at 115 (statement of Robert M. Kimmitt, Deputy Sec’y, U.S. Dep’t of the Treasury).
149. See Graham & Marchick, supra note 134, at 64–69.
150. See id. at 71–73.
151. See Jackson, supra note 124, at 3 (Japanese firm allowed to proceed with acquisition after agreeing to maintain production of military-grade ball bearings in the United States).
152. See id. at 3–4 (French firm allowed to proceed with acquisition after agreeing to transfer classified computing contracts to U.S. parent company).
to increasing the scope of mandatory CFIUS reviews; to restructuring the CFIUS as a congressionally created, rather than executive, committee; to even providing Congress a veto over presidential decisions (although the latter would likely be susceptible to challenge on constitutional grounds). The House eventually passed a bill on February 27, 2007, with bipartisan support and the backing of the White House, that strengthened disclosure requirements of the CFIUS to Congress, codified the CFIUS’s ability to impose mitigation measures, and enhanced scrutiny of transactions involving “critical infrastructure.” The bill passed the Senate and was later signed into law by the president in July 2007.

Edward Graham and David Marchick have recognized the need for greater CFIUS disclosure and have urged development of a “protocol with the relevant congressional committees . . . to establish better ground rules” on information-sharing. Further, they have advocated “frequent, high-level classified briefings to key congressional committees on the types of national security issues that have arisen in [CFIUS] transactions,” thereby increasing mutual dialog and confidence in the review process. They have also argued that confidentiality should be respected throughout the process, with confidential business data remaining undisclosed and with calls for public notice requirements being dropped.

The CFIUS has transformed greatly since its creation in the 1970s, and it will likely continue to do so in the near future as Congress and the executive branch each seek to shape the committee’s role. Despite the controversy over its application of the review process, many would agree that it has played an increasingly important and visible role in the past few years, and that any change in foreign ownership laws and regulations would need to address the CFIUS.

157. Id. at 155.
158. See id. at 154–56.
III. A POTENTIAL SOLUTION: LEGISLATIVE BRANCH ACTION
WITH COMBINED LEGISLATIVE AND EXECUTIVE BRANCH
OVERSIGHT

A. OVERVIEW

Given the intense debate surrounding the DOT’s failed attempt to modify the interpretation of the foreign ownership laws, particularly the criticisms that it lacked the authority to create or modify a regulation without congressional input, this Note suggests that Congress should take action to relax the foreign ownership restrictions in 49 U.S.C. § 40102(a)(15) so as to facilitate investment in U.S. airlines, to ensure the long-term competitiveness and financial health of the industry, and to harmonize Open Skies agreements with other nations. In order to address national security concerns, such as protecting the viability of the CRAF, the law should not lift the restriction entirely, but rather should incorporate certain conditions on foreign ownership and control. This Note suggests a three-pronged test to balance the financial and economic needs of a global aviation industry with the justifiable concerns surrounding national security. Congress should only allow foreign ownership and control of U.S. airlines when:

1. A majority of the airline’s shares and a majority of the board of directors seats are held by U.S. citizens or by citizens of countries with which the United States has an Open Skies Agreement and which affords reciprocal investment opportunities for U.S. citizens in its aviation industry;

2. A majority of the airline’s shares and a majority of the board of directors seats are held by U.S. citizens or by citizens of countries with which the United States has a mutual protection pact; and

3. Where applicable, the CFIUS has conducted a thorough review and has provided adequate disclosure to both chambers of Congress, and the airline has complied with any risk mitigation measures that any member of the CFIUS has deemed necessary to ensure national security, particularly relating to the CRAF.
1. Open Skies/Reciprocity

The first prong requires that foreign investors be from a country with which the United States has an Open Skies agreement and in which reciprocal investment opportunities for U.S. citizens are allowed. In other words, if a company from Country A wishes to invest in a U.S. airline, and the United States and Country A have an Open Skies agreement, and a U.S. company would be allowed to invest in an airline from Country A, the first prong would be satisfied. Conversely, the first prong would not be satisfied if a company from Country X wanted to invest in a U.S. airline and the United States and Country X do not have an Open Skies agreement, or Country X prohibits U.S. control of an airline.

This prong would introduce a degree of fairness and economic alignment of interests between the United States and the foreign citizen’s country. It is similar to one of the DOT’s requirements in its proposal to change its interpretation of actual control. The DOT stated that comments received were generally supportive of this aspect of the proposal. The DOT also claimed that this aspect would be relatively easy to implement administratively as it would “apply longstanding Department practice,” and applicants seeking certificates through the DOT would bear the burden of establishing that reciprocal investment conditions exist.

The Department of State maintains a list of current Open Skies partners, which as of July 2007 represented over ninety countries. In terms of reciprocity of investment opportunities in the aviation industry, the list is narrower. If the U.S.-EU second stage negotiations of the Air Transport Agreement are successful in removing ownership and control restrictions between the United States and the twenty-seven EU Member States, with full reciprocal investment rights and rights of establishment, citizens of the EU Member States would satisfy this condition. Also, a
handful of other countries have already lifted some foreign ownership restrictions on its aviation industry, according to the WTO World Trade Report 2005. Theses include Australia (no ownership restrictions for purely domestic operators), Chile (no restrictions on airlines as long as its principal place of business is in Chile), Indonesia (abolished ownership restrictions in 2000), Peru (allows 70 percent foreign ownership), and Singapore. Given the somewhat varied relaxations, the United States could adopt a mirror image rule, by which reciprocity would be tailored to how far the other country relaxes its restrictions. For example, an Australian company could invest in a purely domestic U.S. airline, as would be allowed in Australia, or a group of Chilean investors could own a U.S. airline, as long its established principal place of business was in the United States.

Australia currently has a cargo-only aviation agreement with the United States, so until and unless an Open Skies agreement is reached, it would not satisfy the first prong. The other countries listed above, however, currently have Open Skies agreements with the United States (or will have with the U.S.-EU agreement). Therefore, citizens from the EU Member States, Chile, Indonesia, Peru, and Singapore would satisfy the first prong.

Allowing foreign investors to invest in U.S. airlines based on whether they come from countries that allow reciprocal investment opportunities may instill a degree of fairness, but it does not necessarily mean that CRAF commitments would be honored. In other words, alignment of economic interests does not necessarily translate into alignment of security interests. Therefore, an additional condition needs to be added.

2. Mutual Protection Pact

The second prong focuses on U.S. security interests, rather than purely commercial interests. To increase the probability that CRAF commitments would be honored, thereby buttressing national security assurances, foreign investment in U.S. airlines should only be allowed when the foreign

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165. Id. at 228.
166. Open Skies Partners, supra note 30.
The investor is also from a country with which the United States has a mutual protection pact. For purposes of this prong, mutual protection pact might be defined as a “ratified and in-force treaty in which the parties agree to render mutual aid in the event of an armed attack on one of the parties.” A prime example in this regard is the North Atlantic Treaty Organization, under which Article 5 reads:

The Parties agree that an armed attack against one or more of them in Europe or North America shall be considered an attack against them all; and consequently they agree that, if such an armed attack occurs, each of them, in exercise of the right of individual or collective self-defense . . . will assist the Party or Parties so attacked by taking forthwith, individually and in concert with the other Parties, such action as it deems necessary, including the use of armed force, to restore and maintain the security of the North Atlantic area.167

Article 5 of NATO has been invoked only once since its inception, which was in the aftermath of the September 11, 2001, attacks.168 After invoking the mutual defense clause, NATO members proceeded to provide support to the United States by patrolling U.S. airspace under Operation Eagle Assist.169 This move shows a degree of willingness by the United States to trust and rely upon its allies in aviation security matters.

Another such treaty is the ANZUS treaty with Australia which states that “the Parties separately and jointly by means of continuous and effective self-help and mutual aid will maintain and develop their individual and collective capacity to resist armed attack”170 and that “[e]ach Party recognizes that an armed attack in the Pacific Area on any of the Parties would be dangerous to its own peace and safety and declares that it would act to meet the common danger in accordance with its constitutional processes.”171 Similar treaties have also been forged between the United States and Japan,172 the United States and Korea,173 and the United States

171. ANZUS Treaty, supra note 170, art. IV.
and the Philippines.\footnote{174} In addition, several countries in the Western Hemisphere are parties to the Inter-American Treaty of Reciprocal Assistance, also known as the Rio Treaty, which contains a provision in Article 3 that declares that “an armed attack by any State against an American State shall be considered as an attack against all the American States.”\footnote{175}

The following countries would therefore be eligible under this definition: Australia, several states in the Western Hemisphere, Japan, Korea, Philippines, and the NATO countries, including Canada and much of Europe.\footnote{176}

There is statutory precedent in restricting commercial-related and military-related opportunities to countries based on criteria such as the existence of a security pact. For example, the Defense Competitiveness Act of 1993, although never passed into law, involved the Export-Import Bank and sought to give special treatment to foreign entities located in Japan, in a NATO country or in an ANZUS country.\footnote{177} Also, under current arms export control law, the consent of the president of certain sales of defense related services and articles is not required if the recipient is the government of a NATO country, Australia, Japan, or New Zealand.\footnote{178} Therefore, creating criteria related to the existence of a security treaty,

\footnotetext[174]{Mutual Defense Treaty, U.S.-Phil., Aug. 30, 1951, 3 U.S.T. 3947 [hereinafter Philippines Treaty]. One could argue that under this definition, the United States would also have mutual defense obligations with New Zealand, Thailand and others through the Southeast Asia Collective Defense Treaty. Southeast Asia Collective Defense Treaty, Sept. 8, 1954, 6 U.S.T. 81, 209 U.N.T.S. 28 [hereinafter SEATO Treaty]. While the organization ceased to exist in 1977, the collective defense treaty remains in force. TREATIES IN FORCE, supra note 170, at 52. The United States, however, inserted an “understanding” into the original treaty by which its mutual defense obligations become effective only if the attack was one of “communist aggression”; otherwise it would simply perform consultative measures. See SEATO Treaty, supra, 6 U.S.T. at 85.}
\footnotetext[176]{See ANZUS Treaty, supra note 170; Japan Treaty, supra note 172; Korea Treaty, supra note 173; Philippines Treaty, supra note 174; Rio Treaty, supra note 175; TREATIES IN FORCE, supra note 170, at 127. The current members of NATO are Belgium, Bulgaria, Canada, Czech Republic, Denmark, Estonia, France, Germany, Greece, Hungary, Iceland, Italy, Latvia, Lithuania, Luxembourg, Netherlands, Norway, Poland, Portugal, Romania, Slovak Republic, Slovenia, Spain, Turkey, United Kingdom, and the United States. TREATIES IN FORCE, supra note 170, at 127.}
\footnotetext[177]{Defense Competitiveness Act of 1993, H.R. 3158, 103d Cong. § 2.}
\footnotetext[178]{22 U.S.C. § 2753(b)(2) (2000).}
while uncommon, is not without precedent.

Restricting foreign ownership to those countries with which the United States has a mutual defense treaty addresses some concerns about alignment of security interests. This assumes that Craf commitments are more likely to be honored by an investor from a country that has committed itself to militarily and diplomatically assisting the United States in the event of an attack than by an investor from a country with no such commitments. National security concerns, while not eliminated, would be lessened by restricting ownership to nationals of countries that the U.S. Senate and president, through ratification process set forth in the Constitution, have determined to be allies. This requirement would also make the law politically more palatable to Congress and less likely to make an investment in a U.S. airline a contentious issue, as the Dubai Ports World controversy was.

Taking into account the first two prongs, ownership would be restricted to citizens of the following countries: Belgium, Bulgaria, Chile, Czech Republic, Denmark, Estonia, France, Germany, Greece, Hungary, Italy, Latvia, Lithuania, Netherlands, Peru, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, and the United Kingdom. To further augment national security, a third condition would also be applied.

3. Full and Transparent CFIUS Review

Whereas the first two prongs focus on the home countries of the potential investors, this prong emphasizes the actions of the CFIUS. Any proposal that deals with foreign investment in the United States and its potential national security implications must address the CFIUS.

This Note suggests that the CFIUS should improve its information reporting to Congress; in particular, in any transaction involving an

179. The president “shall have Power, by and with the Advice and Consent of the Senate, to make Treaties, provided two thirds of the Senators present concur.” U.S. CONST. art. II, § 2, cl. 2.

180. Note that much of the controversy involving the purchase of P&O Ports North America by Dubai Ports World was not so much that several ports would be run by a foreign company, but that it would be run by a foreign government-owned company from the United Arab Emirates. P&O was a British company already operating the ports, so foreign operation of the ports was not the controversial issue. Had Dubai Ports World been another British company, or a Danish company, or a Swedish company, it is very unlikely to have garnered the same amount of public interest and political condemnation, especially considering the large number of foreign firms that continue to operate U.S. shipping terminals. See Leonard C. Gilroy & Adam B. Summers, Detailing Foreign Management of U.S. Infrastructure: Numerous U.S. Ports, Airports, Roads, Water Facilities Already Run by Foreign Businesses, REASON.ORG, Mar. 15, 2006, http://www.reason.org/privatization/foreign_management_us_infrastructure.shtml.
acquisition of a U.S. airline, the CFIUS should provide adequate disclosure of the committee’s findings to and solicit input from the relevant congressional subcommittees, such as the Aviation Subcommittees of both the House and the Senate. These briefings would be kept strictly confidential, in accordance with 50 U.S.C. § 2170(c), which protects the information contained in the CFIUS filing from public disclosure while expressly allowing disclosure to Congress.181 This improved dialogue with Congress would likely improve public and congressional confidence in the CFIUS process and help ensure that any security-related concerns are adequately addressed. It would also address criticisms that the executive branch has provided inadequate disclosure during the CFIUS review process and previously tried to side-step Congress through the DOT’s attempt to modify the interpretations of regulations. Given the multitude of congressional bills that sought to reform the CFIUS and to delay DOT’s abortive rulemaking process, addressing these criticisms is crucial to any proposal that seeks to modify the foreign ownership restrictions. In fact, the House has already passed a bill with bipartisan support and executive branch backing that strengthens the CFIUS review process and increases disclosure to Congress.182 By ensuring adequate transparency between the executive and legislative branches, relaxation of foreign ownership restrictions could become a political reality.

To further ensure that security concerns are addressed, the CFIUS would continue to operate on a consensus basis, with each committee member signing off on the proposed transaction only after the member is sufficiently assured that the security concerns are addressed. In addition, in cases involving U.S. airlines, the DoD could adopt creative risk mitigation measures to ensure CRAF reliability.183

Time is of the essence when CRAF is activated, so only those provisions that contribute in near-real-time to the dependability of the CRAF commitments should carry much weight. Normal legal remedies could prove inadequate, because [it] is not . . . helpful for DoD to win a judgment six months later from an airline that refused to meet its commitment.184

First, the DoD could make a distinction based on whether, after the

182. See supra note 154 and accompanying text.
183. This idea is supported by several aviation experts, including Brian Havel who argues that “annulment of the foreign ownership laws could be accompanied by measures to make CRAF a compulsory obligation for all U.S.-certificated carriers or at least a pre-condition for foreign investment.” Havel, A New Approach, supra note 33, at 13,219.
184. IDA STUDY, supra note 112, at 44–45.
transaction, the carrier would be a U.S.-based airline with foreign investors, in which case it would be CRAF-eligible, or whether it would operate in the United States as a foreign airline, in which case it would not be CRAF-eligible. In the former case, the DoD would continue to have the normal array of enforcement mechanisms at its disposal, such as seizure of aircraft under the Defense Product Act or revocation of the airline’s operating certificate, should the carrier break its CRAF commitments. On the other hand, the risk level would rise if the carrier would be registered as a foreign airline, and the DoD could therefore refuse to let the airline enter into a CRAF contract.

Second, the DoD could require that the foreign-owned, but U.S.-registered airline draft a standby letter of credit that would be immediately payable to the DoD in the event that it does not follow through on its CRAF commitments. A standby letter of credit is “issued by the seller’s bank and runs in favor of the buyer,” the inverse of a traditional letter of credit. A standby letter of credit is used to insure or guarantee performance on the part of the seller of the service or goods. In this case, the seller would be the CRAF-participating airline, and the buyer would be the DoD. “Banks [in the United States] do not issue guarantees or performance bonds or insurance policies because federal law seems to prohibit such transactions by banks under 12 [U.S.C.] § 24 . . . . However, the use of stand-by letters of credit can accomplish the same results, and has not been prohibited by bank regulatory agencies.”

Finally, even considering risk mitigation measures, if the DoD remains unsatisfied with the reliability of the CRAF commitments, or with any security-related concern for that matter, it could still refuse to recommend that the transaction be approved, in which case the prospective acquirer would likely withdraw its application or face a formal presidential determination that it be blocked. In addition, airlines can continue to make

185. See id. at 45.
186. One study proposes using performance bonds, which are similar in result but not form to standby letters of credit. See id. at 45–46. Their availability is limited, however, by the fact that U.S. financial institutions are generally prohibited from issuing them. See infra note 188 and accompanying text.
188. FOLSOM ET AL., supra note 187, at 330.
informed business judgments as to whether they wish to participate in the CRAF. If a prospective foreign buyer of a U.S. airline decides that any prospective risk mitigation measure would outweigh benefits from participation in the CRAF, it could decide to not be contractually obligated, so the government would not then rely on that carrier. In such a case, the decision considered by the CFIUS would be whether the carrier’s withdrawal would impact national security as it relates to the CRAF, and if so, the CFIUS could adopt appropriate measures. Such measures could include seeking increased commitments from other airlines, or choosing to do nothing at all if the program is sufficiently oversubscribed such that one carrier’s withdrawal would not impact the program. The important point is that the CFIUS would continue to evaluate security risks on a case-by-case basis and would retain the right to take into account the impact of any foreign acquisition on CRAF reliability and dependability.

C. ADDRESSING POTENTIAL UNCERTAINTIES

1. Congressional Intransigence

The main uncertainty in relaxing the foreign ownership restrictions is the potential unwillingness of Congress to take action. Much of the criticism of the DOT’s rulemaking process revolved around the lack of authority of the DOT to take an action that was believed to be more properly the province of Congress. Therefore, a proposal that suggests that Congress modify the law would address this criticism, but must also address the possibility that Congress would refuse to take such action. The political process is incredibly unpredictable and continually subject to influence by a range of shifting conditions, both ephemeral and long-lasting. Members of Congress could fear a political backlash by their constituents, or could want to appear “tough” on national security, and therefore shy away from a proposal that opens the U.S. aviation industry to foreign investment, no matter the economic benefits of such a change, nor the economic detriments of maintaining the status quo. The second and third prongs of this Note have attempted to specifically address the national security factors and should help allay some of those concerns. By limiting foreign ownership of airlines to countries with which the United States has a mutual protection pact (prong 2) and by increasing disclosure to Congress through a strengthened CFIUS review process (prong 3), congressional concerns about the national security implications of such ownership could be largely assuaged.
2. Executive Opaqueness

Another uncertainty is the potential reluctance of the executive branch to be transparent in conducting CFIUS review. Given the past reluctance of the CFIUS to be completely forthcoming to Congress, this is a valid concern. If foreign ownership relaxation, however, was predicated on increased transparency in the CFIUS review process, as it is in the third prong, the executive branch would quite likely agree to the process given its past eagerness for a relaxation of the foreign ownership restrictions, as evidenced by the DOT’s recent rulemaking proposal. In addition, the executive branch largely supported the House bill that strengthened CFIUS disclosure requirements, suggesting that in the future it would be more transparent in conducting CFIUS reviews.

3. CRAF Uncertainty and CFIUS Answers

If the United States is willing to rely upon its NATO allies during a crisis for airspace defense, it should be able to rely upon citizens of those allies that invest in U.S. airlines and contractually commit to the CRAF to honor those commitments. Prong 2 attempts to mitigate some of the concerns over the CRAF by restricting investment opportunities to countries that have a mutual protection pact with the United States. Those concerns, however, would not necessarily be eliminated as there is the potential that a foreign-owned U.S. airline would enter into a CRAF contract, yet refuse to provide aircraft when activated. This is quite an important consideration as it reflects much of the hesitation by the DoD to opening the aviation industry to foreign ownership. Indeed there is always the potential for disagreements among allies as seen in the NATO campaigns in the 1990s and the recent Iraq War. The security agreement requirement ensures some alignment of security interests, but cannot guarantee a perfect alignment.

To help deal with such an uncertainty, the DoD could require, within the CFIUS review process or even whenever an airline wishes to enter into a CRAF contract, a standby letter of credit as described above, which would provide the DoD with immediate access to funds that would be payable should the airline refuse to follow its commitments. Since the CRAF is activated during times of crisis, however, money may not be an ideal substitute to the immediate access to airplanes provided by CRAF

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189. “While raising concern about some details of the bill, the White House moved ahead of the vote to welcome the House efforts to ‘strengthen’ the investment-review process.” Hitt, supra note 154.
190. See supra notes 168–69 and accompanying text.
carriers. Therefore, while a standby letter of credit would financially protect the DoD should a carrier break its CRAF commitments, the more valuable use of a standby letter of credit to the DoD is that it would impose a strong disincentive on the carrier to breaking its CRAF commitments in the first place.

Another possibility would be to include a liquidated damages clause in a CRAF contract where the amount of damages would be specified should the airline breach its contract. This would be an inferior remedy however, because it requires court action which is neither inexpensive nor quick and whose outcome is not certain.

One potential loophole in CFIUS review is that it would only apply to acquisitions, mergers, or other takeovers by foreign investors of a domestic airline. This leaves startups outside the review process. In other words, if a foreign company chose to exercise its right of establishment and start an airline in the United States from the ground up, the CFIUS would likely not apply. But CRAF concerns would likely already be mitigated, because since the airline is starting from the ground up, it would be adding to the aviation capacity in the United States, not taking control of a current CRAF-participating carrier. The DoD could choose on its own whether to allow the startup to enter into a CRAF contract. The reliability of the existing CRAF commitments would be unaffected for the most part, unless the new airline somehow threatens the financial viability of the other airlines. But given that competition in the marketplace is generally a favored public policy, and is expressly stated as a goal of the aviation law, and given that antitrust provisions would likely guard against any illegal anticompetitive practices, a startup would likely not greatly impact the viability of the CRAF.

4. Applicability of WTO/NAFTA Principles

Another potential, yet addressable, objection involves the extent to which the first two prongs that limit ownership to certain countries might infringe upon WTO nondiscrimination principles such as Most-Favored Nation (“MFN”) and National Treatment (“NT”) status. MFN status, as defined under Article II of the General Agreement on Trade in Services (“GATS”), embodies the principle that “each Member shall accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favorable than that it accords to like

191. See supra note 77 and accompanying text.
services and service suppliers of any other country.” 192 In other words, parties to the WTO agree that if they give certain favorable trading terms to one of its WTO trading partners, it will give those trading terms to all of its other WTO trading partners. NT status, as defined under Article XVII of GATS, embodies the commitment that “each Member shall accord to services and service suppliers of any other Member . . . treatment no less favourable than that it accords to its own like services and service suppliers.” 193 In other words, WTO parties are committed to treating foreign service providers no worse that it treats its own.

In the case of aviation, however, there is a specific exemption for foreign ownership restrictions from the WTO. 194 The Annex on Air Transport of GATS states that the Agreement and its dispute settlement procedures do not apply to measures affecting “traffic rights, however granted.” 195 “Traffic rights” are subsequently defined as “the right for scheduled and nonscheduled services to operate and/or to carry passengers, cargo and mail for remuneration or hire from, to, within, or over the territory of a Member, including . . . criteria for designation of airlines, including such criteria as number, ownership, and control.” 196 In addition, air services are excluded from the NT and MFN provisions of Chapter 12 of the North American Free Trade Agreement (“NAFTA”). 197

Therefore, relaxing ownership restriction toward some countries but not others would not currently be subject to the WTO agreement or to NAFTA and would therefore not be subject to challenge by other trading partners on those grounds. 198

193. Id. at art. XVII.
194. See Havel, Portents of Change, supra note 7, at 13,212 (identifying the airline industry’s “exceptional status” that has allowed it to “negotiate its future as an industry apart, freed from the cross-sectoral bartering that other industries must confront in fora such as the World Trade Organization”).
195. GATS, supra note 192, art. XXIX, Annex on Air Transport Services ¶ 2.
196. Id. at ¶ 6(d) (emphasis added).
197. North American Free Trade Agreement art. 1201.2(b), U.S.-Can.-Mex., Dec. 17, 1992, 32 I.L.M. 605, 649. The NT and MFN provisions are found in the Chapter on Cross-Border Trade in Services in Articles 1202 and 1203, respectively. Id. at 649, arts. 1202, 1203. The United States also exempted all of its bilateral and multilateral agreements in force at the date of entry into force of NAFTA from Article 1103, the MFN provision of the Chapter on Investment. Id. at 761, Annex IV, Schedule of the United States. The United States also expressly exempted all future international agreements involving “aviation” from the MFN provision. Id.
198. See WORLD TRADE REPORT 2005, supra note 164, at 249 (“WTO Members have simply used the flexibilities offered by the GATS to maintain [bilateral aviation] agreements as exceptions to the most favoured nation principle.”); Ved P. Nanda, Substantial Ownership and Control of International Airlines in the United States, 50 AM. J. COMP. L. 357, 379 (2002) (“It is . . . debatable whether air
The parties to GATS deliberately chose to exclude Open Skies treaties and foreign ownership restrictions from the agreement because there was the belief that:

the application of the MFN principle to international air transport could hold back the on-going process of liberalization between like-minded states. Given the history of bilateral dealing in this sector, there was a reluctance to see states that are unwilling to take similar market-opening measures enjoy the benefits of liberalisation.\footnote{199}

Further, many members of the aviation industry and their governments wanted to keep the existing processes for liberalization intact as “neither states nor airlines wished to see a dual regulatory regime emerge, particularly in respect of traffic rights, in which some states applied GATS obligations while others held to existing arrangements.”\footnote{200}

There is always the possibility, however remote at present, that the WTO members could expand the agreement’s scope to include ownership provisions in the aviation industry. This change would imply a substantial liberalization of foreign ownership provisions, in which case this proposal would need to be modified. Given that the primary push for aviation liberalization, however, has been through the parties’ individual governmental institutions and through the bilateral and multilateral Open Skies agreements they have negotiated, rather than through the WTO, it is unlikely in the near future that the parties and the aviation industry would agree to subject those existing Open Skies agreements to the WTO and to GATS.

IV. CONCLUSION

In the 1920s and 1930s, protection of a fledgling aviation industry was one of the primary justifications for imposing citizenship requirements on U.S. airlines. In the twenty-first century, not only is this justification no longer applicable, but it hinders the ability of U.S. airlines to gain sufficient capital to remain globally competitive. The other justification for restricting foreign ownership arises out of national security concerns and the viability of the CRAF program, but they can be addressed by both restricting ownership to certain countries that are more likely to be aligned with American strategic interests, and by ensuring that a thorough CFIUS transport services will ever be brought under the umbrella of the World Trade Organization.”).


\footnote{200}{Id.}
review gives all committee members the opportunity to negotiate or even impose risk mitigation measures as a condition of a foreign acquisition of a U.S. carrier. Such a move, coupled with adequate disclosure to Congress, would go a long way to ensure the continued viability of the CRAF and to allay congressional concerns. Further, by having Congress rather than the executive branch implement the change, it would address the criticisms of the DOT proposal that it was usurping Congress’s power.

The airline industry has faced a turbulent and stormy several years. Rethinking and retooling an almost century-old restriction, whose original justifications are either irrelevant or adequately addressable, is necessary if the U.S. airlines are to regain their leadership role in the global aviation industry.