CONFIDENTIAL

SLH

cc: D/Transp.
FCO
DTI
HM-Gen.

10 DOWNING STREET

From the Principal Private Secretary

15 January 1985

Dear Charlie,

I have shown the Prime Minister your letter of 24 December 1984 regarding what you said at Camp David about the interpretation of the Bermuda 2 Agreement and in particular Article 12(4), and she was grateful for it.

You will know that the position of both Governments on these matters has been expounded at numerous meetings between us. I am enclosing an Annex to a Note from the British Embassy in Washington to the Department of State on 6 May 1983, which summarises our position.

It is clear from these notes that our two Governments are in disagreement on the legal issues: the present dispute as to the interpretation and application of the Agreement has now lasted for nearly two years. The Prime Minister's feeling is that there is no alternative to resolving these issues between us on an agreed basis, since air services between our two countries can only take place on terms which are acceptable to us both. The Prime Minister's strong wish is that officials of our two Governments should resume discussions on how this issue can be resolved and a more satisfactory framework established.

Yours ever,

Robin Butler

His Excellency The Honorable Charles H. Price II.

DG2ABK

CONFIDENTIAL

OUTLINE OF MAIN UNITED KINGDOM ARGUMENTS

ANNEX TO THE BRITISH EMBASSY NOTE OF 6 MAY 1983

The informal consultations held in March and the formal consultations held in April revealed that an investigation is being carried out by a Grand Jury at the instigation of the Department of Justic into allegations that United Kingdom designated airlines held tariff discussions and entered into tariff agreements between 1977 and 1982. The nature of the investigation is such as to require the participation under compulsion of those airlines and entails potential criminal sanctions. In addition certain of the matters under investigation by the Grand Jury are the subject of an anti-trust civil action in the United States courts for penal damages.

Where the activities of airlines are authorised and regulated in accordance with an international agreement such as Bermuda 2, the domestic laws of a contracting party may not be used to constrain or regulate those activities, unless either this is expressly provided for or it is necessary in order to implement the Agreement or the laws can be applied in a manner which is not incompatible with the Agreement.

Article 11 (and Annex 2) and Article 12 of Bermuda 2 contain full, self-contained and exclusive schemes for the regulation of competition generally, and capacity and tariffs in particular. Together with the designation article and the route schedule, they are the core of any air services agreement. The unilateral application of incompatible domestic laws (including unilaterally determined enforcement measures) is a breach of the Agreement.

The plain words of Article 12(4) are intelligible and capable of application without any elaboration or need to resort to the travaux preparatoires. The terms employed are not consistent with United States anti-trust law under which tariff agreements are unlawful per se. The expression "tariff agreements" cannot include discussions or concerted practices. The reference to "tariff agreements ... concluded as a result of inter-carrier discussions" necessarily imports a freedom for the designated airlines to enter into such discussions without preconditions imposed by the domestic law of either contracting party. To require them to obtain anti-trust immunity under the Federal Aviation Act before entering into tariff discussions goes further than is legitimate under Article 12(4).

There are further indications that discussions or agreements between designated airlines on tariffs cannot be properly subjected to United States anti-trust law. Nowhere in Bermuda 2 is there any explicit, or even implicit, reference to such law: yet when Bermuda 2 envisages the application of domestic law it says so very specifically eg. the final sentence of Article 12(4), Article 4, Article 5 (1)(B) and Article 13(2). Moreover before 1980 there was no mechanism in United States law by which a non-United States airline could itself obtain either anti-trust immunity for tariff discussions or approval of a tariff agreement if the discussions took place or the Agreement was concluded outside an IATA traffic conference.

In deciding whether to approve a tariff agreement the aero-nautical authorities must necessarily apply the standards and criteria of Article 12(2) rather than the different and inconsistent ones of United States anti-trust law or the Federal Aviation Act.

Resort to the travaux preparatoires does not confirm the United States interpretation. The United Kingdom had

during the negotiation of Bermuda 2 proposed a provision expressly exempting tariff procedures from the anti-trust and restrictive practices legislation of the parties. This proposal was not agreed to: but nor was any provision which would have permitted the application of such legislation. Therefore, given the plain words of Article 12 and the object and purpose of the treaty, the non-adoption of that proposal cannot be construed as acceptance by the United Kingdom that United States anti-trust legislation can apply to tariff agreements.

If an airline is alleged not to have followed the procedure of Article 12(4), how to deal with that allegation should be the subject of consultations under Article 16 of the Agreement and is not a matter to be dealt with unilaterally by one of the contracting parties under its domestic law.

SLHAGH

285

10 DOWNING STREET

From the Principal Private Secretary

15 January 1985

US ANTI-TRUST SUITS

Many thanks for your letter of 14 January to Andrew Turnbull enclosing a draft letter to the American Ambassador.

I enclose a copy of the terms in which I have now written to Mr. Price, together with the enclosure.

I am copying this letter to Len Appleyard (Foreign and Commonwealth Office), Callum McCarthy (Department of Trade and Industry) and Henry Steel (Attorney General's Office).

Miss Dinah Nichols,
Department of Transport.

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10 DOWNING STREET

FERB

Although the draft reply has been worked up by Knightsbridge Briefs over a week, it is still not entirely satisfactory.

(i) I find the third para unnecessarily abrasive for a letter from you to Charles Price

(ii) it does not make point that Charles Price was forced to retract his statement.

AT

14/1

Pl. type the draft attached to Miss Nicholl's letter for my signature.

RB

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DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Andrew Turnbull Esq
Private Secretary
10 Downing Street
LONDON SW1

14th January 1985

Dear Andrew,

US ANTI-TRUST SUITS

Robin Butler wrote to Len Appleyard on 28 December enclosing a copy of a letter from Ambassador Price covering a point he made at the Camp David discussions on the current anti-trust suits.

I enclose the draft of a reply which the Prime Minister might send to Ambassador Price. It has been agreed at official level between ourselves and the Foreign Office.

I am copying this to Len Appleyard (Foreign & Commonwealth Office), Callum McCarthy (Trade & Industry), and Henry Steele (Attorney General's Office).

Yours,

Dinah

MISS D A NICHOLS
Private Secretary

DRAFT LETTER FROM THE PRIME MINISTER'S PRIVATE SECRETARY

ADDRESSED TO: His Excellency
The Honourable Charles H. Price II

I have shown the Prime Minister ~~Thank you for~~ your letter of 24 December 1984 regarding what you said at Camp David about the interpretation of the Bermuda 2 Agreement and in particular Article 12(4); and she was grateful for it.

You will know that the position of both Governments on these matters has been expounded at numerous meetings between us. ~~Our position was formally summarised in~~ I am enclosing an Annex to a Note from the British Embassy in Washington to the Department of State on 6 May 1983, ~~of which~~ you may like to have a copy, which ~~formally~~ summarised our position.

~~The fact is~~ It is clear from these notes that our two Governments are in disagreement on the legal issues: the present dispute as to the interpretation and application of the Agreement has now lasted for nearly two years. The Prime Minister's feeling is that there is no alternative to resolving these issues between us on an agreed basis, since air services between our two countries can only take place on terms which are acceptable to us both. ~~As you know the current situation is not acceptable to the United Kingdom, but~~ The Prime Minister's strong wish is that officials of our two Governments should resume discussions on how this issue can be resolved and a more satisfactory framework put in place.

NOTE NO 63

Her Britannic Majesty's Embassy presents its compliments to the Department of State and has the honour to refer to the consultations between the Government of the United Kingdom and the Government of the United States, held at Washington on 26 and 27 April 1983, which considered the question whether and to what extent it is consistent with their respective rights and obligations under the Agreement between them concerning air services of 23 July 1977 ('Bermuda 2') for the provisions of United States anti-trust law to be applied to the activities of the designated airlines of the contracting parties. The consultations on this dispute were held at the request of the Government of the United Kingdom under Article 16 of Bermuda 2.

During these consultations the United Kingdom delegation gave reasons for its contention that the United States had not complied with certain of its obligations towards the United Kingdom under Bermuda 2. The United States delegation rejected this contention. Although both delegations gave their reasons at some length, at the end of the formal consultations the United States delegation stated that the consultations had not been sufficient to allow for an adequate examination of the points at issue and requested that the United Kingdom's arguments be presented in writing.

The United Kingdom delegation did not accept that the consultations were insufficient, nor did they consider that it was necessary

for their detailed case to be presented in writing. Nevertheles the Government of the United Kingdom are willing to give in outline once again their main arguments on the basis that it is without prejudice to their right to reformulate, modify or expand them as necessary at any future stage of the dispute. The arguments are set out in the Annex to this Note.

If, having reconsidered the arguments advanced during the informal consultations and the first round of formal consultations, and this Note and its Annex, the United States Government considers that a second round of formal consultations might resolve the dispute the Government of the United Kingdom is ready and willing to engage in them. In view of the urgency of the matter and of the fact that the Grand Jury investigation is still proceeding, however, the Government of the United Kingdom will regard themselves free to take such further steps as are open to them under Bermuda 2 to bring about a resolution of the dispute unless a second round of consultations is held within a reasonable period. Given the informal and formal consultations already held, it seems reasonable that any further round should be held and completed during the current month.

In its Note of 14 April 1983, and during the formal consultation the United States delegation expressed the view that the dispute is not one which arises under Bermuda 2. As their delegation said during the formal consultations, the Government of the United Kingdom categorically reject such a contention. The

United States Government has instigated a Grand Jury investigation into alleged breaches of its anti-trust laws by United States and United Kingdom airlines designated under Bermuda 2 in respect of certain activities of those airlines in exercise of their rights granted to them pursuant to that Agreement. The Government of the United Kingdom consider that, on a proper interpretation of Bermuda 2, such an investigation is incompatible with the rights and obligations of the contracting parties, in the light of the object and purpose of the Agreement. They consider that the United States is failing to comply with its obligations under Bermuda 2 by permitting its anti-trust laws to be applied in such a way as to found liability to an award of penal damages in respect of tariff arrangements between airlines which are in the view of the Government of the United Kingdom regulated exclusively by Bermuda 2. The United States disagrees with the United Kingdom Government's interpretation of Bermuda 2 on these matters and, in particular, over the true construction of Article 12. There is thus a dispute as to the interpretation and application of, or compliance with, Bermuda 2, which may be and has been, properly the subject of consultations under Article 16.

In the Embassy's Notes of 29 March and 13 April 1983 the Government of the United Kingdom expressed their expectation that the United States Government would, whilst consultations are pending, ensure that no further steps are taken with regard to the Grand Jury investigation. This expectation was expressed

again during the formal consultations. No further explanation for the refusal of the United States Government to accede to this request was, however, given. Once again, therefore, the Government of the United Kingdom fully reserve their rights and the rights of their airlines with respect to any damage, costs or expenses which they may incur as a result of such refusal, or otherwise.

The Embassy avails itself of this opportunity to renew the assurance of its highest consideration.

British Embassy
Washington DC

6 May 1983

ANNEX

OUTLINE OF MAIN UNITED KINGDOM ARGUMENTS

The informal consultations held in March and the formal consultations held in April revealed that an investigation is being carried out by a Grand Jury at the instigation of the Department of Justice into allegations that United Kingdom designated airlines held tariff discussions and entered into tariff agreements between 1977 and 1982. The nature of the investigation is such as to require the participation under compulsion of those airlines and entails potential criminal sanctions. In addition certain of the matters under investigation by the Grand Jury are the subject of an anti-trust civil action in the United States courts for penal damages.

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A2

In deciding whether to approve a tariff agreement the aeronautical authorities must necessarily apply the standards and criteria of Article 12(2) rather than the different and inconsistent ones of United States anti-trust law or the Federal Aviation Act.

Resort to the travaux preparatoires does not confirm the United States interpretation. ~~that~~ The United Kingdom had during the negotiation of Bermuda 2 proposed a provision expressly exempting tariff procedures from the anti-trust and restrictive practices legislation of the parties. This proposal was not agreed to: but nor was any provision which would have permitted the application of such legislation. Therefore, given the plain words of Article 12 and the object and purpose of the treaty, the non-adoption of that proposal cannot be construed as acceptance by the United Kingdom that United States anti-trust legislation can apply to tariff agreements.

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EMBASSY OF THE UNITED STATES OF AMERICA
LONDON

December 24, 1984

Mr. F. E. R. Butler
Principal Private Secretary
Prime Minister's Office
10 Downing Street
London S.W.1.

Dear Robin:

In our discussions on civil aviation at Camp David, I mentioned that Article 12(4) of the Bermuda II Agreement specifically referred to US antitrust laws. On further checking, I find that there is no direct reference to antitrust legislation in the article itself.

However, the Bermuda II Agreement does not contain language which creates an immunity from US antitrust laws, and both the negotiating history and subsequent conduct under the agreement indicate very clearly that no such immunity was intended by the United States. Article 12(4) of Bermuda II requires American and British carriers to submit any agreements they may reach to the aeronautical authorities of both countries for approval. Fare agreements that are so disclosed and approved are protected under the US antitrust laws. On the other hand, fare agreements that are not approved by the governments not only fail to comply with Bermuda II, but also violate US antitrust law.

That, of course, is the basis of our position throughout the many months of the Laker investigation and in the numerous consultative meetings held between representatives of our governments. I am enclosing for your information a more detailed memorandum which provides the legal rationale for our approach to the issues under discussion. You may wish to share this letter and the attached memorandum with the Prime Minister.

Again, I enjoyed very much our discussions during the Prime Minister's highly successful visit to the United States. I look forward to seeing you again soon.

Sincerely,

Charles H. Price II
Ambassador

CIVIL AVIATION: Provisions of Bermuda II Relating to Fare Discussions and Agreements

In the discussions of the tariff provisions of Bermuda II in relation to the Laker antitrust investigation and to negotiations on a new aviation regime for the North Atlantic, the British Government has argued that the terms of Article 12(4) necessarily render the antitrust laws inapplicable to intercarrier fare discussions and agreements. In the British Government's view, that provision contemplates that airlines will meet to discuss tariffs and will reach tariff agreements which they are then directed to submit to the UK Civil Aviation Authority and the US Civil Aeronautics Board for approval before implementation of the agreed individual fares as may then be approved under Article 12(5). According to the British Government, such discussions are necessarily contemplated and authorized by the fare setting process established by Bermuda II.

In the view of the United States Government, Article 12(4) and other provisions of Bermuda II do not support the British Government's position regarding the rights of private parties to enter into undisclosed fare discussions and agreements without regard to US antitrust law.

Briefly, the Article 12(4) tariff provisions do not contain undertakings which preclude the applicability of US antitrust laws to an undisclosed tariff agreement concluded in a forum to which antitrust immunity has not been expressly provided. Article 12(4) does not promise an unfettered liberty to reach tariff agreements. It only states that tariff agreements, if and when concluded, must be submitted for approval.

Indeed, Article 12(4), when read in conjunction with Article 12(9), requires disclosure of intercarrier discussions and agreements. Article 12(4) specifies that any such agreements "will be subject to the approval of the aeronautical authorities" of the two governments and "shall be submitted" under specified procedures. This language clearly obligates the airlines to disclose. Furthermore, Article 12(9) states that, during the pendency of consideration of approval for these agreements, the two governments may exchange views and recommendations which will be taken into consideration by the other government if requested. Therefore, by necessary implication, Bermuda II effectively requires that both governments be notified of the agreement, that the governments will foster disclosure adequate to allow an exchange of views, and that they will cooperate in assessing the acceptability of such agreements.

In addition, the negotiating history makes clear that it was drafted and intended to accommodate the United States unwillingness to provide blanket advance antitrust immunity for intercarrier price discussions, while recognizing that we had a policy of providing immunity for discussions within IATA and had the possibility of extending that immunity to additional intercarrier discussions on specific application.

Finally, we have found no record of any US retreat from its firmly held and articulated position. The compromise language ultimately adopted as Article 12(4) was based on a US proposal to protect our antitrust authority. Hence, we conclude that the negotiating history demonstrates the intent of the US to assure the continued application of the antitrust laws and the UK understanding of that intent.