

**FINAL NON-BCI VERSION  
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***EUROPEAN COMMUNITIES AND CERTAIN MEMBER STATES –  
MEASURES AFFECTING TRADE IN LARGE CIVIL AIRCRAFT***

***(WT/DS316)***

**COMMENTS OF THE UNITED STATES OF AMERICA  
ON THE ANSWERS OF THE EUROPEAN COMMUNITIES  
TO THE PANEL'S ADDITIONAL QUESTIONS**

**February 8, 2008**

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*European Communities and Certain Member States –  
Measures Affecting Trade in Large Civil Aircraft (DS316)*

**Comments of the United States on the  
Answers of the European Communities  
to the Panel’s Additional Questions**

February 8, 2008

1. The United States thanks the Panel for the opportunity to comment on the answers of the European Communities (EC) to the Panel’s additional questions.
2. Before commenting on particular answers, the United States calls the Panel’s attention to a request by the United States in paragraph 36 (end of comments on Question 253) of this submission. In light of the EC’s continuing failure to make available requested documents that are presumably accessible to EC officials, the United States has requested that the Panel again ask the EC to provide the requested material, by February 13, 2008.

**II. QUESTIONS TO THE EUROPEAN COMMUNITIES**

**A. LAUNCH AID / MEMBER STATE FINANCING**

**246. Please provide a copy of the 1981 agreement between the governments of France, Germany, Great Britain and Spain concerning the A300 and A310 projects.**

Comment:

3. The documents that the EC provided in response to this question (Exhibits EC-941 and EC-942) further corroborate the U.S. demonstration that there is a Launch Aid Program that is a subsidy in its own right (distinct from individual provisions of Launch Aid) through which the EC is causing adverse effects to the interests of the United States. As explained in previous submissions, the existence of the Launch Aid Program is substantiated by, *inter alia*, a series of intergovernmental agreements covering almost forty years; bureaucracies at the national level dedicated to performing the administrative functions necessary to maintain the Launch Aid Program; and formal intergovernmental institutions designed to facilitate decisions on the launch and financing of new aircraft. The Program constitutes a subsidy inasmuch as it is a financial contribution—specifically, “a government practice {that} involves a direct transfer of funds . . . {or} potential direct transfers of funds”<sup>1</sup>—that confers a benefit, in the form of the reduced cost of capital for Airbus by virtue of the financial markets’ expectations of continuing government support.<sup>2</sup>

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<sup>1</sup> Article 1.1(a)(1)(i) of the SCM Agreement.

<sup>2</sup> See, for example, U.S. Answers to Second Panel Questions, paras. 22-25 (response to Question 139).

4. The documents newly provided by the EC reinforce this point. For example, in addition to confirming the roles of the various intergovernmental institutions that make up the Launch Aid Program, the agreements contain the following commitment:

The three Governments, unless otherwise unanimously agreed, will not support the participation of their airframe manufacturers which are parties in the programme covered by this memorandum in the development and production of civil programme {s} competing with Airbus Industrie programmes.<sup>3</sup>

5. This commitment supports the proposition that the Launch Aid Program is prospective in nature. As explained in the U.S. response to the Panel’s Question 136, a measure has prospective application if it is intended to apply to situations occurring after the measure comes into existence.<sup>4</sup> Evidence that the Launch Aid Program meets that description includes the inter-governmental apparatus set up to “reinforce European cooperation in the field of aeronautics,”<sup>5</sup> as well as national bureaucracies set up for the same purpose. The above-quoted commitment reinforces the point. By expressly precluding themselves from supporting their respective manufacturers in projects that would compete with Airbus projects, the governments of France, Germany, and the United Kingdom plainly bound themselves to a course of action applying to situations after the inter-governmental agreement came into existence. Indeed, the quoted language explicitly refers to “Airbus Industrie programmes” (plural) in its non-compete obligations – as opposed to “the programme covered” earlier in the sentence – and thus extends the scope of the cooperation between the governments beyond the individual models supported.

6. Moreover, the EC’s newly provided evidence also undermines the EC’s assertion of a lack of “concerted action”<sup>6</sup> on the part of the Airbus governments to adopt the Launch Aid Program. Contrary to the EC’s portrayal of the inter-governmental agreements, the 1981

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<sup>3</sup> Accords Intergouvernements – Principes de cooperation entre les gouvernements français, allemand et du royaume-uni, clause 5 (1981) (Exhibit EC-941). The same commitment is reaffirmed in the 1981 inter-governmental agreement regarding the A310. *See* Accords Intergouvernements – France, Allemagne, Royaume Uni, Espagne – Extension des accords précédents au programme A310, Art. 13 (Sep. 28, 1981) (Exhibit EC-942 (BCI)).

<sup>4</sup> *See* U.S. Answers to Second Panel Questions, paras. 10-16.

<sup>5</sup> U.S. First Written Submission (“FWS”), para. 93 (quoting 1969 agreement, preamble (Exhibit US-11)); *see also* U.S. Second Non-Confidential Opening Statement (“SNCOS”), para. 43.

<sup>6</sup> EC Comments on U.S. Answers to Second Panel Questions, para. 9.

agreement regarding the A310 goes well beyond a general expression of “cooperation and coordination on proposed new LCA.”<sup>7</sup> It sets out detailed obligations regarding [

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**247. For all LA/MSF contracts requiring per-aircraft levies to be made in terms of a percentage of the turnover obtained from each LCA delivery, please explain how the forecast repayment amounts used in the calculations made in Exhibit EC-HSBI-597 were determined.**

Comment:

7. There is an important discrepancy between the Panel’s question and the EC’s response. The Panel asks the EC, “(f) or all LA/MSF contracts requiring per-aircraft levies to be made in terms of the turnover obtained from each LCA delivery, {to} please explain how the forecast repayment amounts used in the calculation made in Exhibit EC-HSBI-597 were determined” (underlining added). The EC’s response is that “{a}ircraft turnover is a factor in MSF return only with respect to [ ] under [ ] Launch Aid agreements.”<sup>9</sup>

8. There is, however, a clear distinction between “per-aircraft levies,” through which Launch Aid is principally repaid, and [ ] which under some Launch Aid contracts are

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<sup>7</sup> EC Comments on U.S. Answers to Second Panel Questions, para. 9.

<sup>8</sup> See Accords Intergouvernements – France, Allemagne, Royaume Uni, Espagne – Extension des accords précédents au programme A310, Arts. 8 and 9 (Sep. 28, 1981) (Exhibit EC-942 (BCI)). The United States also refers in this context to several statements of the EC in its response to Question 249. There, the EC acknowledges that the terms of repayment under the Spanish A330/A340 Launch Aid agreement were set [ ]. A few sentences later, the EC also clarifies that the the A330/A340 agreement, “consistent with the A320 agreement ... [ ].” The references by the EC to such [ ] re-emphasize the systematic nature of Launch Aid as a program and its operation as a “European industrial policy” in support of Airbus (Airbus Press Release, *Heads of State help Celebrate the A380* (Jan. 18, 2005) (Exhibit US-44); US FWS, para. 85, footnote 70).

<sup>9</sup> EC Answers to Third Panel Questions, para. 3 (emphasis added).

provided for only after [ ]<sup>10</sup>

9. Repayment of Launch Aid is based on levies that are either fixed amounts or amounts based on fixed percentages of the total amount of Launch Aid provided.<sup>11</sup> In none of the Launch Aid agreements, however, are levies set as a percentage of the turnover obtained from an LCA delivery. It follows, then, that the real answer to the Panel’s question is that the type of Launch Aid contract for which the Panel wanted to know how forecast repayment amounts were determined simply do not exist.

10. Instead, what the EC refers to are so-called [ ]. As we have discussed before, such [ ] – in the few instances that they are due – are highly uncertain; occur only at the very end of the life of the plane, if at all; and are often capped in time and/or amount.<sup>12</sup> Therefore, any potential “up-side” from [ ], if any, is not actually relevant from a commercial perspective for the determination of the rate of return expected by Airbus governments on Launch Aid provided to Airbus.<sup>13</sup>

11. The EC’s inclusion of any supposed returns from such [ ] in the expected Launch Aid returns is therefore unwarranted. Moreover, as the United States discusses in more detail in the comment to Question 249 below, such supposed [ ] – even if they were commercially relevant – still do not explain how the EC arrived at the rates of return that it posits

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<sup>10</sup> See also U.S. Answers to Second Panel Questions, paras. 33-35.

<sup>11</sup> See EC Answers to First Panel Questions, para. 92.

<sup>12</sup> See generally U.S. Answers to Second Panel Questions, paras. 33-35. To illustrate: in the case of the [ ] Launch Aid contracts referred to by the EC in its response to question 247, [ ]

[ ] See U.S. FWS, HSBI App., paras. 12-15, 18, 24; International Trade Resources, Calculating Magnitude of the Subsidies Provided to the Recipient Entities, para. 28 (Feb. 5, 2007) (Exhibit EC-13 (HSBI)). Thus, for example, under the [ ] Launch Aid contract, [ ] are [ ] and become due only after the [ ] delivery and only until the total return to government reaches [ ], or [ ] delivery. See [ ]. Exhibit EC-597 (HSBI) confirms that even based on Airbus’ own projections [ ]. See also [ ]).

<sup>13</sup> In any event, as the United States demonstrates below, accepting the use of [ ] and the IRRs put forward by the EC (without tax effects) has no bearing on the determination as to the existence of a benefit. See US comments on EC Answers to Third Panel Questions, paras. 24-25 (response to Question 249) and Exhibit US-685 (HSBI).

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or why those rates are consistently higher than the rates explicitly stated in the Launch Aid contracts.

**248. Please reconcile the differences in the repayment schedules for the French A320 LA/MSF contribution that appear in Exhibit EC-HSBI-597 and Exhibit EC-BCI-83 (Article 5), in particular as regards the number of aircraft sales over which repayments must be made and the amount of the anticipated royalty.**

Comment:

12. None.

**249. Please provide a copy of the LA/MSF contract or other relevant document that substantiates the repayment schedules for the Spanish A320, A330/A340, A340-500/600 and A380 LA/MSF contributions that are referred to in Exhibit EC-HSBI-597. Please explain how the relevant per-aircraft levies and repayment amounts used in Exhibit EC-HSBI-597 were derived.**

Comment:

13. The United States observes several aspects of the EC's response that serve to clarify the several critical issues on which the United States and the EC appear to have little disagreement, namely with respect to below-market rates of return for Launch Aid, the existence of benefit, and the significance of business cases and forecasts as evidence of government expectations.

14. First, the EC confirms once again the below-market level of rates of return on Launch Aid. The EC explains how it calculated Spanish A340-500/600 and A380 Launch Aid rates of return by using long-term government borrowing rates and adding to those a 0.2424% premium.<sup>14</sup>

15. The United States notes that the methodology for calculation of the Spanish A340-500/600 and A380 rates itself already confirms the non-market level of the resulting rate. [ ] substantially understates the additional risks involved in corporate lending as opposed to government lending and in no way takes account of the project-specific risks that characterize Launch Aid. Not only is such a rate substantially below risk-adjusted corporate borrowing rates, but even the general corporate borrowing rate for a company with CASA's credit rating would have been significantly higher. For example, in 1997, the year on which the

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<sup>14</sup> The United States takes note of the fact that the EC no longer refers to the IRRs that take into Airbus' tax rate and refers to U.S. Answers to First Panel Questions, para. 252; U.S. Second Written Submission ("SWS"), paras. 125-132.

A340-500/600 rate calculated by the EC is based, the general corporate borrowing rate for a company with CASA's risk profile was 8.29%, i.e., about [ ] higher than the Launch Aid rate calculated by the EC. Similarly, CASA's general corporate borrowing rates at the time were about [ ] higher than the A380 rate calculated by the EC.

16. Comparison with borrowing rates adjusted for the project-specific risk that characterizes Launch Aid demonstrates that the actual benefit was even greater. As compared to project risk-adjusted benchmark corporate borrowing rates, the Spanish A340-500/600 and A380 Launch Aid rates that the EC puts forward are, respectively, [ ] and [ ] below-market.<sup>15</sup>

17. Second, although the EC's response clarifies how ITR arrived at the rates it used for the Spanish A340-500/600 and A380 Launch Aid, it remains unclear why the EC considers that the rates calculated by its consultant for the purposes of this dispute would be more appropriate to use than the rates stated explicitly in the Launch Aid contracts. This is particularly the case for the A340-500/600 Launch Aid. The EC's consultant calculates a rate based on government borrowing in the year of launch (1997), and the EC considers that number more reliable than a number explicitly stated in a Launch Aid contract, pertaining to the Launch Aid at issue and signed a year after that launch date (i.e., when the rates in the year of launch were certainly already known).

18. Apart from these reservations with regard to the Spanish A340-500/600 and Spanish A380 Launch Aid, the United States notes that the EC continues to leave unsubstantiated the methodology that allows ITR to achieve the "implicit rates" that it applies for other Launch Aid. As discussed above, the [ ] play only a very minor role in the overall return that the government may have expected. Indeed, they represent only a small part of the difference between the contractual Launch Aid rates stated in these Launch Aid contracts and the IRR rates alleged by the EC. The US has tried to "reverse engineer" the EC's calculations to find the other factors that could explain the differences, but has been unable to do so. Nevertheless, it is clear, as the United States has pointed out before, that in addition to the inclusion of potential [ ], ITR's analysis suffers from several methodological flaws that critically undermine its reliability.<sup>16</sup>

19. However, it is noteworthy that even if one were to accept the IRRs proposed by the EC there is no question that Launch Aid confers a substantial benefit. Exhibit US-685 (HSBI) contains a comparison between the IRRs calculated by the EC itself (without the tax effect) and

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<sup>15</sup> See Exhibit US-685 (HSBI).

<sup>16</sup> See U.S. Answers to First Panel Questions, Question 42, para. 252.

the project risk-adjusted commercial benchmark rates as calculated in the Ellis Report.<sup>17</sup> As this exhibit shows, even if one were to accept the EC’s calculations of IRRs in their entirety, a benefit would remain substantial and almost identical in range to the interest rate spreads calculated on the basis of the contractual Launch Aid rates.

20. Third, the United States notes that the EC, in its response, acknowledges the importance of the business cases and the forecast delivery and “refund” schedules in establishing the expectations of the governments at the time of the initial provision of Launch Aid. According to the EC, [

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The United States welcomes this further acknowledgment by the EC<sup>19</sup> that the business cases and forecasts are critical indicia of governments’ expectations when making their decision to grant Launch Aid and thus are extremely relevant to an analysis of export contingency.<sup>20</sup>

**250. Please explain the extent to which the repayment terms of the Spanish A320, A330/A340, A340-500/600 measures involved progressively increasing per-aircraft levies. Please provide a copy of the relevant repayment terms for each of these contracts.**

Comment:

21. None.

**251. As we understand it, Clausula Quinta of the Spanish A340-500/600 contract indicates that the interest rate charged by the Spanish government on the LA/MSF contribution to CASA was [ ] for [ ] of the disbursed funding amount, and [ ] for [ ] of the disbursed funding amount. Please explain how, on the basis of**

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<sup>17</sup> Exhibit US-80 (BCI).

<sup>18</sup> EC Answers to First Panel Questions, para. 9 (response to question 249).

<sup>19</sup> For a similar statement by the EC, the United States also refers to the EC’s Answers to First Panel Questions, paras. 98-101 (response to Question 69). There, the EC notes that “implicit” rates of return on Launch Aid were “explicitly anticipated at the time the parties entered into the MSF contracts” (para. 98) and subsequently refers to the “business case delivery forecasts for these programmes” as a basis for its IRR calculation, noting that “{t}his calculation confirms that the method yields accurate results, and that the Member States base their per-aircraft repayment on the Airbus business case.” (Para. 101, emphasis added)

<sup>20</sup> See U.S. FWS, paras. 346, 366; U.S. SWS, paras. 135, 143. In this context the United States also refers to the [ ] provided in the business case that the EC has now provided as Exhibit EC-958 (HSBI) (p. 8 of 19).

these interest rates, it was possible to arrive at the rate of return for this contract of [ ] that is set out in Exhibit EC-HSBI-597.

Comment:

22. See comment to the EC's response to Question 249 above.

**252. Please reconcile the differences in the repayment schedules for the French A330/A340 LA/MSF contribution that appear in Exhibit EC-HSBI-597 and Exhibit EC-BCI-96 (Article 6), in particular as regards the number of aircraft sales over which repayments must be made, the amount of the per-aircraft levy for the first 200 aircraft sales and the amount of the anticipated royalty.**

Comment:

23. In its question, the Panel observes a discrepancy between two repayment schedules for the French A330/A340 Launch Aid contract: one set out in a document that the EC now informs the Panel is an *amendment* to the French A330/A340 Launch Aid contract (Exhibit EC-96 (BCI)), and the other set out in a document (Exhibit EC-597 (HSBI)) described by the EC as an explication of the Launch Aid rates of return calculated in the ITR Report. The EC seeks to explain this discrepancy by noting that Exhibit EC-597 does, in fact, reflect the repayment terms set out in the newly-submitted *original* French A330/A340 Launch Aid contract (Exhibit EC-948).

24. In so doing, the EC incorrectly suggests that the document it calls the original contract provides the definitive repayment schedule for French A330/A340 Launch Aid. By their own terms, the repayment provisions set out in that document are provisional. Thus, Article 6 of the contract states:

Le remboursement sera obtenu par [ ] . . . .<sup>21</sup>

Article 6 then goes on to state:

Les conditions définitives de remboursement seront celles qui figureront dans le Protocole d'Accord entre l'Etat Français et l'AEROSPATIALE concernant le développement des avions A330-A340, après approbation par le Comité

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<sup>21</sup> Convention 88/90.024.00, Art. 6 (Dec. 13, 1987) (emphasis added) (Exhibit EC-948 (BCI)).

Intergouvernemental du dossier du coût de développement et feront, si nécessaire, l'objet d'un avenant à la présente convention.<sup>22</sup>

25. The “definitive” repayment conditions (as contemplated in Exhibit EC-948) are those set out in the document the EC originally submitted as the French A330-A340 contract (Exhibit EC-96). It follows, therefore, that Exhibit EC-96, rather than Exhibit EC-948, contains the information most relevant to the Panel’s examination of the actual repayment terms for the French A330/A340 Launch Aid contract.

26. Unlike the “provisional” terms, whereby the reimbursement rate for the first [ ] aircraft delivered was to be [ ] percent per aircraft, under the “definitive” terms, the rate is [ ] percent per aircraft.<sup>23</sup> The reimbursement rate for the [ ] delivery remains unchanged at [ ] percent, and the reimbursement rate starting with the [ ] delivery remains unchanged at [ ] percent.<sup>24</sup> The net result is that under the definitive terms, full repayment of Launch Aid is [ ], with [ ] percent repayment as of the [ ] delivery, as compared with [ ] percent repayment under the provisional terms.

**253. Please provide a copy of the A330/A340 LA/MSF agreement between Deutsche Airbus GmbH and the German government, which we understand is referred to in the ITR Report as the "MSF Agreement, November 24 1989".**

Comment:

27. In Question 253, the Panel requested the German A330/A340 Launch Aid agreement from November 1989. Rather than providing this document, the EC points the Panel to the repayment terms contained in *another* document. The EC does not claim, as it does in other answers,<sup>25</sup> that it is unable to locate the document that the Panel explicitly requested, or that it is

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<sup>22</sup> Convention 88/90.024.00, Art. 6 (Dec. 13, 1987) (emphasis added) (Exhibit EC-948 (BCI)).

<sup>23</sup> Compare Convention 88/90.024.00, Art. 6 (Dec. 13, 1987) (Exhibit EC-948 (BCI)), with French A330-340 contract, Art. 6 (Exhibit EC-96) (BCI)).

<sup>24</sup> Under both the provisional reimbursement terms and the definitive reimbursement terms, the number of deliveries after the [ ] delivery required to achieve full repayment of Launch Aid is [ ]. This is because the sum to be reimbursed to achieve full repayment is [ ]. The provisional terms contain a general provision to this effect (referring to [ ]), whereas the definitive terms include an annex (Annex 4) setting out [ ].

<sup>25</sup> See, e.g., EC Answers to Third Panel Questions, paras. 33 (response to Question 257) and 178 (response to Question 278).

otherwise prevented from providing the document. Indeed, it is apparent from its answer that the EC examined that document before asserting that “the repayment provisions in that agreement” were the same as those contained in another document.<sup>26</sup> If those repayment provisions are in fact identical, it is not clear to the United States why, in light of the Panel’s specific request, the EC would refuse to provide the requested document.

28. The EC’s refusal to comply with the Panel’s request is all the more difficult to understand where, as the Panel recognized in its question and the EC acknowledged in its answer, ITR “relied on” the Launch Aid contract itself as the original source for the data it used to conduct its benefit analysis.

29. Without access to the document requested by the Panel and relied upon by ITR and the EC, one can only speculate what *might* exist in that document, whether in the repayment provisions or elsewhere. Rather than speculate, however, the United States requests the Panel to again ask the EC to provide this document that appears to be readily available. In the interest of avoiding further delay, the United States further requests that the Panel require this submission to be made by February 13, 2008, with an appropriate opportunity for the United States to comment thereon.

**254. Does the EC agree with the United States' assertion at para. 172 of its FWS that LA/MSF "covered 100 percent of development costs for the A300, and between 70 and 90 percent of the costs for the A310"? If not, please identify, with reference to the relevant legal instruments or any other documents, what percentage of the development costs for these two LCA were funded by LA/MSF.**

Comment:

30. The EC’s answer establishes that the EC agrees with the United States that Launch Aid covered 100 percent of development costs for the A300, and between 70 and 90 percent of the costs for the A310.

31. After acknowledging this agreement,<sup>27</sup> however, the EC proceeds to digress from the Panel’s question and speak of the relationship between Launch Aid and specific variations of the A300 and A310, citing figures that appear to have no basis in evidence on the record of these proceedings. In so doing, the EC relies, *inter alia*, on data from German Launch Aid contracts

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<sup>26</sup> EC Answers to Third Panel Questions, para. 16.

<sup>27</sup> EC Answers to Third Panel Questions, para. 20 (response to Question 24).

said to be contained in Exhibits EC-601 and EC-602.<sup>28</sup> The United States recalls, however, that these contracts, originally submitted as Exhibits EC-601 and EC-602, were “withdraw {n}” by the EC and instead “replaced” with “model contracts” and an “overview table.”<sup>29</sup> These “model contracts” cannot serve as the basis for establishing amounts that can only be calculated from data contained in the actual German Launch Aid contracts; and, it is undisputed that those exhibits do not contain the entirety of the German Launch Aid contracts. As the actual contracts themselves are not part of the record of this proceeding, neither the Panel nor the United States is able to verify the EC’s assertions regarding the contents of those contracts. The figures cited by the EC, therefore, have no evidentiary basis in this proceeding.

32. Similarly, while the EC asserts that the United States was “inaccurate” in identifying the portion of development costs for A300 and A310 variants covered by French Launch Aid, the EC provides no support for what it alleges to be the correct numbers.<sup>30</sup>

33. The United States also notes that the EC raises again its argument that Launch Aid for the A300 and A310 are “outside the temporal scope of these proceedings.”<sup>31</sup> This argument has already been fully considered and properly rejected by the Panel in its preliminary ruling,<sup>32</sup> and warrants no further discussion here.

34. Finally, the EC advances the erroneous argument that Launch Aid for the A300 and A310 “cannot . . . cause any present adverse effects to US LCA interests,” because “Airbus SAS no longer markets or produces these LCA.”<sup>33</sup> In fact, the A300 and A310 are part of the Airbus LCA family produced and delivered during the period being reviewed by the Panel.<sup>34</sup> Airbus continued to repay Launch Aid for the A300 and A310 under preferential terms and thus continued to receive benefits from that Launch Aid during this period. And, to the extent Airbus had not fully repaid Launch Aid when the A300 and A310 ceased to be marketed and produced

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<sup>28</sup> EC Answers to Third Panel Questions, para. 21 and n.22 (response to Question 24).

<sup>29</sup> Letter from the European Communities to Panel, May 15, 2007.

<sup>30</sup> EC Answers to Third Panel Questions, para. 22 (response to Question 24).

<sup>31</sup> EC Answers to Third Panel Questions, para. 18 (response to Question 24).

<sup>32</sup> Preliminary Ruling of the Panel, paras. 36-57 (July 11, 2007).

<sup>33</sup> EC Answers to Third Panel Questions, para. 19.

<sup>34</sup> See U.S. SNCOS, para. 183.

just seven months ago,<sup>35</sup> the outstanding amounts became grants that confer benefits and through which the EC causes present adverse effects.<sup>36</sup> Therefore, the EC's contention that Launch Aid for the A300 and A310 cannot cause present adverse effects also should be rejected.

**255. Please explain, with reference to the relevant contractual provisions, the extent to which the LA/MSF funds promised by the German government for the A330/A340, A320, A310 and A300 were disbursed in advance of costs being incurred, on the basis of projected expenditure, subject to subsequent adjustment to ensure that total borrowing did not exceed the level of development costs it was agreed would be financed.**

Comment:

35. The Panel's question and the EC's response relate to situations where the Launch Aid actually disbursed may differ, in terms of amount or the way amounts are disbursed over time, from the Launch Aid as originally committed, and to the mechanisms built-into the Launch Aid measure to avoid disbursements of amounts that exceed the level of development costs that was agreed would be financed.

36. In its response the EC points out that the German government [

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37. The United States notes two points with respect to the EC's response. First, it is important to distinguish between, on the one hand, the Launch Aid committed in the Launch Aid agreements and thus available to Airbus at the time of launch and based on the development costs it expects to incur, and, on the other hand, the amount that it may later receive in fact based on actual development costs incurred. When there are minimal differences between the amount committed and the amount actually disbursed, because actual development costs are slightly lower than those on which the Launch Aid commitment was based, this may affect the actual year-to-year cash flow benefit that Airbus enjoys; it does not change the conclusion that there is a benefit conferred upon launch. To put it differently, the committed amount is not unlike a guarantee for Airbus that if its development costs reach the level on which the initial commitment is based the full committed amount of Launch Aid is available (e.g., 100% or 90%

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<sup>35</sup> *Ibid.*

<sup>36</sup> See U.S. SWS, para. 16.

of development costs). The fact that, later, Airbus' development costs are slightly lower or spread out over time in a different way, does not change that initial benefit assessment.

38. Second, the United States recalls that the EC's consultant, ITR, based its analysis of internal rates of return (IRRs) and its quantification of the benefit on a comparison of actual disbursements and projected delivery and repayment schedules. As we pointed out in our previous submissions,<sup>37</sup> in calculating the "amount" of the benefit ITR compared actual disbursement data with projected repayment data. ITR uses the same methodology in trying to come up with what the EC calls the "implicit" IRRs that the EC suggests the Launch Aid contracts provide for. The problem with ITR's approach is that: (i) by using actual disbursement data, it accounts for later than expected disbursements (reducing the "benefit" by increasing the effect of later repayments on the rate of return), but (ii) by using projected repayment data as a comparator, it does not account for delayed repayments (which, given the link between disbursements and the development costs incurred by Airbus will often occur precisely when disbursements are also delayed). As a result, the use of actual disbursement schedules that take into account delays in the development process and the resulting changes in the disbursement stream can artificially lower the net present value of the disbursements. In other words, under ITR's approach, delayed disbursements (i.e., the same payments later in time) result in a lower net present value in the year of launch, and therefore increase the IRR established. The EC approach would thus understate the benefit. For an apples-to-apples comparison, the use of projected disbursements would be more appropriate, or a comparison between actual disbursements and actual repayments. This is all the more critical here given that in reality disbursements were often somewhat delayed, but deliveries (and thus repayments) have consistently been substantially delayed – and in many cases it is highly uncertain if the levels predicted in Airbus' delivery forecasts will ever be achieved.

**256. Please explain, with reference to the relevant contractual provisions, the extent to which the LA/MSF funds promised by the French, Spanish and UK governments for the A310 and A300 were disbursed in advance of costs being incurred, on the basis of projected expenditure, subject to subsequent adjustment to ensure that total borrowing did not exceed the level of development costs it was agreed would be financed.**

Comment:

39. See comment to EC response to question 255 above.

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<sup>37</sup> U.S. SWS, para. 606; U.S. Answers to First Panel Questions, para. 252.

**257. Please provide a copy of the Annex referred to in the Quinta Clausula of the Spanish A340-500/600 contract.**

Comment:

40. None.

**258. The EC has identified the amounts of disbursements it asserts were provided for under the LA/MSF contracts for the A320 and the A330/A340 in two places in its FWS, in both national currency at the time of the disbursement, and in EUR. The following table lists the relevant amounts. Please explain how these amounts were derived, in all cases referring to the conversion/exchange rates that were applied.**

LA/MSF Contract	Amount (million)
French A320	[ ]
French A330/A340	[ ]
German A320	[ ]
German A330/A340	[ ]
Spanish A320	[ ]
Spanish A330/A340	[ ]
UK A320	[ ]
UK A330/A340	[ ]

Comment:

41. None.

**259. At para. 339 of its FWS, the EC states that the funding committed to Airbus Spain for the A380 was [ ]. We note, however, that pp 3 and 4 of the Spanish A380 contract (Exhibit US-BCI-73) reveal that the Spanish government agreed to provide a maximum of up to [ ]. Please explain the difference in these two figures.**

Comment:

42. The Panel correctly observes that the United States has provided evidence showing that the Spanish government agreed to provide up to Euro [ ] in Launch Aid for the A380. Not only is this evidence uncontroverted by any other evidence before the Panel, but the EC

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makes clear in its response that this figure is an accurate reflection of the funds Spain committed for the A380.<sup>38</sup>

43. By contrast, the EC offered no evidence or explanation to support the assertion in its first written submission that Euro [ ] was “{t}he loan amount{ }” for the A380 provided by Spain.<sup>39</sup> Indeed, in its response to Question 259, the EC does not even confirm the Euro [ ] figure, let alone provide evidentiary support or any other rationale for it. It merely asserts that Euro [ ] is “a maximum amount,” but gives no basis on which the Panel might be able to identify an actual amount below Euro [ ].<sup>40</sup> Without the EC pointing to such a basis in support of its bald assertion, the Euro [ ] figure is not a fact of which the Panel may take cognizance.

## B. CAPITAL INVESTMENT AND SHARE TRANSFERS

**260. At several places in the United States' Answers to the Panel's Second Questions (*i.e.*, Response to Question 158, paras. 145 and 147; Response to Question 160, para. 157) and in its Comments on the EC's Answers to the Panel's Second Questions (e.g. Comment on EC Response to Question 157, paras. 138-140) the United States alleges that the EC has failed to substantiate its assertions that particular transactions were consistent with the usual investment practice of private investors in the territory of the Member because it has not adduced evidence that the governments in question commissioned or undertook contemporaneous studies of the costs/benefits of such transactions or analyses of the going concern value of the company. What conclusions should the Panel draw, regarding the consistency of the various transactions with the usual investment practice of private investors, from the absence of analyses of the going concern value of Deutsche Airbus in 1989, of the financial condition and prospects of Aérospatiale in 1988, 1989, 1992 and 1994 and of the costs/benefits of the 1998 transfer of shares in Dassault Aviation to Aérospatiale?**

### Comment:

44. At the conclusion of its response to this question, the EC finally acknowledges a point that the United States has been making all along: “{W}hether a company needs capital says

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<sup>38</sup> See EC Answers to Third Panel Questions, paras. 35-36.

<sup>39</sup> EC FWS, para. 339.

<sup>40</sup> EC Answers to Third Panel Questions, para. 35.

nothing about whether a private investor would provide that capital.”<sup>41</sup> This is precisely why the presence or absence of contemporaneous, independent financial analyses is particularly relevant to determining whether a government-provided equity infusion is consistent with the usual investment practice of private investors. The presence of such analysis can be objective evidence that the decision to provide the infusion is consistent with how the market would act and not just a reflexive response to the demands of management. Conversely, the absence of such analysis shows that the government did not act consistently with the market; it made an investment decision without the analytical foundation private investors ordinarily would require. As a result, the recipient received a financial contribution through a decision that was inconsistent with the usual investment practice of private investors, which is strong evidence that the recipient received a benefit as compared to the market.

45. In fact, in *EC – DRAMs*, the EC itself acknowledged the relevance of an absence of contemporaneous, independent financial analyses. At issue there were the government-directed investments of certain Korean banks in the Hynix company – investments allegedly made on the belief that the company’s going concern value exceeded its liquidation value. In finding that these investments conferred a benefit, the panel agreed with the EC that “the banks do not seem to have based this conclusion on independent assessment studies, as could be expected given the situation of Hynix.”<sup>42</sup> In other words, the EC argued – and the panel agreed – that the absence of contemporaneous, independent financial analyses was strong evidence that the investments at issue were made inconsistently with market practices and thus conferred a benefit.

46. In the present dispute, contrary to its position in *EC – DRAMs*, the EC takes a dismissive view of the significance of the presence or absence of contemporaneous, independent financial analyses. It claims to have provided evidence of such analyses only with respect to one of the equity infusions at issue – the French government’s 1998 provision of its Dassault Aviation shares to Aérospatiale<sup>43</sup> – thus admitting the absence of such analyses with respect to the other infusions – the French government’s 1987-to-1993 infusions to Aérospatiale and the German

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<sup>41</sup> EC Answers to Third Panel Questions, para. 81. See U.S. First Non-Confidential Oral Statement (“FNCOS”), para. 106 (“{EC’s} extended discussion of the views of Boeing’s and Aérospatiale’s management ignores that the relevant test for examining an equity infusion is the usual investment practice of private investors, not the views of management.”).

<sup>42</sup> *EC - DRAMs*, para. 7.208 (discussed in U.S. Answers to Second Panel Questions, para. 315).

<sup>43</sup> See EC Responses to Third Panel Questions, para. 40. There, the EC states that in Section B of its response to Question 260 it has “provided analyses demonstrating that certain of the transactions listed by the Panel are *consistent* with the usual investment practice of private investors.” *Id.* (emphasis in original). In Section B, the EC addresses the Dassault share transfer. See *id.*, paras. 49-59. It also discusses the “1989 restructuring of Deutsche Airbus and the 1998 settlement.” *Id.*, paras. 60-68. However, the EC simply ignores the German government’s 1989 investment in Deutsche Airbus as a separate and distinct equity infusion.

government's DM 505 million infusion to Deutsche Airbus in 1989. As has been discussed in previous submissions,<sup>44</sup> and as will be summarized below, the evidence the EC has provided regarding the 1998 Dassault share transfer is not evidence of contemporaneous, independent financial analyses of that transaction; it is evidence pertaining to an entirely different transaction (the 1999 merger between Aérospatiale and Matra Hautes Technologies).

47. The EC falls back on the argument that contemporaneous, independent financial analyses “are not the exclusive means to demonstrate that the terms of a transaction are consistent with market.”<sup>45</sup> While this observation may be correct in theory, it is irrelevant here, as the EC has failed to come forward with any evidence (whether in the form of financial analyses or otherwise) to rebut the U.S. demonstration that the equity infusions in dispute were provided to companies in dire financial circumstances without the government basing its decision on the information and analysis that a private investor would have required; that the infusions, therefore, were not “consistent with market;” and that, accordingly, they conferred a “benefit” on the companies within the meaning of Article 1.1(b) of the SCM Agreement. As will be discussed below, the evidence described in the EC’s response to Question 260 fails to rebut the U.S. case.

48. Before commenting on the EC’s discussion of evidence regarding particular transactions, the United States will address the EC’s discussion of the measures at issue and its discussion of the relative burdens of the United States and the EC.

#### Measures at Issue

49. The EC’s response to Question 260 assumes that the issue of the absence of contemporaneous, independent financial analyses is relevant to only three measures, which the EC describes as “the capital contributions to Aérospatiale,” “the transfer of Dassault shares,” and “the restructuring of Deutsche Airbus in 1989.”<sup>46</sup> The EC thus ignores entirely the relevance of the issue to the German government’s DM 505 million equity infusion to Deutsche Airbus in 1989, even though the United States has raised it explicitly in that context.<sup>47</sup>

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<sup>44</sup> See, e.g., U.S. Answers to Second Panel Questions, paras. 145-151, 152-155, 156-158, 326-329; U.S. Comments on EC Answers to Second Panel Questions, paras. 159-163, 164-167, 168-169, 170-172.

<sup>45</sup> EC Answers to Third Panel Questions, para. 39.

<sup>46</sup> EC Answers to Third Panel Questions, para. 42.

<sup>47</sup> See, e.g., U.S. Answers to Second Panel Questions, paras. 309-319; U.S. Comments on EC Answers to Second Panel Questions, paras. 356-360.

50. Instead of addressing the German government's 1989 equity infusion, the EC repeats its argument that "it is the 1998 debt settlement that is the measure before the Panel, and not the 1989 restructuring."<sup>48</sup> As discussed in the U.S. comment on the EC's response to Question 187, the DM 505 million equity infusion (which the EC only belatedly acknowledged as part of the 1989 restructuring, as opposed to an investment made following the restructuring<sup>49</sup>) is a distinct measure at issue. The United States does not have to establish that other elements of the restructuring package constitute subsidies in order to establish that the equity infusion constitutes a subsidy.<sup>50</sup> Accordingly, even if the restructuring package as a whole is not a measure at issue, the equity infusion indisputably is,<sup>51</sup> and the EC has provided no evidence to rebut the U.S. demonstration that the infusion was provided to Deutsche Airbus inconsistently with the usual investment practice of private investors and thus conferred a benefit.

51. In addition to ignoring the German government's 1989 equity infusion, the EC's response to Question 260 makes only the most cursory reference to the French government's 1987 to 1993 equity infusions to Aérospatiale – a single paragraph in a 45-paragraph response.<sup>52</sup> What is left is a repetition of the EC's arguments regarding the French government's 1998 transfer to Aérospatiale of its stake in Dassault, which, as discussed below, fails to overcome the U.S. showing that the transfer was inconsistent with the usual investment practice of private investors and thus conferred a benefit on Aérospatiale.

### Burden of Proof

52. Not only does the EC's response to Question 260 largely ignore certain transactions, it also confuses the respective burdens of the United States and the EC. Thus the EC asserts that the absence of contemporaneous, independent financial analyses "would not demonstrate anything of relevance to this case" because, it contends, "there is no requirement for Members to

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<sup>48</sup> EC Answers to Third Panel Questions, para. 68; *see also id.*, para. 60 ("the 1998 settlement between Deutsche Airbus and the German government is the only specific measure at issue challenged by the United States").

<sup>49</sup> *See* U.S. Comments on EC Answers to Second Panel Questions, paras. 127-128.

<sup>50</sup> *See* U.S. Comments on EC Answers to Second Panel Questions, paras. 127-131.

<sup>51</sup> *See European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft*, Request for the Establishment of a Panel by the United States, WT/DS316/2 at 2-3, numbered para. (5) (referring to "equity investment by the German government through Kreditanstalt für Wiederaufbau ('KfW') in Deutsche Airbus in 1989 and the return of the shares acquired through this transaction to Deutsche Airbus' parent, the Daimler group, without compensation, in 1992" as among "{t}he measures of the EC and the member States that are the subject of this panel request").

<sup>52</sup> *See* EC Answers to Third Panel Questions, para. 80.

conduct contemporaneous analyses of proposed transactions to show that they would be *consistent* with the usual investment practice of private investors, or a burden to provide such analyses in dispute settlement.”<sup>53</sup>

53. The EC misses the point. In particular, it ignores the burden that the defending party bears in dispute settlement once the complaining party has established its *prima facie* case, as the United States has done in this dispute. As the Appellate Body has explained:

{I}t is a generally-accepted canon of evidence in civil law, common law and, in fact, most jurisdictions, that the burden of proof rests upon the party, whether complaining or defending, who asserts the affirmative of a particular claim or defence. If that party adduces evidence sufficient to raise a presumption that what is claimed is true, the burden then shifts to the other party, who will fail unless it adduces sufficient evidence to rebut the presumption.<sup>54</sup>

54. In this dispute, the United States has established its *prima facie* case with respect to the equity infusions at issue (as well as with respect to each of its other claims). In particular, it has shown that Deutsche Airbus and Aérospatiale were in dire financial circumstances when the infusions were made and that, nevertheless, the German and French governments, respectively, made the infusions without undertaking the contemporaneous, independent analyses that private investors ordinarily would require.<sup>55</sup> The infusions, therefore, were “inconsistent with the usual investment practice . . . of private investors.”<sup>56</sup> As such, these financial contributions conferred a “benefit” and thus constitute subsidies within the meaning of Article 1 of the SCM Agreement.

55. As the United States established its *prima facie* case, it “raise{d} a presumption that what is claimed is true,” and the burden shifted to the EC, which “will fail unless it adduces sufficient

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<sup>53</sup> EC Answers to Third Panel Questions, para. 38.

<sup>54</sup> *US – Wool Shirts (AB)*, p. 14 (emphasis added); *see also EC – Hormones (AB)*, para. 98 (“When {the complaining party’s} *prima facie* case is made, the burden of proof moves to the defending party, which must in turn counter or refute the claimed inconsistency.”).

<sup>55</sup> *See* U.S. FWS, paras. 546-547 (Deutsche Airbus), paras. 569-572, 583-589, 591-593, 598-603, 610-619 (Aérospatiale); U.S. FNCOS, paras. 106-107 (Aérospatiale); U.S. Answers to First Panel Questions, paras. 170-172, 173-175, 187-190; U.S. SWS, paras. 460-462 (Deutsche Airbus), paras. 463-478, 479-486 (Aérospatiale); U.S. SNCOS, paras. 99-104 (Aérospatiale), paras. 109-111 (Deutsche Airbus); U.S. Answers to Second Panel Questions, paras. 129-139 (Deutsche Airbus), paras. 145-151, 152-155, 156-158 (Aérospatiale), 306-329; U.S. Comments on EC Answers to Second Panel Questions, paras. 144-148 (Deutsche Airbus), paras. 159-163, 164-167, 168-169, 170-172 (Aérospatiale); U.S. Answers to Third Panel Questions, paras. 114-121.

<sup>56</sup> SCM Agreement, Art. 14(a).

evidence to rebut the presumption.”<sup>57</sup> One way the EC might have rebutted the presumption was by providing evidence of contemporaneous, independent analyses, which might have shown that the German or French government’s actions were consistent with the usual investment practice of private investors. But, the EC provided no such evidence. Alternatively, the EC might have provided evidence that, notwithstanding the absence of such analyses, the equity infusions were consistent with a market benchmark. But, the EC did not provide evidence of this type either. Alternatively, the EC might have provided evidence that, notwithstanding the absence of such analyses, the equity infusions were consistent with a market benchmark. But, the EC did not provide evidence of this type either.

56. Here it bears emphasis that, contrary to the EC’s repeated assertion, the United States does not argue that there is a “requirement for Members to conduct contemporaneous analyses of proposed transactions to show that they would be *consistent* with the usual investment practice of private investors.”<sup>58</sup> In suggesting otherwise, the EC obscures what is a straightforward evidentiary issue.<sup>59</sup>

57. There may well be circumstances in which a government did not rely upon contemporaneous, independent financial analyses, but other evidence establishes that the government’s investment did not confer a benefit as compared to what the market would have provided. The panel in *Japan – DRAMs* recognized this possibility too.<sup>60</sup> However, in this dispute (as in *Japan – DRAMs*) such evidence is entirely lacking.

58. The EC insists that contemporaneous, independent financial analyses “are not the exclusive means to demonstrate that the terms of a transaction are consistent with market.”<sup>61</sup> While the United States does not disagree with this generic proposition, it is irrelevant here, as the EC has not provided any evidence to rebut the U.S. showing that the equity infusions at issue

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<sup>57</sup> *US – Wool Shirts (AB)*, p. 14.

<sup>58</sup> EC Answers to Third Panel Questions, para. 38 (underscoring added; italics in original); *see also id.* paras. 72, 76.

<sup>59</sup> In this regard, the EC’s discussion at paragraph 76 of its response to Question 260 is entirely irrelevant. The United States has not argued that “a requirement” of the SCM Agreement is “applicable to the specific actions taken by Members *in the 1980s and 1990s.*” EC Answers to Third Panel Questions, para. 76 (emphasis in original). Rather, it has argued that as an evidentiary matter, the failure of the German and French governments to base their investment decisions on contemporaneous, independent financial analyses shows that they acted inconsistently with the usual investment practice of private investors.

<sup>60</sup> *See* U.S. Answers to Third Panel Questions, paras. 111-114.

<sup>61</sup> EC Answers to Third Panel Questions, para. 39; *see also id.*, paras. 70-73.

in this dispute were provided without the support of independent financial analyses, that they were thus provided contrary to the usual investment practice of private investors, that they were inconsistent with the market, and that they thus conferred a benefit on Airbus.

59. The EC asserts that it has provided such rebuttal evidence and that it has addressed this evidence in Section C of its response to Question 260.<sup>62</sup> There, the EC describes certain evidence allegedly relevant to the French government’s 1998 transfer to Aérospatiale of its stake in Dassault and its 1987-to-1993 equity infusions to Aérospatiale. However, none of the evidence described rebuts the U.S. showing that the transactions at issue conferred benefits.

Evidence Other Than Contemporaneous, Independent Analyses as Described in Section C of EC Response

60. With respect to the 1998 transfer of Dassault shares, the EC refers to evidence of private investors’ interest in the 1999 public offering of shares in the entity resulting from the merger between Aérospatiale and Matra, known as ASM.<sup>63</sup> However, this is a *non-sequitur*. Even if the EC were correct that in 1999 “private investors flocked to the public offering of ASM shares in droves,”<sup>64</sup> this post-dates the French government’s 1998 decision to relinquish its control of Dassault without compensation and is entirely irrelevant to establishing whether that 1998 decision by the French government to transfer to Aérospatiale its stake in Dassault was consistent with the usual investment practice of private investors. In short, the EC confuses the matter by referring to private investment in a transaction entirely different from the transaction at issue.

61. With respect to the French government’s 1987-to-1993 equity infusions to Aérospatiale, the EC claims to have provided “masses of contemporaneous documents.”<sup>65</sup> However, by the EC’s own admission, these documents pertain not to Airbus in particular but to the state of the LCA industry in general.<sup>66</sup> As discussed in the U.S. oral statement at the second Panel meeting, the “masses of contemporaneous documents” to which the EC refers consist almost entirely of internal documents from Aérospatiale and Airbus GIE, as well as the French state-owned bank Crédit Lyonnais and, accordingly, can hardly be considered objective – a point the EC now

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<sup>62</sup> See EC Answers to Third Panel Questions, paras. 39, 78-81.

<sup>63</sup> See EC Answers to Third Panel Questions, para. 79.

<sup>64</sup> EC Answers to Third Panel Questions, para. 79.

<sup>65</sup> EC Answers to Third Panel Questions, para. 80.

<sup>66</sup> See EC Answers to Third Panel Questions, para. 80 (referring to “steady growth in commercial airline traffic and robust, untapped demand for LCA well into the future”).

admits in acknowledging that “whether a company needs capital says nothing about whether a private investor would provide that capital.”<sup>67</sup> The remainder of the documents include statements by Boeing regarding the state of the industry in general.<sup>68</sup> The EC has yet to explain how it would be consistent with the usual investment practice of private investors to provide equity to Airbus (as opposed to Boeing or to a supplier of both companies, for example) on the basis of such generic statements.

62. An additional point regarding the information cited by the EC in connection with the 1987-to-1993 equity infusions is that even if, in theory, the information could have supported the French government’s investments (a proposition the United States contests, for the reasons summarized above), there is no evidence that the French government actually analyzed it and relied on it in making its investment decision.<sup>69</sup> The EC counters that Articles 1.1(b) and 14(a) of the SCM Agreement “require only that the relevant information existed at the time of the capital contributions,” not that the government actually relied on that information.<sup>70</sup> In support of this argument, the EC repeatedly quotes from a footnote in the *Canada – Aircraft II* panel report.<sup>71</sup> That footnote, however, provides no support for the EC’s argument.

63. The potential relevance of the information cited by the EC in connection with the 1987-to-1993 equity infusions is the light it might shed on the practice of the French government. If there were evidence that the French government relied on this information, that might help establish whether the government’s investment decisions were consistent or not with “the usual investment practice . . . of private investors”<sup>72</sup> (putting to one side the other reasons the evidence is not probative, as summarized above). However, the mere fact that the information may have existed at the time of the government’s investment decisions has no bearing whatsoever on whether those decisions were consistent or not with “the usual investment practice of private investors.”

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<sup>67</sup> EC Answers to Third Panel Questions, para. 81.

<sup>68</sup> See U.S. SNCOS, paras. 99-104.

<sup>69</sup> See U.S. SNCOS, para. 104.

<sup>70</sup> EC SWS, para. 544 (emphasis in original).

<sup>71</sup> See EC SWS, para. 544; EC Comments on U.S. Answers to Second Panel Questions, para. 419; EC Answers to Third Panel Questions, paras. 75, 187 (quoting *Canada – Aircraft II*, para. 7.242, n.201).

<sup>72</sup> SCM Agreement, Art. 14(a) (emphasis added).

64. The observation of the *Canada – Aircraft II* panel in footnote 201 of its report has nothing to do with whether a government investment decision is consistent with the usual investment practice of private investors. First, the financial contribution at issue there was a *loan* (export credit), for which Article 14 of the SCM Agreement sets out a different standard for determining benefit than that used in cases, such as here, involving *equity*.<sup>73</sup> Second, the panel was addressing an entirely different issue – *i.e.*, whether a market transaction contemporaneous with the government transaction at issue could be used as a benchmark in a benefit analysis if the government did not actually refer to that transaction when it made its own financial contribution.<sup>74</sup> Even if the answer is yes (as the panel found), that has no bearing on how it may be established that a government investment decision is or is not consistent with the usual investment practice of private investors. An analysis of a government’s practice necessarily requires an assessment of what it did, not simply of random information that may have existed when it made its decision.

65. With respect to the 1987-to-1993 equity infusions, therefore, the EC has failed to rebut the U.S. showing that Aérospatiale’s poor financial fundamentals, an assessment by its chairman that the company was “repellent” from an investor’s point of view,<sup>75</sup> and the absence of any contemporaneous, independent financial analyses meant that the infusions were inconsistent with the usual investment practice of private investors, and thus conferred a benefit.

#### Evidence of Analyses Described in Section B of EC Response

66. The United States now turns to the EC’s discussion of evidence of “analyses” that it characterizes as showing that certain transactions were “consistent with the usual investment practice of private investors.”<sup>76</sup> As noted above, the EC contends that it has provided such analyses in connection with only one of the equity infusions at issue – the French government’s 1998 transfer to Aérospatiale of its stake in Dassault. It also contends that it provided such evidence in connection with the German government’s 1998 forgiveness of Deutsche Airbus’ debt to it (a transaction that the EC characterizes as a “settlement . . . of all outstanding

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<sup>73</sup> Compare the different means of determining benefit for loans (Article 14(b) of the SCM Agreement) with that for determining benefit for equity (Article 14(a) of the SCM Agreement).

<sup>74</sup> *Canada – Aircraft II*, para. 7.242, n.201.

<sup>75</sup> *EC to review France’s Aérospatiale capital injection*, Aerospace Daily, at 217-218 (Feb. 9, 1994) (Exhibit US-275) (discussed in U.S. FWS, para. 558; U.S. SNCOS, para. 98).

<sup>76</sup> EC Answers to Third Panel Questions, para. 48.

claims”<sup>77</sup>). The United States first will address the Dassault share transfer and then the Deutsche Airbus debt settlement.

#### Dassault Share Transfer

67. The EC begins its discussion of the Dassault share transfer by making two unsupported assertions that the United States has “acknowledged” certain propositions. First, it alleges that the United States acknowledges that the share transfer was “simply a matter of accounting.”<sup>78</sup> The United States acknowledges nothing of the sort. In asserting otherwise, the EC cites to paragraph 152 of the U.S. response to the Panel’s Question 159. The EC’s citation entirely disregards context.

68. At the outset of its response to Question 159, the United States addressed the relevance to a benefit analysis of Aérospatiale’s issuance of new shares to the government of France upon the receipt of France’s stake in Dassault. It was the issuance of new Aérospatiale shares – not the transfer of the Dassault stake itself – that the United States described as “simply a matter of accounting” in light of the French government’s ownership of 100 percent of Aérospatiale.<sup>79</sup> In the very next paragraph, the United States explained:

The primary benefit to Aérospatiale from the French government’s contribution of the Dassault shares was that it received an equity infusion through a transaction inconsistent with the usual investment practice of private investors in France. For reasons explained in previous submissions and summarized in response to Question 158, above, a private investor would not have engaged in the transaction that resulted in Aérospatiale’s receipt of the Dassault shares. At a time when Aérospatiale was in dire financial circumstances, the government incurred considerable costs – including, notably, ceding control of Dassault without any compensation – in order to provide new capital to Aérospatiale. The consequence for Aérospatiale was a significant boost to its balance sheet – a 20 percent increase in its equity.<sup>80</sup>

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<sup>77</sup> EC Answers to Third Panel Questions, para. 48.

<sup>78</sup> EC Answers to Third Panel Questions, para. 50.

<sup>79</sup> See U.S. Answers to Second Panel Questions, para. 152.

<sup>80</sup> U.S. Answers to Second Panel Questions, para. 153.

69. In short, as the foregoing reference makes unmistakably clear, contrary to the EC’s assertion, the United States does not and has never acknowledged that “the transfer was ‘simply a matter of accounting.’”<sup>81</sup>

70. Nor has the United States “expressly agreed with the European Communities that the transfer at issue . . . is of no economic significance to anyone other than the Dassault family and Dassault Industries.”<sup>82</sup> As the United States has explained in previous submissions, the transfer resulted in Aérospatiale receiving a valuable financial contribution – the French government’s stake in Dassault. In order to make that contribution to Aérospatiale, the government had to relinquish its control in Dassault to the Dassault family. However, the government received no compensation for its relinquishment of control, even though a 30 percent premium usually attaches to control.<sup>83</sup> That was a significant cost of transferring the Dassault shares to Aérospatiale. A private investor knowing that it would not be compensated for relinquishing control to another shareholder of the company either would have retained control or relinquished it only upon a reasonable expectation of profits outweighing the substantial financial sacrifice. The French government did neither of these things. In other words, in providing a substantial equity infusion to Aérospatiale, the government acted inconsistently with the usual investment practice of private investors. As Aérospatiale received equity through an investment decision that was inconsistent with the usual investment practice of private investors it received a “benefit” within the meaning of Article 1.1(b), understood in the context of Article 14(a) of the SCM Agreement.<sup>84</sup>

71. After mischaracterizing the U.S. arguments regarding the Dassault share transfer, the EC goes on to assert that it has provided analyses showing that the terms of the transfer were “consistent with market.”<sup>85</sup> It relies, in particular on a report by the French *Commissaires aux Apports* and various investment bank reports – none of which address the transaction at issue. As explained in previous submissions, these reports were prepared after the Dassault share transfer, they pertain to an entirely different transaction (the merger between Aérospatiale and Matra), and, to the extent they mention the Dassault shares at all, they do not purport to analyze

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<sup>81</sup> EC Answers to Third Panel Questions, para. 50 (emphasis added).

<sup>82</sup> EC Answers to Third Panel Questions, para. 52.

<sup>83</sup> See Lauren D. Fox, 1998 Dassault Share Transfer Valuation Report at 6 (“Fox Report”) (Exhibit US-595 (HSBI)).

<sup>84</sup> See U.S. Answers to Second Panel Questions, paras. 145-151, 152-155, 156-158, 326-329; U.S. Comments on EC Answers to Second Panel Questions, paras. 159-163.

<sup>85</sup> EC Answers to Third Panel Questions, para. 54.

the costs and benefits to the French government of transferring those shares without compensation for the relinquishment of control of Dassault. Accordingly, they have no bearing on whether the government's provision of the Dassault shares to Aérospatiale was consistent with the usual investment practice of private investors and, hence, whether it conferred a benefit on Aérospatiale.<sup>86</sup>

72. Evidently recognizing these flaws in its evidence, the EC tries to portray the Dassault share transfer and the subsequent Aérospatiale-Matra merger as a single transaction, with the reports by the *Commissaires aux Apports* and various investment banks pertaining to the “synergies” supposedly associated with this mega-transaction.<sup>87</sup> However, this self-serving and inaccurate portrayal cannot rescue the EC's misplaced reliance on analyses having nothing to do with the transaction at issue – the Dassault share transfer.

73. The analyses on which the EC relies take the Dassault share transfer as a given, an event that already has occurred. It stands to reason, therefore, that they do not assess the costs and benefits of undertaking that transfer in the way that an analysis would if it were being done to inform a private investor's decision whether to undertake the transfer in the first place. Accordingly, they give no support to the EC's contention that the French government's decision to provide its Dassault stake to Aérospatiale was consistent with the usual investment practice of private investors.

74. The EC further contends that the analyses on which it relies “valued synergies to be realised” by the Aérospatiale-Matra merger as exceeding the French government's loss from its uncompensated relinquishment of control of Dassault.<sup>88</sup> This contention, even if true, is irrelevant for two reasons. First, as already discussed, the analyses post-dated the Dassault share transfer. Therefore, they cannot possibly have “justified” that transaction, as the EC alleged in its response to Question 194.<sup>89</sup>

75. Second, whatever value the reports may have attributed to the synergies to be realized in the Aérospatiale-Matra merger obviously would not redound entirely to the benefit of the French government. Much of that value would redound to the benefit of the Lagardère firm (the owner

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<sup>86</sup> See U.S. Comments on EC Answers to Second Panel Questions, paras. 159-163, 164-167, 168-169, 170-172.

<sup>87</sup> See EC Answers to Third Panel Questions, paras. 57-59 and n.62.

<sup>88</sup> EC Answers to Third Panel Questions, para. 57.

<sup>89</sup> EC Answers to Second Panel Questions, para. 208; see also U.S. Comments on EC Answers to Second Panel Questions, paras. 165-166.

of Matra) and to purchasers of shares in the newly merged entity. However, the relevant question is whether the French government had a well-founded basis for expecting that its knowing incurrence of a loss (*i.e.*, its uncompensated relinquishment of control of Dassault) would be offset by gains to the French government, not by gains to third parties. It would be inconsistent with the usual investment practice of private investors to knowingly incur a loss based on an expected realization of new value for third parties, as opposed to new value for the investor itself.

76. Finally, the EC argues that even though the analyses on which it relies post-dated the Dassault share transfer, some of the information on which those analyses were based was allegedly “available to the parties months in advance of the share transfer.”<sup>90</sup> Even if that statement is true, it still does not establish that the French government’s investment decision was consistent with the usual investment practice of private investors. As discussed above, the focus of the inquiry under Article 14(a) of the SCM Agreement is practice. The mere fact that information may have existed at the time of the government’s investment decision has no bearing whatsoever on whether the decision was consistent or not with the usual investment practice of private investors. This is particularly so given that such practice usually involves analysis of the investment contemplated, and the EC has proffered no evidence that the French government performed any such analysis.

77. In sum, the EC’s repetition of evidence and arguments in Section B of its response to Question 260 fails to rebut the U.S. showing that the French government’s provision of its Dassault shares to Aérospatiale was inconsistent with the usual investment practice of private investors and thus conferred a benefit on Aérospatiale within the meaning of Article 1.1(b) as understood in the context of Article 14(a) of the SCM Agreement.

#### 1989 Restructuring of Deutsche Airbus and 1998 Forgiveness of Deutsche Airbus Debt

78. While the EC includes a section on “{the} 1989 restructuring of Deutsche Airbus and the 1998 settlement” in its discussion of “{a}nalyses provided by the European Communities,” it mentions the analyses at issue only in passing.<sup>91</sup> The discussion, in fact, is devoted to an issue unrelated to the Panel’s question – that is, a re-argument of the EC’s position that the 1989 restructuring of Deutsche Airbus is not a measure at issue in this dispute and that the restructuring does not constitute a subsidy.<sup>92</sup>

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<sup>90</sup> EC Answers to Third Panel Questions, para. 58.

<sup>91</sup> See EC Answers to Third Panel Questions, para. 61.

<sup>92</sup> See EC Answers to Third Panel Questions, paras. 60-68; see also *id.*, paras. 42-47.

79. The United States has addressed these arguments in previous submissions.<sup>93</sup> As explained in those submissions, the EC misunderstands the relevance of the 1989 restructuring of Deutsche Airbus to this dispute. The United States has made claims regarding two measures that the EC does not dispute are properly before the Panel: the German government's DM 505 million equity infusion to Deutsche Airbus in 1989 and the government's forgiveness of DM 7.7 billion of debt owed to it by Deutsche Airbus in 1998. In responding to those claims, the EC has made arguments regarding the 1989 restructuring. In particular, it has contended that the equity infusion can be found to be a subsidy only if the entire restructuring package is found to be a subsidy,<sup>94</sup> and that the U.S. complaint regarding the 1998 debt forgiveness is really a complaint about the 1989 restructuring package.<sup>95</sup> In other words, it is the EC, not the United States, that has made an issue of the 1989 restructuring package.

80. The United States has made counter-arguments in light of the EC's attempt to focus on the 1989 restructuring package. In particular, it has shown that finding the 1989 equity infusion to be a subsidy (as the German government itself described the transaction<sup>96</sup>) does not require the Panel to find that other elements of the restructuring package also are subsidies; it requires the Panel to find the infusion to be a financial contribution that confers a benefit. To the extent that the restructuring package is relevant as context, it shows the error in the EC's contention that Daimler-Benz's investment in MBB is a benchmark confirming the consistency with market of the KfW investment. Daimler made its investment only because the government gave Deutsche Airbus a restructuring package that included the DM 505 million equity infusion.<sup>97</sup>

81. The United States also has shown that its claim regarding the German government's forgiveness of Deutsche Airbus' debt is in fact a claim about that 1998 transaction and not about the 1989 restructuring giving rise to the debt. In particular, it has shown that the even accepting the EC's characterization of the 1998 transaction as a payment by Deutsche Airbus of the fair value of the government's claims (as opposed to debt forgiveness), Deutsche Airbus still received a benefit distinct from any benefit conferred by the underlying restructuring. The 1998 settlement converted a future, potential benefit to the company into a current cash grant

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<sup>93</sup> See U.S. SWS, paras. 436-442; U.S. Comments on EC Answers to Second Panel Questions, paras. 126-143, 149-152.

<sup>94</sup> See, e.g., EC SNCOS, paras. 258-261.

<sup>95</sup> See, e.g., EC SWS, para. 585.

<sup>96</sup> See U.S. FWS, paras. 540, 547 (citing BT-Drs. 13/8409, at 13-14 (Exhibit US-31)).

<sup>97</sup> See, e.g., U.S. Answers to Second Panel Questions, paras. 128-139, 140-144; U.S. Comments on EC Answers to Second Panel Questions, paras. 126-143.

(available for use in causing current adverse effects) and it removed uncertainty as to benefits that might accrue to the company in the future.<sup>98</sup>

82. Thus, the EC errs in urging the Panel to dismiss the U.S. claims as claims about the 1989 restructuring package. However, even if the Panel were to agree with the EC's mischaracterization of these claims, it still should reject the EC's suggestion that the claims are beyond the Panel's terms of reference, for the reasons discussed in the U.S. second submission and in its comments on the EC response to Question 189.<sup>99</sup>

83. Finally, given that the EC has responded to the equity infusion and debt forgiveness claims by making arguments about the 1989 restructuring package – asserting, for example, that “{i}n the particular factual circumstances . . . the German government minimized its losses while providing certain contributions to rebalance the value of Deutsche Airbus' assets and liabilities”<sup>100</sup> – the United States has addressed those arguments directly, in the interest of completeness. It showed that even the comprehensive analysis of the 1989 restructuring package that the EC (erroneously) suggests is required does not rebut the U.S. demonstration that the equity infusion and debt forgiveness are subsidies within the meaning of Article 1 of the SCM Agreement.<sup>101</sup>

84. In short, in response to a question on an entirely different topic (*i.e.*, the relevance of the absence of contemporaneous, independent financial analyses of particular transactions at issue), the EC has chosen to re-argue its position regarding the 1989 restructuring of Deutsche Airbus. As its arguments have not changed, neither do the necessary conclusions: The German government's DM 505 million equity infusion to Deutsche Airbus and its subsequent forgiveness of DM 7.7 billion in debt owed by Deutsche Airbus are subsidies within the meaning of Article 1 of the SCM Agreement through which the EC is causing adverse effects to the interests of the United States in breach of Article 5 of the Agreement.

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<sup>98</sup> See U.S. Answers to First Panel Questions, paras. 196-200; U.S. SWS, paras. 439-442; U.S. Comments on EC Answers to Second Panel Questions, paras. 132-134;

<sup>99</sup> See U.S. SWS, paras. 435-438; U.S. Comments on EC Answers to Second Panel Questions, paras. 149-152.

<sup>100</sup> EC Answers to Second Panel Questions, para. 164.

<sup>101</sup> See U.S. Comments on EC Answers to Second Panel Questions, paras. 135-143.

**C. ADVERSE EFFECTS**

**261. Could the EC please indicate whether, and if so, the extent to which, the data set forth at paragraph 2162, of its first written submission, in the table entitled "Trends in Boeing's LCA Operations" includes results relating to sales for export?**

Comment:

85. The EC, like the United States, bases its arguments with respect to material injury on data regarding Boeing's LCA operations as a whole. As the United States explained in response to Question 239, Article 16.1 of the SCM Agreement defines the "domestic industry" as "the domestic producers as a whole of the like products."<sup>102</sup> The EC does not appear to disagree with this approach.<sup>103</sup>

86. In the remainder of its answer, the EC attempts to "update" its assessment of trends in Boeing operations with estimated data on Boeing operations for 2007. The United States does not see how this new information is responsive to the Panel's question, which was limited to a clarification of the data through 2006 previously provided by the EC.

87. In any event, as the United States has explained, the claim made by the United States and included in the Panel's terms of reference is that the EC and the Airbus governments were in breach of their obligations under Article 5 of the SCM Agreement in that, at the time of panel establishment, they were, through the use of the challenged subsidies, causing adverse effects to the interests of the United States including, *inter alia*, material injury within the meaning of Article 5(a).<sup>104</sup> Questions about the situation after the establishment of the Panel, such as whether the EC or Airbus governments have removed any of the adverse effects caused by their subsidies or whether there is new or increased serious prejudice to the interests of the United States, therefore, are outside the terms of reference of the Panel. The EC estimates of the financial performance of Boeing's LCA operations in 2007, therefore, are not relevant to this dispute.

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<sup>102</sup> U.S. Answers to Third Panel Questions, para. 83.

<sup>103</sup> The EC opines that, if the Panel were to adopt a different definition of the relevant domestic industry, the United States would have the burden of providing data on the domestic industry so defined. EC Answers to Third Panel Questions, para. 83. However, the EC does not argue that the Panel should adopt a different definition.

<sup>104</sup> U.S. SWS, paras. 672-683; U.S. FNCOS, paras. 182-184.

88. The EC's lengthy discussion of order and backlog data is likewise not relevant, as the United States has also already explained.<sup>105</sup>

**262. Please provide copies of any business case analyses, including sensitivity analyses, prepared in connection with the launch of Airbus LCA models prior to the [ ].**

Comment:

89. As an initial matter, the EC has failed to respond to the Panel's request with respect to business case analyses for the launch of the Airbus A300 and A310 models. As the United States has shown, Launch Aid was instrumental to Airbus's launch of the A300 and its derivative, the A310. In fact, Airbus officials have publicly acknowledged that Airbus could not have launched the A300 without Launch Aid.<sup>106</sup> Not only has the EC failed affirmatively to rebut the U.S. demonstration, but it has also failed to explain why it has not provided the business case documents requested by the Panel that could have shed further light upon the matter.

90. With respect to later Airbus launch decisions, the documents referred to by the EC in its response to this question, including newly provided documents, confirm other, previously discussed evidence with respect to the impact of Launch Aid on the launch decisions of Airbus. Because the EC has designated most of these documents as HSBI, the United States provides its detailed comments in the HSBI Appendix. These comments show that:

- Launch Aid has been an instrumental part of every major Airbus launch decision;
- the launch of each new Airbus model is designed to build on prior launches;
- the launch of a new Airbus model puts downward pressure on Boeing prices; and
- Launch Aid is even more significant when the sensitivity analysis overstates the case for launch by overstating the likely sales volume and understating the risk of shortfall.

**263. In paragraphs 1036 - 1042 of its second written submission, the EC argues, *inter alia*, that LA/MSF is not a factor in Moody's rating of EADS. Would the EC clarify its**

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<sup>105</sup> U.S. Answers to Third Panel Questions, para. 87.

<sup>106</sup> U.S. Answers to Third Panel Questions, para. 42 (citing Speech of Jan Pierson, Managing Director, Airbus Industrie, at Cranfield Management School, Apr. 1991, quoted in Matthew Lynn, *Birds of Prey*, at 150 (1995) (Exhibit US-42)); U.S. FWS, para. 830.

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**position in that respect, in view of the following statement in Exhibit US 56: "The rating also considers the expectation for continuing government support, which is primarily in the form of refundable advance for up to 1/3 of the development cost of each new aircraft program on the Airbus level."**

Comment:

91. The EC's response to this question confirms the point made by the United States in response to question 228: Moody's accounts for Launch Aid in its baseline credit assessment of EADS, and the incremental improvement in Moody's credit rating of EADS resulting from the company's status as a government-related issuer (GRI) is a distinct factor in Moody's analysis of the creditworthiness of EADS.<sup>107</sup> Moody's always takes into consideration all "aspects of the entity's existing (or anticipated) business model, including benefits (such as regular subsidies or credit extension)" within the baseline credit assessment of EADS, as it would for any company, GRI or not.<sup>108</sup> Launch Aid is, and always has been, integral to the business model for Airbus, and indeed the EC admits that Launch Aid is a factor in Moody's "baseline credit rating for EADS."<sup>109</sup> In addition, because EADS is a GRI, Moody's also takes into consideration the likelihood of extraordinary government support in the event of a future catastrophic loss.<sup>110</sup>

92. Thus, when Moody's speaks of Launch Aid as "continuing government support," as it does in the statement quoted in the Panel's question, it is taking account of the effect of Launch Aid. That analysis is unrelated to the status of EADS as a GRI. The EC acknowledges as much in its response to the Panel's question.<sup>111</sup> The EC's lengthy description of the impact of EADS's status as a GRI in its second written submission<sup>112</sup> is therefore, by the EC's own admission, completely irrelevant.

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<sup>107</sup> U.S. Answers to Third Panel Questions, paras. 16-22.

<sup>108</sup> U.S. Answers to Third Panel Questions, para. 20 (citing Moody's Investor Service, *The Application of Joint Default Analysis to Government Related Issuers* (Apr. 2005) at 2 (Exhibit EC-836)).

<sup>109</sup> EC Answers to Third Panel Questions, para. 100.

<sup>110</sup> U.S. Answers to Third Panel Questions, para. 18 (citing Moody's Investor Service, *The Application of Joint Default Analysis to Government Related Issuers* (Apr. 2005) at 1 (Exhibit EC-836)).

<sup>111</sup> EC Answers to Third Panel Questions, para. 102 ("The company's status as a GRI is, thus, unrelated to MSF loans ....").

<sup>112</sup> EC SWS, paras. 1036-1042.

93. Notably, the EC also admits in its response that Launch Aid is relevant to Moody's analysis of the credit rating of EADS

to the extent that these loans offload risk (*i.e.*, the variable repayment terms of MSF loans shift risk from EADS/Airbus to the member States).<sup>113</sup>

This is, of course, exactly the point that the United States has made throughout this dispute – that Launch Aid shifts the commercial risk of aircraft launch from EADS and Airbus to the EC and the Airbus governments. The LCA industry is profoundly shaped by a handful of strategic decisions to launch particular aircraft and the enormous commercial risk associated with these “bet-the-company” decisions.<sup>114</sup> This effect of Launch Aid on the economics of the most fundamental business decisions an LCA producer can make is precisely why Launch Aid distorts LCA markets in ways that other forms of government support may not.

94. In its response, then, the EC acknowledges that, by providing Launch Aid, the Airbus governments assume some of the commercial risk of Airbus LCA launch decisions. However, the EC contends that Moody's cannot assume that the Airbus governments do so on subsidized terms. According to the EC, any provision of risk-sharing capital, whether subsidized or not, would have the effect of transferring risk from EADS and Airbus, thus resulting in an improved credit rating for EADS.<sup>115</sup> In other words, the EC asserts that the improvement in the credit rating of EADS is not an effect of the subsidy because it flows from the very existence of risk-sharing capital, whether on subsidized terms or not. The EC argues that Moody's is indifferent to the cost of the risk-sharing capital.

95. The EC argument is incorrect. Moody's baseline credit assessment takes into account all “aspects of the entity's existing (or anticipated) business model.”<sup>116</sup> If Airbus had offloaded the same amount of risk at commercial rates, the cost of servicing that debt would have significantly impacted its “business model.”<sup>117</sup> The EC argument rests on the assumption that the subsidized terms of Launch Aid made no difference to the commercial behavior of Airbus. But, as the

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<sup>113</sup> EC Answers to Third Panel Questions, para. 103.

<sup>114</sup> U.S. Answers to Third Panel Questions, paras. 171-174; U.S. FCNOS, para. 128; *see also* U.S. FWS, para. 714-715.

<sup>115</sup> EC Answers to Third Panel Questions, para. 103.

<sup>116</sup> Moody's Investor Service, *The Application of Joint Default Analysis to Government Related Issuers* (Apr. 2005) at 2 (Exhibit EC-836).

<sup>117</sup> NERA Economic Consulting, *Quantification of Benefit of Launch Aid* (May 24, 2007) (Exhibit US-606); U.S. SWS, paras. 610-612.

United States has shown, the evidence proves that this assumption is false. The evidence shows both that Launch Aid was decisive at the time of each individual Airbus launch decision and that the cumulative financial impact of Airbus's having to repay Launch Aid at commercial rates is several times the market capitalization of EADS.<sup>118</sup> Thus, as Professor Kaivanto observes, "Launch Aid commits European governments to absorbing much of any possible losses, so even if Airbus is risk averse, it has little incentive not to adopt a risky, aggressive strategy."<sup>119</sup> One of the effects of Launch Aid, therefore, is to allow Airbus to "adopt a risky, aggressive strategy" – to the detriment of competitors – while enjoying access to capital at rates appropriate to a more "risk averse" company.

96. Finally, the EC is incorrect when it again contends that the improvement in EADS' credit rating is a "benefit" of Launch Aid that is already taken into account in the calculation of the magnitude of the subsidy.<sup>120</sup> The EC argument confuses "benefit" and "effect"; the improvement in EADS' credit rating resulting from Launch Aid is an effect of the subsidy that is properly included in the analysis of the subsidy's effects.

**264. In paragraph 1043 of its second written submission, the EC presents information which purports to demonstrate the GRI impact on Moody's credit rating. The EC presents [ ] which consider the change in current yield resulting from a change from A1 to A3. Does the EC consider that the change from A1 to A3 measures the total impact of the GRI? If so, could the EC please explain the basis for this view?**

Comment:

97. As the EC explains in its response, the EC is contending that the change from A1 to A3 represents only Moody's evaluation of the likelihood of a future government bailout of EADS. The EC does not contend that this change in credit rating measures the impact of Launch Aid; rather, the effect of Launch Aid is taken into account in Moody's baseline credit rating and therefore is accounted for in both the A1 and A3 ratings. Thus, the EC admits that its argument on this point has nothing to do with the impact of Launch Aid on the credit rating of EADS.

**265. Would the EC please address the following statement in Exhibit US-18 with respect to the A380 : "It seems doubtful that the enterprise would be in a position to find outside**

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<sup>118</sup> E.g., U.S. Answers to Third Panel Questions, paras. 41-43 (summarizing evidence).

<sup>119</sup> Kim Kaivanto, *Promise and Practice of UK Launch Aid*, 40 *Journal of World Trade* 495, 498 (2006) (Exhibit US-2).

<sup>120</sup> EC Answers to Third Panel Questions, para. 101.

**financing to meet its needs. ... Above all, however, such external financing would apparently add excessively to the financial expenses incurred by the firms, and would throw their balance sheets out of equilibrium because of the low level of their equity capital." Is it the EC's position that not only was the A380 economically viable without LA/MSF but that Airbus was in a position to seek outside financing to cover its development costs? If this is the EC position how should the Panel understand the above comment?**

Comment:

98. The EC contends both that the A380 was economically viable without Launch Aid and that Airbus could have financed the A380 launch without Launch Aid.<sup>121</sup> As the French Senate report provided as Exhibit US-18 makes clear, neither EC contention is credible.

99. In support of its contention that the A380 was economically viable without Launch Aid, the EC response (as elaborated in its response to Question 266) is that the A380 “business case confirms that the A380 programme was commercially viable absent” Launch Aid.<sup>122</sup> Because the EC has designated much of the A380 business case document as HSBI, the United States discusses it in the HSBI Appendix to these comments.

100. The EC also contends that the French Senate report is incorrect when it states that Airbus could not have financed the A380 launch without Launch Aid. First, the EC argues that the French Senate report, which was issued in 1997, addresses only the situation of Aérospatiale prior to the corporate reorganization that led to the formation of EADS and Airbus SAS.<sup>123</sup> The EC states, without proof, EADS – a corporate amalgamation of three of the Airbus companies – had greater financial resources than did Aérospatiale. However, EADS also had to bear the combined development costs attributable to each of those entities, while absent the reorganization Aérospatiale would only have been responsible for its portion of these costs. Moreover, the EC offers no evidence to support of its assertion that the evaluation of the French Senate would have been affected by the corporate reorganization of Airbus in 2000.

101. Second, the EC asserts that the French Senate report addressed only the impossibility of finding external “on balance sheet” financing, while not considering the possibility of “off-

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<sup>121</sup> EC Answers to Third Panel Questions, para. 106.

<sup>122</sup> EC Answers to Third Panel Questions, para. 111.

<sup>123</sup> EC Answers to Third Panel Questions, para. 107.

balance sheet” financing, such as contributions by risk-sharing suppliers.<sup>124</sup> To the contrary, the report is unequivocal in its conclusion that Launch Aid is the only possible way for Airbus to undertake major product development:

Taking into account the magnitude of the necessary financing for aeronautical programs, it would seem that, without public support, the companies might not be able to find the internal or external means necessary to undertake them.<sup>125</sup>

The report therefore does not support the EC’s argument that “public support” was considered only as an alternative to “on-balance-sheet” financing. Rather, it clearly concludes that “public support” is a necessary condition for Airbus to have access to any form of internal or external financing.<sup>126</sup>

102. Indeed, as the United States has previously observed, the participation of risk-sharing suppliers in Airbus projects is itself facilitated by Launch Aid. As the Airbus governments assume part of the commercial risk of the project, it becomes easier – and cheaper – for Airbus to find other entities willing to share the remainder of that risk.<sup>127</sup> Nothing in the French Senate report, or in the EC’s comments on it, alters that conclusion.

**266. At paragraph 1071 of its SWS, the EC notes that [**

**] Could the EC please explain how [**  
**] Could the EC also indicate how [**

**].**

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<sup>124</sup> EC Answers to Third Party Questions, para. 108.

<sup>125</sup> French Senate Report at 71 (“Compte tenu de l’ampleur des financements nécessaires aux programmes aéronautiques, il apparaît que, sans soutien public, les entreprises pourraient ne pas trouver les moyens internes ou externes nécessaires à leur mise en oeuvre.” (emphasis added)) (Exhibit US-18).

<sup>126</sup> The possibility that “partners outside of {Airbus} GIE” might assume part of the costs of the A380 is expressly considered in the report. French Senate Report at 73 (“A supposer que des partenaires extérieurs au GIE {Airbus} soient associés à ce programme ....”) (Exhibit US-18).

<sup>127</sup> See U.S. Comments on EC Answers to Second Panel Questions, paras. 43-52 and HSBI Appendix thereto (comments on EC answer to Question 215); U.S. SWS, paras. 113-119 and evidence cited therein.

Comment:

103. As noted in the comments to the EC's response to the previous question, the EC has designated much of the A380 business case document as HSBI, and the United States therefore discusses it in the HSBI Appendix to these comments.

104. However, the United States has already shown, through the analysis by Dr. Gary Dorman of the economics of a stylized launch decision, how Launch Aid not only increases the net present value (NPV) of an aircraft program, but also – and more importantly – increases the likelihood that the NPV will be positive and thus the likelihood that a decision will be made to proceed with a launch.<sup>128</sup> The EC provides a published study of the A380 launch decision, done at the Harvard Business School, that provides further insights into the economics of a launch decision and the factors to be taken into account in making such decisions.<sup>129</sup> Although the Harvard study employs publicly available estimates of various parameters affecting the A380 business case rather than the actual figures used by Airbus in its internal evaluation, the methodology used is instructive.

105. The Harvard study summarizes the enormous stakes of the launch of an aircraft like the A380:

First, the superjumbo is a strategic commitment of more than average interest because of its sheer size, irreversibility and potential impact on industry structure. The superjumbo represents one of the largest product launch decisions in corporate history given Airbus' projected launch cost of \$11.9 billion (a figure that also represented 26% of total industry revenues – \$45.6 billion – and more than 70% of Airbus' total revenues – \$17.2 billion – in 2000). The riskiness of expenditures of this magnitude is magnified by the fact that Airbus has to spend essentially the entire amount before it makes its first delivery, in an industry in which many firms – e.g., Glenn Martin, General Dynamics, and, more recently, Lockheed – failed as a result of bet-the-company product development efforts. If, however, the launch succeeds, Airbus is expected to dislodge Boeing as the market leader in commercial aircraft ....<sup>130</sup>

106. The Harvard study, like the prototypical business case described by Dr. Dorman, sets out a “base case” and various alternatives in order to answer the question: “{H}ow optimistic do we

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<sup>128</sup> Dr. Gary J. Dorman, *The Effect of Launch Aid on the Economics of Commercial Airplane Programs* (Nov. 6, 2006) (Exhibit US-70).

<sup>129</sup> Benjamin Esty & Pankaj Ghemawat, *Airbus vs. Boeing in Super Jumbos* (Harvard Business School Strategy Working Paper No. 02-061, Feb. 2002) (“Harvard Study”) (Exhibit EC-344).

<sup>130</sup> Harvard Study at 1 (Exhibit EC-344).

have to be about the volumes of and margins on superjumbos to make the project a value-enhancing proposition for Airbus?”<sup>131</sup> The “base case” in the Harvard study assumes a steady-state delivery rate of 50 aircraft per year (equivalent to 701 total deliveries by 2020), a sales price of \$225 million (denominated in 2008 dollars), costs that are low enough to yield an estimated operating margin of 15 percent, total fixed investment of \$11.9 billion (including \$2.5 billion in Launch Aid), and a discount rate of 11 percent.<sup>132</sup> On these assumptions, the Harvard study calculates a total NPV for the project, discounted to December 2000, of \$348 million.<sup>133</sup>

107. The Harvard study also includes a sensitivity analysis in Table I of the paper.<sup>134</sup> In the sensitivity analysis, the authors evaluate peak delivery rates ranging from 20 to 70 per year (i.e., 60% below to 40% above the “base case”), prices ranging from \$165 million to \$245 million per plane (i.e., 27 percent below to 9 percent above the “base case”), fixed launch costs ranging from \$8.7 billion to \$12.7 billion (i.e., \$1 billion below to \$3 billion above the “base case”), variations in the length of the ramp-up period (up to a possible two-year delays), and discount rates from 8% to 14%.<sup>135</sup> The study concludes that, while the NPV of the “base case” is positive at \$348 million, the NPV becomes sharply negative if any one of the following events occurs:

- ***Decrease in volume sold of 20%.*** If the “steady-state” delivery stream is 40 aircraft per year rather than 50, the NPV falls from positive \$348 million to negative \$876 million.
- ***Decrease in average price of 18%.*** If the average sales price falls from \$225 million (in 2008 dollars) to \$185 million, a decrease of about 18 percent, the NPV falls from positive \$348 million to negative \$732 million.
- ***Decrease in operating margin to 10%.*** If per-unit costs increase such that the operating margin is 10% rather than 15%, the NPV falls from positive \$348 million to negative \$1,677 million.

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<sup>131</sup> Harvard Study at 11 (Exhibit EC-344).

<sup>132</sup> Harvard Study at 11-12 and Appendix I (Exhibit EC-344).

<sup>133</sup> Harvard Study at 12 (Exhibit EC-344).

<sup>134</sup> Harvard Study at 49 (Exhibit EC-344).

<sup>135</sup> Harvard Study at 49 (Exhibit EC-344).

- **Two-year delay in ramp-up.** If the delivery rate of 50 aircraft per year is achieved two years later than planned, the NPV falls from positive \$348 million to negative \$601 million.<sup>136</sup>

108. The inherent uncertainty of predicting the LCA market over a twenty-year period requires an LCA producer to carefully consider such a sensitivity analysis in making the decision to launch any aircraft program, let alone a project of the colossal scale and risk of the A380. Indeed, the downside risks outlined in the previous paragraph [

].<sup>137</sup> Based on publicly available information, some, if not all, of them are in fact actually occurring – including lower prices, higher costs, and significant delivery delays.

109. The Harvard study illustrates, first, what a robust sensitivity analysis actually entails, and makes clear that the full downside risks of a program like the A380 are not captured by an analysis of an optimistic “base case” and a “worst case” that fails to capture the true risk over the life of a program. One must also examine the NPV of a wide range of possible outcomes in order to know how sensitive the program’s success will be to the assumptions underlying the “base case.” Because Launch Aid reduces the risk to the producer in the event that the assumptions fall short of expectations, it decreases the LCA producer’s sensitivity to these assumptions, and makes launches more likely – even if the NPV of the “base case” would be positive without Launch Aid.

#### D. INFRASTRUCTURE

**267. At paragraph 363 of its SWS, the United States argues that, even if the investment in creating the land is not taken into account, the land-lease price for the Mühlenberger Loch site is below the price Airbus would have paid in the market because, (a) the lease price was determined based on the value of the land, with a return on investment equal to the property interest rate, which is used for valuation of land, but provides no guidance as to the appropriate market rent for a specific property, and (b) even this price was reduced because of the expected settlement of parts of the site, requiring additional investment by Airbus it would not have incurred had the land not been newly reclaimed. Could the EC please respond to these arguments?**

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<sup>136</sup> Harvard Study at 49 (Exhibit EC-344).

<sup>137</sup> EC Answers to Third Panel Questions, para. 114.

Comment:

110. See comment to the EC's response to Question 268 below.

**268. The EC asserts, at paragraphs 808 - 818 of its FWS, that a benchmark return on investment involves only a fair price for the current value of the land, and does not include a component to compensate Hamburg for the full costs for development of the site. Does the EC agree that the amount of rent charged to Airbus Germany does not include a component to compensate Hamburg for the full costs for development of the site?**

Comment:

111. The EC's responses to these two questions once again reflect the fundamental difference between the approach taken by the EC and the approach taken by the United States to the analysis of the creation and provision of land for Airbus in *Hamburg-Finkenwerder*: The EC seeks to make the Panel believe that one can (and should) distinguish between the creation of the land for Airbus and the lease thereof to Airbus. Based on this distinction, the EC argues that the terms of the lease agreement should be analyzed, for the purpose of determining whether they convey a benefit to Airbus, as if the land had always existed.

112. However, the EC is asking the Panel to ignore the specific facts of this case, namely, that Hamburg created the land specifically, and only, for Airbus.<sup>138</sup> The distinction suggested by the EC between the creation of tailor-made land for the exclusive use by Airbus, and its provision to Airbus, is artificial and theoretical. This approach is flawed because it fails to take into account that the land is not general infrastructure and thus does not capture the economic effect of the measure at issue here: the creation and provision of land to Airbus.<sup>139</sup>

113. The course of action chosen by the City of Hamburg - and defended by the EC - ultimately results in a benefit to Airbus equivalent to a grant of at least Euro 630 million.<sup>140</sup> The lease price paid by Airbus did not even come close to creating a return on the investment made by Hamburg; in fact, considering the average German inflation rate, the effective return is negative. Even using the 6.5 percent return that the EC alleges a commercial investor would have requested (instead of the 9 to 12 percent return established by Dr. Keunecke), the lease price such an investor would have asked for would have been more than [ ] times the effective

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<sup>138</sup> See, e.g., U.S. SWS, paras. 317-352.

<sup>139</sup> See also U.S. SWS, para. 316.

<sup>140</sup> See U.S. SWS, para. 359.

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average lease price paid by Airbus. The United States has explained this in detail in its previous submissions.<sup>141</sup>

114. But the City of Hamburg did not even ask for a commercial rent if one accepts the EC's hypothesis that the land had not been created specifically for Airbus, but had already existed. In its response to question 267, the EC fails to rebut the arguments made in the U.S. SWS. The United States has shown in its SWS that, first, the "*Liegenschaftszinssatz*" used by the Hamburg Committee of Experts for Property Values is not the appropriate commercial benchmark.<sup>142</sup> Second, it has shown that a commercial investor would not have accepted a further reduction of the lease price for future settlements of the land.<sup>143</sup>

115. The United States will respond to the EC's failed attempt at a rebuttal of these points in turn. Before doing so, the United States notes again, in response to the EC's assertion that it is "undisputed" that the Hamburg Committee of Experts for Property Values is "competent" and "independent,"<sup>144</sup> that in this case there are doubts as to the independence of the Committee. As noted before, the Committee itself acknowledges that the lease agreement between Hamburg and Airbus refers to [

] The Committee says that this has not tainted its review of the rent. According to the opinions, rather than [

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<sup>141</sup> See, e.g., U.S. SWS, paras. 356-362.

<sup>142</sup> U.S. SWS, paras. 367-372.

<sup>143</sup> U.S. SWS, para. 366.

<sup>144</sup> EC Answers to Third Panel Questions, para. 116.

<sup>145</sup> Committee of Experts for Property Values in Hamburg, Report, G03.0058 M21, October 23, 2003, at 2-3 of the English translation (Exhibit EC-563) (BCI).

] for the Committee’s opinion<sup>146</sup> which raises doubts as to the credibility of the reports.<sup>147</sup>

“Liegenschaftszinssatz” is not appropriate as a benchmark

116. The United States has demonstrated why the *Liegenschaftszinssatz* (property interest rate) is not appropriate as a commercial benchmark for examining the rent paid by Airbus for the *Mühlenberger Loch* site (even assuming it had already existed).

117. In brief: The *Liegenschaftszinssatz* is an average value based on a very broad range of other properties. It does not reflect the specific lease price that could be asked for a specific property. In addition, it is only a calculating factor used in one of three methods for the valuation of land, and, notably, the method used for the valuation of built-up land (which is a “mass-market” where average lease prices may be informative) rather than for the valuation of vacant land (where lease agreements for industrial property are rare).<sup>148</sup> The Committee of Experts for Property Values itself acknowledged that it is difficult to “determine a market-oriented interest rate on the property” and pointed to the problems associated with using an average property interest in a case that is “untypical even for industrial land in Hamburg.”<sup>149</sup>

118. The United States has shown that the monthly lease price of Euro [ ] per square meter effectively paid by Airbus (and endorsed by the Committee) is far off the monthly lease price of at least Euro 1.00 per square meter for vacant land for industrial use in Hamburg and elsewhere.<sup>150</sup> In addition, the United States has shown that a commercial owner - in the EC’s hypothetical that the land had already existed - would have asked for (and would have obtained) a premium on the generally applicable commercial benchmark because the location and size of the site are particularly suitable for Airbus.<sup>151</sup>

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<sup>146</sup> Committee of Experts for Property Values in Hamburg, Report, G03.0058 M21, October 23, 2003, at 2 of the English translation (Exhibit EC-563) (BCI).

<sup>147</sup> See also U.S. SWS, para. 365.

<sup>148</sup> U.S. SWS, paras. 367-372.

<sup>149</sup> Committee of Experts for Property Values in Hamburg, Report, G03.0058 M21, October 23, 2003, at 6 of the English translation (Exhibit EC-563) (BCI)

<sup>150</sup> U.S. SWS, para. 371 and footnote 457.

<sup>151</sup> U.S. SWS, para. 372 and footnote 458.

119. In its response to the Panel’s question, the EC does not address any of these facts. Instead, the EC relies primarily on the Keunecke opinion to defend the lease price paid by Airbus. But its statement that “Dr. Keunecke has confirmed the approach of the Hamburg Expert Committee” (i.e., to determine the rent based on the *Liegenschaftszinssatz*)<sup>152</sup> is plainly wrong. Most notably, Dr. Keunecke did not undertake to determine the rent that a commercial owner of pre-existing land in the immediate vicinity of Airbus’ existing site at Hamburg Finkenwerder would have charged Airbus - which is a purely hypothetical situation that Dr. Keunecke did not need to address.

120. Rather, Dr. Keunecke’s study focused on the measure at issue: the creation and provision of new land to Airbus. The study therefore examines whether a commercial investor would have provided Airbus with a newly created, tailor-made site for Airbus’ exclusive use (including the geographical and legal limitations on the use of the land described previously<sup>153</sup>) under the terms and conditions of the lease agreement between the City of Hamburg and Airbus.

121. As pointed out by Dr. Keunecke, before investing in the creation of new industrial or commercial space, a commercial investor undertakes a cost/benefit analysis. As part of such a cost/benefit analysis, a commercial investor compares the costs of planning, preparing, developing and marketing as well as the risks and the expected profit margin with the expected sales proceeds (or with other return, such as from renting the property). If the terms and conditions of an investment are such that the results of the cost/benefit analysis are negative (or if the profit margin is lower than the profit margin that the investor expects to generate with such investments), the project is not implemented at all (or, at least, it is not implemented under those terms and conditions).<sup>154</sup>

122. Against this background the United States asked Dr. Keunecke to “review{...} land values for sites in Hamburg and elsewhere similar to Airbus’ site at Kreetslag 10, 21129 Hamburg-Finkenwerder.” It also asked Dr. Keunecke to assess “whether, based on these benchmarks, a commercial investor would have made the investments undertaken by the Hamburg government.”<sup>155</sup> In order to make this assessment, Dr. Keunecke analyzed what return on this investment a typical commercial investor would have sought to achieve, based on

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<sup>152</sup> EC Answers to Third Panel Questions, para. 122.

<sup>153</sup> U.S. SWS, paras. 340-349.

<sup>154</sup> Keunecke Report (Exhibit US-189), pp. 9-10.

<sup>155</sup> Keunecke Report (Exhibit US-189), p. 2.

“general expectations concerning return on real estate investments.”<sup>156</sup> These general expectations are not the equivalent of the lease price for a specific (pre-existing) piece of land (which the EC seeks to establish in its hypothetical), but they determine the outcome of an investor’s decision whether or not to make this investment. If the expected return under the terms and conditions of a specific lease agreement falls below the generally expected return, the investor would either re-negotiate the terms to bring the profit margin up to the expected level or turn to a more profitable investment.

123. Based on the specific facts of this case (rather than on the EC’s theory that there had been land in the *Mühlenberger Loch* that the City of Hamburg happens to lease to Airbus), Dr. Keunecke concludes that

“the creation and development of the ‘Mühlenberger Loch’ site for Airbus was not guided by commercial considerations. A commercial investor would neither have undertaken the investment in the first place, nor would a commercial investor lease the land to Airbus at the terms and conditions of the lease agreement between Hamburg and Airbus as reported.”<sup>157</sup>

124. But the EC even goes beyond arguing that the Keunecke opinion supports its determination of the lease price for pre-existing land in the *Finkenwerder* area. It also argues that Dr. Keunecke’s conclusion, that a commercial investor would either have asked Airbus for a lease price (or equivalent) commensurate with a reasonable return on the investment or would not have undertaken the investment, is “inconsistent with the rest of Dr. Keunecke’s report”. The EC acknowledges that “the cost of the land far exceeds its value.” It asks: “Having concluded that a market investor would not have undertaken the land reclamation project in the first place, how can Dr. Keunecke then posit a ‘market’ rent based on the cost of the reclamation?”<sup>158</sup> Put differently, the EC appears to argue that the Panel should simply ignore the cost of creating the land because it exceeds the value of the land. And, in the EC’s view, because the cost of creating the land exceeded its value, Hamburg was also right to ignore this cost when determining the lease price (and, instead, according to the EC, rightly reverted to an entirely hypothetical situation where the land leased to Airbus has always existed).

125. It is this approach, rather than that of Dr. Keunecke, that is “not credible.” In fact, in the view of the United States (and of Dr. Keunecke), this is exactly the point: The City of Hamburg

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<sup>156</sup> Keunecke Report (Exhibit US-189), pp. 8-9.

<sup>157</sup> Keunecke Report (Exhibit US-189), p. 9.

<sup>158</sup> EC Answers to Third Panel Questions, para. 129.

provided Airbus with a newly created, tailor-made site adjacent to its existing manufacturing facilities at Finkenwerder. As explained in previous submissions, the site was created exclusively for the purpose of allowing Airbus to expand its existing facilities; in fact, given the geographical situation and legal restrictions, the site cannot be leased to, and used by, any other user.<sup>159</sup> The City of Hamburg invested over Euro 500 per square meter in the creation of the non-general infrastructure provided to Airbus for its exclusive use.<sup>160</sup> But it asks for a lease price calculated on the basis of Euro 55 per square meter (and then even [ ] the lease price so calculated because the land was newly created and thus still settles).<sup>161</sup>

126. One thing is clear: A commercial investor would not have agreed to any of this, but would have asked for a return that is reasonable in light of the investment in the creation and provision of the site as non-general infrastructure for Airbus (or, alternatively, would not have undertaken the investment). Unlike the City of Hamburg, a commercial investor would not have accepted an arrangement under which the effective return on the investment is negative (because the average inflation rate exceeds the return): This is all that Dr. Keunecke says. When Dr. Keunecke's analysis is thus properly understood, it is not clear to the United States on what basis the EC finds any of this to be "fundamentally inconsistent" and "not credible."<sup>162</sup>

127. Finally, the EC argues that no further adjustment on the *Liegenschaftszinssatz* (property interest rate) used by the Hamburg Committee of Experts on Property Values - 6.5 percent - was needed because the land has no limited life cycle and because the long-term nature of the lease agreement with Airbus reduces the risk of vacancy to zero.<sup>163</sup> However, first, the United States has shown that Hamburg could have asked for a premium on the lease price, given the particular

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<sup>159</sup> U.S. SWS, paras. 340-349.

<sup>160</sup> The City of Hamburg spent Euro 751 million to create 1,400,000 square meters of new land.

<sup>161</sup> U.S. SWS, para. 353.

<sup>162</sup> To the extent that the EC's argument rests on the phrase "assuming an investment sum" in Dr. Keunecke's opinion (which leads the EC to conclude that Dr. Keunecke himself did not actually reach the conclusion that a commercial investor would not have leased the land to Airbus at the price charged by Hamburg) (*see* para. 130 of the EC Answers to Third Panel Questions), the EC ignores that the phrase "assuming an investment sum" refers back to the description of the facts in part 1 (pp. 2-3) of the opinion. This phrase reflects the fact that Dr. Keunecke did not himself examine whether Euro 751 million was actually the investment sum, but relied on reports published by the Hamburg government, Parliament and Court of Auditors for this and other information/data used in his study.

<sup>163</sup> EC Answers to Third Panel Questions, para. 151. The Hamburg Committee of Experts on Property Values has relied on similar reasons, *see* the quote at EC Answers to Third Panel Questions, para. 120.

benefits of the site for Airbus.<sup>164</sup> The EC has not disputed this fact. Second, while an adjustment might not be justified in other cases for the reasons submitted by the EC, this is not true in this case. As explained before, the land leased to Airbus can, for geographical and legal reasons, only be used by Airbus and only for the purpose of building and operating an aircraft factory.<sup>165</sup> Thus, the risks associated with marketing the “reclaimed land and special-purpose facilities at issue”<sup>166</sup> are, in fact, quite high: Airbus is the only potential user (with a high risk, and, in fact, certainty of vacancy if Airbus fails to rent the land), and the (economic) life cycle of the land (i.e., the time during which the land generates return) is limited to the duration of the lease to Airbus. As confirmed by Dr. Keunecke’s analysis, a commercial investor would factor those risks into its expected rate of return as an upward adjustment.

Reduction of the lease price to account for future settlements of the land

128. The EC justifies the reduction of the lease price to account for future settlements of the land by arguing that, if one accepts the EC’s hypothetical that the land had already existed (rather than having been newly created), the settlement is a “defect of the land.” In other words, assuming Airbus had leased existing industrial land, Airbus would have been entitled to compensation for additional expenses incurred associated with the settlement process. The reduced lease price, according to the EC, is the economic equivalent to such compensation.<sup>167</sup>

129. As a preliminary matter, the United States notes that the EC’s arguments highlight the absurdity of its distinction between the creation and the provision of the newly created land to Airbus: Not only did the City of Hamburg create tailor-made land for the sole purpose of allowing Airbus to expand its existing facilities in Hamburg, investing Euro 751 million into the land. The City went so far as to see the need to create new land as a “defect” of that land and to commit itself to remedy any inconveniences that Airbus might experience because the land had to be newly created for it.

130. Even accepting *arguendo* the false distinction advanced by the EC, however, the United States disagrees that a lower lease price would have been warranted by virtue of the settlements. First, the risk of settlements is already priced into the value of the site and does not justify any further reduction of a lease price calculated by the City of Hamburg based on this price. As the

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<sup>164</sup> U.S. SWS, para. 232.

<sup>165</sup> EC Answers to Third Panel Questions, para. 127.

<sup>166</sup> EC Answers to Third Panel Questions, para. 127.

<sup>167</sup> EC Answers to Third Panel Questions, paras. 133-139.

*Bodenrichtwertkarte* for Hamburg (a map containing average benchmark values for land) shows (and as the EC agrees<sup>168</sup>), the value of the (existing) land at *Kreetslag* in *Finkenwerder* (the existing site of Airbus in Hamburg) was between Euro 51 (2000) and Euro 59 (2005) per square meter.<sup>169</sup> Airbus experiences the same problems concerning the settling of the land on this existing site that, in the EC view, justify the reduction of the lease price for the newly created land. In fact, the opinion of the Committee of Experts for Property Values states that the expected costs to prevent and repair damages from future settlements of the land “are based on the experience of the DASA at its previous work site.”<sup>170</sup> In other words: The value of the land is quite low, compared with other land in Hamburg, because there is a risk of settlement (and flooding) that requires additional construction work. The methodology suggested by the EC therefore effectively results in double-counting the risk of settlement.

131. Second, the methodology used by the EC - an adjustment of the lease price according to the specific costs that Airbus expects to incur - is not suitable to determine a market price for the land. A commercial investor - that is, in the EC’s hypothetical, the owner of pre-existing land that could be used by a variety of users - would aim to maximize the lease price. Such an investor would not accept any reduction of the lease price simply because the land does not meet the specific requirements of one user. A close examination of the opinion issued by the Committee of Experts shows that the expected costs to prevent and repair damages from future settlements are closely associated with the specific use of the site by Airbus (including the location, number and size of the buildings and the special requirements applying to taxiways and parking space for aircraft).<sup>171</sup>

**269. At paragraphs 872-874 of its FWS, the EC acknowledges that Airbus is the only user entitled to use the full length of the Bremen runway, and recognizes that provision of this exclusive right may amount to a financial contribution. However, the EC argues that Airbus should not be liable for any additional fees beyond those generally applicable to all users of the runway (without the extension). Is it the EC view that the provision of this exclusive right has no value? Could the EC explain whether, and if so, under what**

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<sup>168</sup> See, e.g., EC FWS, paras. 806-807.

<sup>169</sup> Keunecke Report (Exhibit US-189), pp. 4-5, and Annex 2 to the Keunecke Report.

<sup>170</sup> Committee of Experts for Property Values in Hamburg, Report, G03.0058 M21, October 23, 2003, at 9 of the English translation (Exhibit EC-563) (BCI)

<sup>171</sup> Committee of Experts for Property Values in Hamburg, Report, G03.0058 M21, October 23, 2003, at 9-14 of the English translation and Annexe 1 (Exhibit EC-563) (BCI). In fact, as noted before, the calculations have been based on DASA’s prior experience with its existing site (at 9) and are thus necessarily linked to the specific requirements of Airbus.

**circumstances, this exclusive right could be revoked? Could the EC explain whether, and if so, under what circumstances, this exclusive right could be transferred to another company or made non-exclusive by allowing another company to also use the full length of the runway?**

Comment:

132. The United States notes that the EC finally admitted that “the use of the extended runway is currently only open to certain freighters from Airbus and not to other companies.”<sup>172</sup> In other words, Airbus is the only company allowed to use the full length of the runway at Bremen airport (including the extensions at both ends of the runway) under the current regulations.<sup>173</sup> The EC also admits that “allowing Airbus to use the extended runway” constitutes a financial contribution within the meaning of Article 1.1(a) (iii) of the SCM Agreement: the provision of a service other than general infrastructure.<sup>174</sup> As Airbus is the only company allowed to use the extended runway, the measure is also specific, within the meaning of Art. 2 of the SCM Agreement.

133. Having recognized that allowing Airbus to use the extended runway falls plainly within the terms of Article 1.1(a)(1)(iii) of the SCM Agreement, the EC then attempts to introduce a distinction between the provision of a service and access to a service, asserting that “{t}he agreement” is not concerned with questions of access to services provided by governments.<sup>175</sup> Notwithstanding the EC’s reference to “the agreement,” the text of the SCM Agreement not only fails to support the EC’s assertion, but flatly contradicts it. Indeed, Article 2 of the SCM Agreement makes clear that “limit{ing} access to a subsidy to certain enterprises” renders that subsidy specific. Article 14(d) also provides that the “availability” of (i.e., access to) a government-provided service is one factor to be considered when examining adequacy of remuneration in the context of a benefit determination. Therefore, where the subsidy at issue is, as provided for in Article 1.1(a)(1)(iii), the provision of a service by a government, the extent to which other users may access that service is critical to any inquiry under the SCM Agreement.

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<sup>172</sup> EC Answers to Third Panel Questions, para. 146.

<sup>173</sup> EC Answers to Third Panel Questions, paras. 145-146.

<sup>174</sup> See EC Answers to Third Panel Questions, paras. 146-147. The United States has explained in more detail why the extension of the runway and the noise protection measures are not general infrastructure in response to Panel Questions 20 (a) and 22, see U.S. Answers to First Panel Questions, paras. 152-154 and 158-161.

<sup>175</sup> See EC Answers to Third Panel Questions, para. 147 (response to question 269).

**270. The EC contends that aircraft weight bears a relationship to the use of the runway extension because heavier aircraft require a longer runway. The EC contends that Airbus operates heavier planes, and consequently it pays for the use of the runway extension. The United States, however, argues at paragraph 419 of its SWS that the fees are based on maximum take-off weight, which has nothing to do with the actual take-off weight, which latter determines the runway length necessary, and is therefore not dispositive of whether or not a departing or landing aircraft uses the extended runway. The United States also argues that the maximum take-off weight of the aircraft used by Airbus to transport wings from Bremen is not particularly high, and that in any event, regardless of the maximum take-off weight, users other than Airbus are not allowed to use the extended runway. Could the EC please comment?**

Comment:

134. Before commenting on the EC's response to this question, the United States recalls that the EC admits that Airbus does not pay any fee for the use of the runway extension that would allow Bremen airport (or the City of Bremen) to recoup the investment made in the runway extension.<sup>176</sup> The EC argued, however, that the City of Bremen's fee regulations imposed an implicit fee for the runway extension because "{h}eavy aircraft trigger the highest user fees" and, therefore, "the City of Bremen earns higher fees from use of the extended runway, since aircraft using that runway pay the highest weight-related fee."<sup>177</sup>

135. The United States has shown that the EC's argument based on the City of Bremen's fee regulation is factually and legally wrong for the reasons summarized by the Panel in its question.<sup>178</sup> The EC fails to rebut the facts and the legal argument presented by the United States. First, the United States is surprised to find the EC advancing the view that the (obvious) fact that the "additional number of passengers has a clear influence on the actual take-off weight" affects whether Airbus pays adequate remuneration for the use of the extended runway.<sup>179</sup> It is beyond dispute that the extended runway may only be used by Airbus-owned freighters, and, for that matter, by extra-large freighters, the Beluga and the Super Guppy. Airbus may not use the extended runway for passenger airplanes, and the use of the extended runway by Belugas or

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<sup>176</sup> See U.S. SWS, para. 418, for cites to the EC submissions.

<sup>177</sup> EC Answers to First Panel Questions, para. 257.

<sup>178</sup> U.S. SWS, para. 419.

<sup>179</sup> EC Answers to Third Panel Questions, paras. 150-151.

Super Guppies carrying Airbus wings will certainly not depend on the number of passengers on board.

136. Second, the United States has not argued in this dispute that there is anything wrong with choosing the maximum take-off weight (rather than the actual take-off weight) to determine landing fees. Nor does the United States argue that “landing fees must be 100% proportional to the actual take-off weight.”<sup>180</sup> The United States only notes, in response to the EC’s defense summarized above, that a fee calculated on the basis of maximum take-off weight has nothing to do with a fee for the use of the extended runway that would generate a return on the investment made building the extension).

137. Third, the EC appears to have forgotten its own explanation why the Bremen fee regulations impose an implicit fee for the use of the runway extension. Its implicit fee theory would only make sense if the maximum weight of the Airbus-owned aircraft allowed to use the extended runway - the Beluga and the Super Guppy - were so extraordinarily high that Airbus would have to pay, by definition, a higher fee than any other user of the airport (which is not allowed to use the extension). If so, the difference between the fee charged for the Beluga and the Super Guppy (which may use the extension) and “usual” aircraft of other users (which may not use the extension) might be seen as an implicit fee for the extension. The comparison submitted by the United States shows, however, that the maximum weight of the Beluga and the Super Guppy is not such as to carry an implicit fee.<sup>181</sup>

138. To the extent that the EC now says that the United States should have compared fees paid for the Beluga and the Super Guppy to the fees paid for “passenger aircraft using the ordinary length of the runway,”<sup>182</sup> the United States notes that the discrepancy becomes even bigger: As the EC correctly notes, fees paid for passenger aircraft are “based on the maximum take-off weight of the aircraft ... and, in addition in commercial and intra-company traffic, on the number of passengers on board of the aircraft.”<sup>183</sup> Typically, fees for passenger aircraft using the ordinary length of the runway are therefore often substantially higher than the fees paid for the Beluga or Super Guppy using the extended runway.<sup>184</sup> Finally, contrary to the EC’s view, the United States

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<sup>180</sup> EC Answers to Third Panel Questions, paras 152-154.

<sup>181</sup> See U.S. SWS, para. 419, n.529.

<sup>182</sup> EC Answers to Third Panel Questions, para. 155 (response to Question 270).

<sup>183</sup> EC Answers to Third Panel Questions, para. 150 (response to Question 270) (quoting the Bremen fee regulation).

<sup>184</sup> See U.S. SWS, para. 419, n.529.

has not argued that the Bremen fee regulation is discriminatory.<sup>185</sup> The United States simply contests the EC's own theory that it contains an implicit fee for the use of the extended runway.

139. Fourth, the EC suggests that the fact that Airbus is the only company allowed to use the extended runway is irrelevant for determining the benefit.<sup>186</sup> This is wrong. As the EC admits, "allowing Airbus to use the extended runway" constitutes the provision of a service within the meaning of Article 1.1 (a) (iii) of the SCM Agreement.<sup>187</sup> Only Airbus - as the exclusive user of the extended runway - could therefore receive a benefit from that use and it does so if it pays less than adequate remuneration for the use (Article 14 (d) of the SCM Agreement). Because the extension of the runway is only available to Airbus and may not be used by any other user of Bremen airport, it would be inappropriate to allocate the investment made by Bremen for the extension to such other users.<sup>188</sup> Rather, Airbus (as the exclusive user of the runway) should pay a fee that, to be adequate, generates a reasonable return on the investment made by Bremen.

140. In sum, having invested in the runway extension exclusively for the benefit of Airbus, the City of Bremen fails to recoup from Airbus a return on that investment. Instead, Airbus continues to enjoy the use of that extended runway to the exclusion of all other users for a nominal fee that in no way compensates for that use.

**271. The Panel understands the United States to argue, at paragraph 411 of its SWS, that the lease price for the EIG facilities in the ZAC Aéroconstellation was calculated so as to amortize the investment cost of €80.1 million over 40 years, with an interest rate of 2.2 percent for €62.6 million, and an interest rate of 4.5 percent for the remaining €17.5 million. The Panel further understands the United States to argue that these amounts are not consistent with a market benchmark because the resulting 3.9 percent initial net return on the entire investment of €80.1 million in building the EIG facilities is less than the amount a commercial investor in industrial real estate in Toulouse would have required, which the United States asserts would have been between 9 and 11 percent for the period 2002 and 2004, resulting in a lease price of between €7.2 million and €8.8 million. Could the EC please comment on this argument?**

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<sup>185</sup> EC Answers to Third Panel Questions, para. 155.

<sup>186</sup> EC Answers to Third Panel Questions, para. 156; see also the EC's response to Panel Question 269, paras. 147-148.

<sup>187</sup> EC Answers to Third Panel Questions, para. 146. See above at para. 126 (comment on response to Question 269).

<sup>188</sup> In that sense, contrary to the EC's view in response to Panel Question 269, it is of course relevant that access to this service is limited to Airbus. See above at para. 127 (comment on response to Question 269).

Comment:

141. The EC criticizes the demonstration by the United States that the lease of the EIG facilities constitutes a subsidy to Airbus, within the meaning of Article 1 of the SCM Agreement, because, in the EC's view, the lease should be treated as a long-term, 40-year loan, with Airbus France's average cost of debt at the time as benchmark (which the EC admits was 6.83 percent). In doing so, the EC effectively concedes that the lease confers a substantial benefit of at least Euro 2.3 million per year (or over Euro 90 million over the term of the lease) on Airbus.

142. As explained in previous submissions,<sup>189</sup> under the terms of the lease agreement, the lease price for the EIG facilities is calculated so as to amortize the investment cost of Euro 80.1 million over 40 years; the lease price also reflected a mark-up of 2.2 percent on Euro 62.6 million of the investment cost, and a mark-up of 4.5 percent for the remaining Euro 17.5 million. Assuming equal annual payments,<sup>190</sup> the terms of the lease agreement translate into a lease price of Euro 2.3 million per year for the Euro 62.6 million share and Euro 0.9 million per year for the Euro 17.5 million share of the investment (totaling Euro 3.2 million). The EC does not dispute any of these facts.

143. Accepting for the sake of argument the approach taken by the EC, including its admission that Airbus cost of debt for this period was 6.83 percent,<sup>191</sup> a market-based lease price should have been Euro 5.5 million per year<sup>192</sup> – almost double the amount paid by Airbus. Thus, even using the EC's approach to analyzing the lease term, including the benchmark proposed by it, Airbus saves at least Euro 2.7 million per year from the beneficial terms of the lease of the EIG facilities.<sup>193</sup>

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<sup>189</sup> See, e.g., U.S. SWS, paras, 410-411.

<sup>190</sup> In fact, as shown before, the lease did not provide for equal payments, but for progressively increasing payments, a source of additional benefit to Airbus.

<sup>191</sup> EC Answers to Third Panel Questions, para. 160.

<sup>192</sup> See the calculation attached as Exhibit US-686. The United States fails to understand how the EC arrived at the amount of Euro 4.4 million used in EC Answers to Third Panel Questions, para. 161. The EC has not explained its calculation method, nor has it revealed its calculation.

<sup>193</sup> While the EC suggests that 6.83 percent was Airbus France's average cost of debt throughout the entire period (EC Answers to Third Panel Questions, para. 160), the United States has used previously 6.83 percent for the Euro 62.6 million share agreed in 2002 and 6.17 percent for the Euro 17.5 million share agreed in 2004 (U.S. SWS, para. 411, n.512). Even if calculated on this more conservative basis, the lease price would have been Euro 4.3 million for the Euro 62.6 million share and Euro 1.1 million for the Euro 17.5 million share (totaling Euro 4.4 million per year, or Euro 2.2 million per year more than the lease price agreed). See the calculation attached as

144. In addition, even accepting *arguendo* the approach of the EC, the use of Airbus France's average cost of debt understates by far the true value of the benefit of the lease to Airbus. First, a 40-year loan would carry a very significant mark-up for the duration of the loan (which increases the risk of default of the creditor and the risk of inflation significantly)<sup>194</sup> and for the risk that (refinancing) interest rates would increase during such a long period.<sup>195</sup> Second, the lease price is progressive and thus effectively results in a deferral of repayments of the EC's hypothetical loan.<sup>196</sup> While the average lease price was calculated as if it were the annual repayment on a 40-year loan carrying 2.2 percent or 4.5 percent interest, respectively, the individual lease prices per year are progressive, with payments falling below the average for the first fifteen years of the lease term.<sup>197</sup> Even if the EC's approach to assessing the lease of the EIG facilities were correct in principle, this deferral of repayments under the EC's hypothetical loan scenario would result in an additional premium on the interest rate. Thus, although the EC effectively admits an annual subsidy benefit of Euro 2.3 million, even using its methodology, the true benefit would be far higher than that.

145. In addition to challenging the methodology applied by the United States to assessing the lease agreement for the EIG facilities, the EC also challenges the United States' benchmark lease price of at least between Euro 7.2 million and Euro 8.8 million (which was based on an initial net return of at least between 9 and 11 percent).<sup>198</sup> The arguments presented by the EC, however, suffer from a series of substantial flaws:

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Exhibit US-686.

<sup>194</sup> The yield curve is generally upward sloping, i.e., longer-term loans will carry higher rates. Credit spreads will increase with maturity as well, thus resulting in even higher rates on longer-term borrowing. See NERA, Economic Assessment of the Benefits of Launch Aid (Nov. 10, 2006), Exhibit US-80 (BCI), p. 8 and Annex I (Overview of Conservative Assumptions), assumption (2). See also Andrew Chisholm, *An Introduction to Capital Markets* at 102 (2002) (Exhibit US-687) ("Normally the spread over Treasuries will increase with time to maturity. There is a higher risk that a corporate issuer will default over 10 years than over one year and investors will demand an increased risk premium.").

<sup>195</sup> See already U.S. SWS, para. 411, n.512. The EC, while relying on the cost of debt noted in this footnote (see EC Answers to Third Panel Questions, para. 160, n.186) conveniently fails to address this point in its response to Panel Question 271.

<sup>196</sup> See also comment to the EC response to Panel Question 272 below.

<sup>197</sup> U.S. SWS, para. 413.

<sup>198</sup> U.S. SWS, para. 411.

146. First, according to the EC, the lease of the EIG facilities “is effectively secured by the EIG equipment itself”.<sup>199</sup> This is quite a surprising statement as this is no different from any other lease. In fact, it is inherent in the very concept of a lease that the owner of the real estate or facilities subject to a lease agreement always retains ownership and is thus “secured” by the real estate and facilities owned by it when the lessee is no longer able to pay. In fact, this is not even a security for the lease at all, it is the simple consequence of ownership.

147. Second, the EC also argues that the EIG facilities lease is characterized by occupancy and default risks that are lower than those on “typical industrial real estate”.<sup>200</sup> This is not true; in fact, the risks are higher than for typical real estate. All of the infrastructure, real estate and facilities on the Aéroconstellation are tailor-made to Airbus’ and the aeronautics industry’s use;<sup>201</sup> Airbus is the predominant or exclusive user of most of the site;<sup>202</sup> and the use of the site is legally restricted to the aeronautics industry.<sup>203</sup> Thus, the EIG facilities are extremely specialized facilities for which there exists virtually no company other than Airbus that would be interested in leasing those facilities - or could lease the facilities which are located on a site the use of which is restricted by law (unlike in cases of “typical industrial real estate”). Rather than a low occupancy risk to the investor, as suggested by the EC,<sup>204</sup> the lease therefore carries a significant occupancy risk - which is even higher looking at the extremely long period needed for recoupment of the investment (at a very low rate of return): Even if Airbus France were a company with a low risk of default, the risk of default over a period of 40 years is always very high.

148. Third, the EC’s assertion that Airbus France enjoyed very good credit ratings<sup>205</sup> is equally flawed (regardless of the fact that, over 40 years, there is always a risk of default). The EC bases

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<sup>199</sup> EC Answers to Third Panel Questions, para. 159.

<sup>200</sup> EC Answers to Third Panel Questions, para. 159.

<sup>201</sup> U.S. FWS, paras. 458-462.

<sup>202</sup> U.S. FWS, paras 460-462: Most of the taxiways on the site exclusively connect Airbus’ assembly and testing facilities to the airport; the large space in front of Airbus’ production hall is used exclusively by Airbus as an A380 testing site; most of the roads on the site are for access to Airbus’ facilities, and most of the parking spaces will be used by Airbus and its suppliers’ employees, who will account for 70 percent of the employees on the site.

<sup>203</sup> U.S. FWS, para. 459; U.S. Answers to First Panel Questions, paras. 144-147.

<sup>204</sup> EC Answers to Third Panel Questions, para. 159.

<sup>205</sup> EC Answers to Third Panel Questions, para. 159.

this assertion on the company's credit ratings in 2007.<sup>206</sup> However, while EADS's credit rating may have been A1 in 2007, the company was rated only A2 in 2001 and was put on a negative credit watch to be downgraded even further to A3 in early 2002 (when the lease terms were negotiated and agreed).<sup>207</sup> This rating persisted until about 2 years past the start date of the EIG facilities lease.<sup>208</sup>

149. Finally, the EC argues that, in any event, "Airbus France would not agree to an investor return that exceeded its own borrowing cost (i.e., the cost of financing for the purchase of these assets)."<sup>209</sup> This assertion is clearly at odds with economic reality and disregards the fact that numerous elements go into a company's choice between leasing and purchasing property. In particular, companies regularly prefer lease constructions over purchases because it keeps the debt involved in purchases off their balance sheets. This may have been particularly relevant to Airbus which, at the time of the lease agreement, was in the early stages of development of the A380. The United States also recalls in that context that the lease was entered into as part of the same package as the AeroConstellation site purchase by Airbus and the other aeronautics companies using it.<sup>210</sup> It is not clear if Airbus was even given a choice to construct and/or purchase the EIG facilities itself. Indeed, the EC's assertion is difficult to reconcile with actual practice in the market where lease prices are frequently higher than purchases prices based on a company's cost of borrowing.

150. In sum, the EC has not been able to show any flaw in the methodology used by the United States to assessing the EIG lease agreement or in the benchmark initial net return determined and used by the United States. Thus, the United States maintains that Airbus receives a benefit of at least Euro 4 million to Euro 5.6 million per year from the EIG lease (and indeed, as explained before and reiterated in the US comment on the EC's response to Question 272, in fact much more). In any event, however, the United States notes that the EC has admitted that Airbus receives a benefit from the terms and conditions of the EIG lease agreement that is worth at least Euro 2.3 million per year.

**272. The United States asserts, at paragraph 413 and 414 of its SWS, that the lease price for the EIG facilities increases progressively, thus reducing the effective net initial return to**

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<sup>206</sup> EC Answers to Third Panel Questions, footnote 184.

<sup>207</sup> See Moody's screen-print (Exhibit US-688).

<sup>208</sup> *Id.*

<sup>209</sup> EC Answers to Panel Questions, para. 160.

<sup>210</sup> See EC FWS, n.726.

far below 3.9 percent, and that the lease price is not subject to [ ], remaining [ ] over the 40 year lease term. These two elements, the United States argues, demonstrate the non-commercial nature of the lease price. Could the EC please comment?

Comment:

151. The EC’s response to this question fails to refute the United States’ demonstration that the lease price for the EIG facilities is not a market price. The EC first criticizes the United States for suggesting that the lack of [ ] of the lease price or the progressive nature of repayment would be inherently non-commercial.<sup>211</sup> Such factors, according to the EC, “are only relevant to the extent that they affect the investor’s rate of return.”<sup>212</sup> But that is precisely the point that the United States made by noting that the progressive nature of repayments “further reduc{es} the effective net initial return to far below the 3.9 percent”.<sup>213</sup> Indeed, the fact that larger repayments occur later in time – i.e., the repayment stream is progressive – by definition reduces that effective return on the investment as compared to a constant repayment stream. Similarly, the absence of indexation – in other words, the fact that the lease price does not increase with inflation – has a direct effect on the investor’s rate of return.

152. The EC’s second point is equally unsupported. The EC characterizes as “incoherent” the fact that the United States has pointed out both the effects of the progressive nature of repayments and the lack of [ ] at the same time.<sup>214</sup> Contrary to the EC’s view, however, a progressive repayment structure and [ ] are two different things.

153. Thus, for example, the repayment terms of the EIG facilities lease are progressive: Grand Toulouse has determined an annual lease price based on the average annual repayment on a hypothetical loan carrying interest of 2.2 percent and 4.5 percent, respectively. It then went on to charge only [ ] of this average amount in 2007, with an increase to [ ] percent of the average 15 years later and to [ ] 25 years later.<sup>215</sup>

154. On the other hand, the lease price is not [ ], i.e., the lease price is not [ ]. The average annual lease price, as well as each individual lease price calculated

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<sup>211</sup> EC Answers to Third Panel Questions, para. 163.

<sup>212</sup> *Id.*

<sup>213</sup> U.S. SWS, para. 412.

<sup>214</sup> EC Answers to Third Panel Questions, para. 164.

<sup>215</sup> U.S. SWS, para. 413.

using the progression methodology, have been fixed in 2002 and 2004 (when the lease agreement was concluded). These amounts remain [ ] In contrast, if the lease price had been [ ]

[ ]. While an [ ] repayment stream will usually develop progressively over time (simply because in most years in most countries there will be some level of [ ]), [ ] can theoretically also lead to a [ ] in lease price (namely, when there is [ ]).

155. In other words, the United States argument is twofold (and not at all “incoherent”): (i) due to the time-value of money, the fact that larger lease payments are not made until later results in a lower rate of return for the investor/lessor; and (ii) the lease price is not [ ], *i.e.*, it does not [ ] which exposes the investor to the additional risk of further reducing his return because of [ ]. A [ ] lease price would typically demand a premium to compensate for this additional risk (in particular in light of the long term of the lease), but the 3.9% return that is achieved through the EIG lease does not include such a premium.

156. Third, the EC refers back to its argument that the lease is more properly considered “debt financing”, and argues that this “obviates the need for indexing”. The United States already explained that the lease cannot be characterized as “debt financing” simply because the lease term allegedly covers the entire life cycle of the EIG facilities. There are many reasons why a company may choose to enter into a lease agreement, rather than to use debt financing to purchase certain assets, even if the lease term is for the entire life of those assets.<sup>216</sup> The United States further notes that [ ] risk does not magically disappear when a lease is characterized as a loan. The reason that debt financing is not typically [ ] is that the rate of return already includes the monetary risk or opportunity cost element resulting from such [ ] risk. For example, the 6.83% average corporate borrowing rate for EADS that the EC refers to in its response to Question 271 already includes provision on the part of the lender for [ ] in the years leading up to full repayment. In other words, characterization of the lease as debt financing does not “obviate” the need for [ ]. It simply means that while [ ] is usually made explicit in lease contracts, it is usually implicit in debt financing. It also means, as explained above, that, in the case of a 40-year arrangement like the EIG facilities lease, such “implicit [ ]” would need to take account of the [ ] that comes with a longer term loan, *i.e.*, that the premium would be far higher than on the average borrowing of the company.

<sup>216</sup> See above at para. 140 (response to Question 271).

157. Finally, the United States observes that the Panel's question asks the EC to respond to two elements raised by the United States as evidencing the non-market-based nature of the lease price paid by Airbus. It is worth noting, however, that the benefit for Airbus under the terms of the EIG lease agreement stems not only from the progressive nature of the lease price and the lack of [ ] noted in the Panel's question. Airbus also benefits significantly from the fact that the calculation of the lease price undertaken by Grand Toulouse is based exclusively on the cost of creating the EIG facilities while ignoring the value of the land on which the facilities were built. In fact, Grand Toulouse provides the land to Airbus for free. If the value of the land is added to the lease price, a market-based landowner would have asked for an annual lease price of at least between Euro 9.9 million and Euro 12.1 million, instead of the Euro 3.2 million that Grand Toulouse in fact charges.<sup>217</sup> Viewed in this light, the true benefit Airbus receives by virtue of the EIG lease agreement by far exceeds the amount of Euro 4 million to Euro 5.6 million per year noted in the U.S. comment on the EC's response to Panel Question 271 above.<sup>218</sup>

**E. R&D AND TECHNOLOGY**

**273. Please provide corporate organizational charts depicting the wholly-owned subsidiaries, partially-owned subsidiaries and joint venture participations, held both directly and indirectly, for the following entities (and their successor entities, as applicable) between 1986 and 2001.**

- (i) Aérospatiale SNI**
- (ii) Aérospatiale Matra S.A.**
- (iii) MBB GmbH**
- (iv) Deutsche Aerospace AG**
- (v) CASA**
- (vi) British Aerospace PLC**
- (vii) BAe Systems PLC**

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<sup>217</sup> U.S. SWS, paras. 412 and 415.

<sup>218</sup> See US comments on EC Answers to Third Panel Questions, para. 141 (EC response to Question 271).

Comment:

158. See comment on EC response to Question 277 below.

**274. Please provide corporate organizational charts depicting the wholly-owned subsidiaries, partially-owned subsidiaries and joint venture participations, held both directly and indirectly, for EADS, N.V. for the period between 2000 and 2005.**

Comment:

159. See comment on EC response to Question 277 below.

**275. Please provide corporate organizational charts depicting the wholly-owned subsidiaries, partially-owned subsidiaries and joint venture participations, held both directly and indirectly, for the following entities between 2001 and 2005:**

- (i) **Airbus S.A.S.**
- (ii) **Airbus France SAS**
- (iii) **Airbus Deutschland GmbH**
- (iv) **Airbus Espana SL**
- (v) **Airbus UK Limited**

**In providing the above-referenced information, please ensure that the corporate name of each entity is correctly indicated.**

Comment:

160. See comment on EC response to Question 277 below.

***EC Framework Programmes***

**276. Please explain what the "Contract Nr" information disclosed in Exhibits EC-189, EC-190, EC-191, EC-192 and EC-193 means for each of the projects the EC alleges were financed under the Second, Third, Fourth, Fifth and Sixth Framework Programmes. Please explain the extent to which the funding provided under each of these contracts can**

be traced to one or more of the "specific programmes" referred to under each of the Second, Third, Fourth, Fifth and Sixth Framework Programmes.

Comment:

161. None.

277. Without prejudice to the Panel's view on the parties' interpretations of the relevant Airbus entities in this dispute, and in addition to the information already submitted, please provide:

- (a) In respect of the "Specific Activities Relating to Aeronautics" objective of the Industrial Manufacturing Technologies and Advanced Materials Applications programme implementing part of the Second Framework Programme –
  - (i) a break-down of all LCA-related projects in which the entities identified in response to Questions 273 to 275 participated;
  - (ii) the EC contribution to each project; and
  - (iii) the amounts received by each of those entities.
- (b) In respect of the "Aeronautics Research" objective of the Industrial and Materials Technologies programme implementing part of the Third Framework Programme –
  - (i) a break-down of all LCA-related projects in which the entities identified in response to Questions 273 to 275 participated;
  - (ii) the EC contribution to each project; and
  - (iii) the amounts received by each of those entities.
- (c) In respect of the "aeronautics sector" funding under the "Technologies for Transport Means" objective of the Industrial and Materials Technologies programme implementing part of the Fourth Framework Programme –
  - (i) a break-down of all LCA-related projects in which the entities identified in response to Questions 273 to 275 participated;

- (ii) the EC contribution to each project; and**
  - (iii) the amounts received by each of those entities.**
- (d) In respect of the "New Perspectives for Aeronautics" activity under the Competitive and Sustainable Growth programme implementing part of the Fifth Framework Programme –**
  - (i) a break-down of all LCA-related projects in which the entities identified in response to Questions 273 to 275 participated;**
  - (ii) the EC contribution to each project; and**
  - (iii) the amounts received by each of those entities.**
- (e) In respect of the "Aeronautics and Space" objective under the Integrating and Strengthening the European Research Area programme implementing part of the Sixth Framework Programme –**
  - (i) a break-down of all LCA-related projects in which the entities identified in response to Questions 273 to 275 participated;**
  - (ii) the EC contribution to each project; and**
  - (iii) the amounts received by each of those entities.**

Comment:

162. The United States submitted, as Exhibit US-485,<sup>219</sup> an overview of all known Airbus recipients of Framework Programme funding for which the amounts of such funding had not yet been disclosed by the EC. This exhibit is based in particular on Exhibits US-319, US-322 and US-324 that the United States submitted with its First Written Submission and that include overviews of aeronautics-related research projects funded by Framework Programmes and the participants in those projects. The publicly available information on which Exhibit US-485 is based, however, contains information only on the entities that received funding in respect of particular R&D projects, but does not contain a breakdown of the amounts of Framework funding provided to each of these entities. This was the reason the United States asked the

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<sup>219</sup> This exhibit was submitted in conjunction with the U.S. Answers to First Panel Questions, para. 217 (response to Question 34).

Facilitator to request this information from the EC and subsequently the Facilitator requested this information from the EC.<sup>220</sup>

163. The United States notes that, over the course of the Panel proceedings, the EC has steadily acknowledged more and more of the Framework Programme monies that were provided to Airbus entities.<sup>221</sup> Based on Exhibit EC-968 – EC-972, the EC has now provided information on at least [ ]<sup>222</sup> in Framework Program monies provided to Airbus entities. While this amount is already almost 25% larger than the amount the EC originally acknowledged,<sup>223</sup> there are still numerous clear gaps in the numbers that the EC is willing to disclose. These gaps can be established by simply comparing the overview in Exhibit US-485 to the information now disclosed by the EC. The results of this comparison, provided by the United States in Exhibit US-685 (HSBI), show that the EC has still not disclosed amounts of funding provided to several Airbus entities in 64 of 145 R&D projects funded through the Framework Programme.<sup>224</sup> In other words, almost half of the aeronautics project categories funded under the EC's Framework Programme involved the participation of Airbus entities, as to which the EC remains silent on monies provided them.

164. Thus, for example, the United States established that monies under the Third Framework Programme were provided to a research project named “Basic Research in Aircraft Interior Noise” or “BRAIN”. Based on public information, the United States has demonstrated that contributions went to Aerospatiale Division Avions, Deutsche Aerospace Airbus GmbH, and Construcciones Aeronauticas S.A.<sup>225</sup> These entities were specifically listed in Exhibit US-485 as

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<sup>220</sup> See U.S. FWS, paras. 629-630, 632-635, 637-640, 642-645, and 647-650 and the information from the Facilitator's Report cited there.

<sup>221</sup> In its First Written Submission, the EC referred to “payments to relevant companies” amounting to [ ] (EC First Written Submission (“FWS”), para. 1225). The EC at the same time acknowledged that if one included the Second and Third Framework Programs the amount would increase to [ ] (EC FWS, para. 1231), but then, in its response to First Panel Questions, para 299, backtracked again and explained that it considered the amount of [ ] billion included for the Second Framework Program not actually relevant.

<sup>222</sup> Euro [ ] to be precise. See Exhibits EC-968 (BCI) to EC-972 (BCI).

<sup>223</sup> Euro [ ] compared to Euro [ ] or [ ] (see footnote above.)

<sup>224</sup> Exhibit US-689 identifies, on a per project basis, the Airbus entities that the United States has demonstrated receive R&D subsidies from the EC and Member States, but as to which the EC, contrary to the Panel's request, continues to refuse to indicate funds provided under the Framework Programmes.

<sup>225</sup> See Exhibit US-485 and Exhibit US-318. See also Exhibit US-319, p. 3, which sets out in detail the participants in this research project.

recipients of monies under the Third Framework Programme for the “BRAIN” research project. Nevertheless, the overview provided by the EC shows amounts that went to Airbus Deutschland, Airbus France and Airbus UK, but does not contain any information on monies provided to Construcciones Aeronauticas S.A., nor any explanation for the absence of such information. Similarly, the entry on the EC’s overview for monies provided for the “Crashworthiness for Commercial Aircraft” study includes money provided to Airbus Deutschland, but not monies that according to public information were provided to BAe Airbus and Construcciones Aeronauticas S.A.<sup>226</sup> Numerous similar examples exist in the Third Framework Programme as well as each of the subsequent Framework Programmes.<sup>227</sup>

165. The United States reiterates that all of the entities on its list of R&D programmes and participants are Airbus entities, and all of the monies referred to were provided under the aeronautics budgets of the EC Framework Programmes which, by definition, relate directly to civil aeronautics research and development. The EC has failed to justify why it has refused to provide the evidence necessary to substantiate its claims of lower R&D funding levels. Therefore, the information submitted by the United States<sup>228</sup> provides the most reliable basis for the Panel to conduct its inquiry into R&D subsidies received by Airbus entities.

### *France*

**278. Without prejudice to the Panel's view on the parties' interpretations of the relevant Airbus entities in this dispute, and in addition to the information already submitted, please provide:**

- (i) a break-down of all LCA-related projects funded by the French government between 1986 and 1993 in which the entities identified in response to Questions 273 to 275 participated;**
- (ii) the French government's contribution to each project; and**

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<sup>226</sup> See Exhibit US-485. See also Exhibit US-319, p. 23, which sets out in detail the participants in this research project.

<sup>227</sup> As said, Exhibit US-485, submitted with U.S. Answers to the Panel’s Questions following the First Panel Hearing, contains an overview of projects and Airbus participants that the United States has been able to put together based on publicly available information. The United States submits as Exhibit US-685 (HSBI) a new overview showing the information that still appears to be missing. The United States also refers the Panel to its response to Question 34 in which the United States set out in more detail the types of information that appeared to be missing at the time of the Panel’s first questions and much of which is still missing despite the Panel’s requests.

<sup>228</sup> See U.S. FWS, paras. 621-703; U.S. SWS, paras. 487-519.

**(iii) the amounts received by each of those entities.**

Comment:

166. The United States identified Euro 391 million, on the basis of evidence before the Panel, as the amount of money budgeted by the French government for grants to the aeronautics industry for civil aeronautics research and development in the period 1986 to 1993.<sup>229</sup> This figure was based solely on publicly available evidence, because the EC refused to comply with the Annex V Facilitator's request for a full breakdown of the projects, amounts, and recipients of French civil aeronautics R&D grants provided between 1986 and 2005.<sup>230</sup> In the face of the EC's refusal to provide the requested information so as to allow for further detailed examination of R&D subsidies provided to Airbus by the French government in the period 1986 to 1993, the supporting documentation provided by the United States remains the most probative evidence before the Panel.

167. At no point in these proceedings has the EC sought to rebut the United States' evidence on this issue. Even when given yet another opportunity with this question, the EC again declined to provide the documentation necessary to do so. Instead, it surmises that the Euro 391 million figure substantiated by the United States is an overstatement on the basis of the proportion of R&D funds that the EC claims went to Airbus in the period 1994-2005.<sup>231</sup>

168. R&D funds provided to Airbus in 1994-2005 as a proportion of budgeted funds, however, has no probative value as to the amounts that went to Airbus in the period 1986-1993. Such an approach is based on a mere assumption that the ratio of disbursed funds to budgeted funds was the same in 1986-1993 as it is alleged to have been in 1994-2005. Such an assumption cannot substitute for evidence, evidence that one would expect to be exclusively within the control of the EC but that, according to the EC, it is "unable to obtain." Therefore, the 391 million figure substantiated by the United States reflects the best evidence available to it and, in the absence of verifiable evidence from the EC that responds to Panel's appropriate request for information, remains the only reliable data before the Panel on this issue.

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<sup>229</sup> See U.S. FWS, para. 678; French Government Funding for Civil Aeronautics Research and Development (yearly budgets) (Exhibit US-337).

<sup>230</sup> See *Replies to Questions by the Facilitator under Annex V of the SCM Agreement by the European Communities* at 186-192 (Nov. 18, 2005) (response to Questions 247 and 248) (Exhibit US-5 (BCI)).

<sup>231</sup> See EC Answers to Third Panel Questions, para. 178.

**279. Without prejudice to the Panel's view on the parties' interpretations of the relevant Airbus entities in this dispute, and in addition to the information already submitted, please provide:**

- (i) a break-down of all LCA-related projects funded by the French government between 1994 and 2005 in which the entities identified in response to Questions 273 to 275 participated;**
- (ii) the French government's contribution to each project; and**
- (iii) the amounts received by each of those entities.**

Comment:

169. See comment on EC response to Question 277 above.

### **III. QUESTIONS TO BOTH PARTIES**

#### **A. CAPITAL INVESTMENTS AND SHARE TRANSFERS**

**280. In *Japan - DRAMS*, the Panel considered (at para. 7.276) that the determination of the existence of benefit under Article 1.1(b) of the SCM Agreement might be based on, *inter alia*, evidence of whether or not a financial contribution was provided on the basis of "commercial considerations". Do the parties consider that the absence of independent financial analyses of a company's financial condition and prospects is evidence of "non-commercial considerations" sufficient to establish the existence of benefit? Please indicate how, if at all, the presence or absence of independent financial analyses should affect the Panel's assessment of any benefit conferred by the alleged German equity infusion into Deutsche Airbus and the alleged French equity infusions into Aérospatiale.**

Comment:

170. The EC's response to Question 280 repeats certain errors from the EC's response to Question 260. In particular, in both responses the EC confuses the respective burdens of the complaining party and defending party. In both responses the EC makes arguments about types of evidence that in theory might be brought to bear in demonstrating that a government investment is consistent with the usual investment practice of private investors but that the EC, in fact, has not brought to bear in this dispute. And, in both responses the EC makes the erroneous assertion that consistency of a government investment decision with the usual investment practice of private investors can be evaluated on the basis of information that merely existed at

the time of the investment, even if there is no evidence that the government actually relied on the information, as a private investor would have done. Given the repetition in the EC's responses, the United States refers the Panel to its comment on the EC's response to Question 260, above. The United States also makes the following additional observations, which are particular to the EC's response to Question 280.

171. First, the EC asserts without elaboration that the portion of the *Japan – DRAMs* panel report cited by the Panel “did not address the relevance, to an assessment of ‘benefit’, of the absence of independent financial analyses of a company’s financial condition and prospects.”<sup>232</sup> The EC ignores the context in which the excerpt cited by the Panel occurs. Indeed, the EC was careful to include the qualification “to an assessment of ‘benefit’” in its assertion (thus acknowledging that the panel did address the relevance of the absence of independent financial analyses in other parts of its report), although even that qualification is incorrect.

172. The excerpt from the *Japan – DRAMs* report cited by the Panel occurs in a section on the determination of the Japanese investigating authority (“JIA”) in a countervailing duty investigation that the participation in two restructurings of the Hynix company by certain Korean creditors conferred a benefit on Hynix.<sup>233</sup> That section is immediately preceded by an extensive review of the JIA’s determination that the creditors were entrusted or directed by the government of Korea to participate in the restructurings, thus making their participation a “financial contribution” within the meaning of Article 1.1(a)(1)(iv) of the SCM Agreement.<sup>234</sup> In the latter section, the panel upheld the JIA’s determination in part and rejected it in part, basing its conclusions largely on its assessment of the JIA’s intermediate determinations that various financial analyses did not properly establish the commercial reasonableness of the creditors’ participation in the restructurings. To the extent the panel upheld the JIA’s determination of entrustment or direction, it did so on the ground that the JIA did not err in finding that an absence of objective financial analyses meant that the creditors’ participation in one of the two restructurings was not based on “commercial reasonableness.”<sup>235</sup>

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<sup>232</sup> EC Answers to Third Panel Questions, para. 181.

<sup>233</sup> See *Japan – DRAMs (Panel)*, paras. 7.255-7.317.

<sup>234</sup> See *Japan – DRAMs (Panel)*, paras. 7.49 - 7.254.

<sup>235</sup> See *Japan – DRAMs (Panel)*, paras. 7.133-7.154. Likewise, to the extent the panel rejected the JIA’s determination of entrustment or direction with respect to the second restructuring, it did so on the ground that the JIA erred in finding that particular financial analyses were not objective or otherwise not credible such as to establish the commercial reasonableness of the creditors’ participation in the restructuring. See *id.*, paras. 7.155-7.245.

173. The panel then proceeded to its discussion of benefit, which included the passage cited in Question 280. As explained in the U.S. response to this question, the panel found “evidence of whether or not the financial contribution was provided on the basis of commercial considerations” to be sufficient to support the JIA’s conclusion that the financial contribution at issue conferred a benefit on the recipient.<sup>236</sup> The panel made a point of noting that where an investigating authority is presented with other evidence (such as “evidence of the terms that the market would have offered”) the authority would have to “weigh the probative value of one type of evidence against the probative value of the other.” But, where the investigating authority is not presented with such other evidence – as was the case in *Japan – DRAMs* and is the case in the present dispute – evidence that a financial contribution was provided on a basis other than commercial considerations suffices.<sup>237</sup>

174. The *Japan – DRAMs* panel’s findings regarding “commercial considerations” in its benefit discussion was directly linked to its findings regarding the absence of objective financial analyses and “commercial reasonableness” in its entrustment or direction discussion. The panel was explicit about this link in paragraph 7.281 of its report, stating:

The JIA concluded that the Four Creditors had failed to participate in the October 2001 restructuring on the basis of commercial considerations. We have rejected Korea’s arguments challenging that conclusion. Since we uphold the JIA’s finding that the October 2001 restructuring was not commercially reasonable, it follows that we also uphold the JIA’s determination that the October 2001 restructuring conferred a benefit on Hynix.<sup>238</sup>

175. Accordingly, while the *Japan – DRAMs* panel’s findings regarding the relevance of the absence of independent financial analyses were set out in its discussion of entrustment or direction, the panel explicitly incorporated them by reference into its discussion of benefit. The EC’s suggestion to the contrary is simply wrong.

176. The EC then compounds its error by suggesting that ascribing significance to an absence of independent financial analyses as evidence that a financial contribution was provided on the basis of non-commercial considerations would be contrary to the findings of the Appellate Body

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<sup>236</sup> See U.S. Answers to Third Panel Questions, para. 111 (citing *Japan – DRAMs (Panel)*, para. 7.276 and n.475).

<sup>237</sup> See *Japan – DRAMs (Panel)*, para. 7.276 and n.475.

<sup>238</sup> *Japan – DRAMs (Panel)*, para. 7.281 (emphasis added).

in its *Japan – DRAMs* report.<sup>239</sup> However, as the United States noted in its response to Question 280, the Appellate Body upheld the panel’s findings in this regard.<sup>240</sup>

177. The EC’s quotation from the *Japan – DRAMs* Appellate Body report comes from a section addressing an entirely different set of findings (pertaining to “calculation of the amount of benefit”).<sup>241</sup> There, the Appellate Body rejected the proposition that, for purposes of identifying a benchmark for a benefit analysis under Articles 1.1(b) and 14 of the SCM Agreement, there are distinct “inside investor” and “outside investor” standards. It found, as the EC quotes, “There is but one standard – the market standard – according to which rational investors act.”<sup>242</sup> The EC concludes from this statement that “placing presumptive weight on evidence of a government’s ‘considerations’, without considering evidence regarding consistency with market (*i.e.*, the usual investment practice of private investors) would effectively supplant the single, market standard.”<sup>243</sup>

178. In addition to ignoring the Appellate Body’s affirmance of the *Japan – DRAMs* panel’s finding regarding the probative value of “a government’s ‘considerations,’” this statement once again makes a theoretical point that is irrelevant given the evidence actually before the Panel in this dispute. The theoretical point concerns the relative weight to be given “evidence of a government’s ‘considerations’” as compared to “evidence regarding consistency with market.” The point is theoretical, because the EC has not provided the Panel with any “evidence regarding consistency with market” in connection with any of the equity infusions at issue.<sup>244</sup>

179. Finally, the EC’s reliance on the Appellate Body’s statement that, for purposes of a benefit analysis under Articles 1.1(b) and 14 of the SCM Agreement, there is one market standard and not separate “inside investor” and “outside investor” standards is curious given

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<sup>239</sup> See EC Answers to Third Panel Questions, para. 184 and n.202.

<sup>240</sup> See *Japan – DRAMs (AB)*, paras. 222, 226-229 (cited in U.S. Answers to Third Panel Questions, para. 111).

<sup>241</sup> See *Japan – DRAMs (AB)*, paras. 165-185.

<sup>242</sup> *Japan – DRAMs (AB)*, para. 172 (quoted in EC Answers to Third Panel Questions, para. 184).

<sup>243</sup> EC Answers to Third Panel Questions, para. 184.

<sup>244</sup> See U.S. Answers to Third Panel Questions, paras. 106-121 (response to Question 280); see also U.S. Comment on EC Answer to Question 260, *supra*.

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previous EC statements about the equity infusion claims in this dispute. In particular, the United States calls the Panel’s attention to the EC’s response to Question 224.<sup>245</sup>

180. The Panel had asked whether “the parties consider that the usual investment practice of private investors should be determined in light of the specific circumstances surrounding the government investment.” The EC responded that such circumstances “are indeed critical to the identification of the benchmark against which to assess whether a ‘benefit’ was conferred.”<sup>246</sup> It restated the relevant inquiry under Articles 1.1(b) and 14(a) of the SCM Agreement as “whether a private investor, standing in the government’s shoes, would have made the investment.”<sup>247</sup> As an example, referring to part (a) of the Panel’s question, the EC noted that “{p}rivate investor ‘practice’ will differ depending on such factors as: whether the investment target is insolvent and the private investor is an existing creditor.”<sup>248</sup> Similarly, in the case of the French government’s 1987-to-1993 infusions to Aérospatiale, the EC suggests that it is relevant to a benefit analysis that “in a situation of {a} company with a single shareholder, the shareholder is inevitably bound to be closely informed about the management’s analysis of the prospects and needs of the company.”<sup>249</sup>

181. In sum, although the EC now acknowledges that “{t}here is but one standard – the market standard,” it previously has urged the Panel to examine the equity infusions in dispute from what amounts to an “inside investor” perspective. The United States is pleased that the EC now disavows a separate “inside investor” standard. As the parties are in agreement on this point, and as the Appellate Body has also found that there is a single “market standard,” the United States requests that the Panel analyze the equity infusions according to that standard. For the reasons set forth in this and previous U.S. submissions, doing so will lead to the conclusion that each equity infusion confers a benefit on Airbus.

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<sup>245</sup> See EC Answers to Second Panel Questions, paras. 565-570.

<sup>246</sup> EC Answers to Second Panel Questions, para. 566.

<sup>247</sup> EC Answers to Second Panel Questions, para. 566 (emphasis added).

<sup>248</sup> EC Answers to Second Panel Questions, para. 567.

<sup>249</sup> EC SWS, para. 546; *see also* U.S. Answers to First Panel Questions, paras. 183-184 (discussing EC’s misplaced focus on the perspective of management in contending that investment decisions were consistent with the usual investment practice of private investors); U.S. SWS, paras. 472-474 (same).

**B. ADVERSE EFFECTS**

**281. Neither party has presented or relied upon either list prices, or actual transaction prices, for LCA, in the context of arguments relating to price suppression, price depression, price undercutting, or lost sales, with respect to injury under Article 5(a), or serious prejudice under Article 6(3)(c). Could the parties explain the reason for the lack of such information - is it their view that such information is unreliable, not probative, not meaningful, or unavailable?**

Comment:

182. As the United States explained in its response to this question, the United States has provided relevant evidence of price suppression, price depression, price undercutting, and lost sales with respect to claims of material injury under Article 5(a) and serious prejudice under Articles 5(c) and 6.3(c). This relevant evidence does not include list prices or actual transaction prices, for the reasons previously given.<sup>250</sup>

183. The EC agrees that list prices in this industry generally do not provide relevant information for these purposes.<sup>251</sup> Nor does the EC contend that actual transaction prices, as such, are necessarily required to sustain a claim of price suppression, price depression, price undercutting, or lost sales. Rather, the EC asserts that, “in light of the way the United States has structured its claims,” evidence of actual transaction prices is necessary.<sup>252</sup> The EC develops this assertion through the same mischaracterizations of the U.S. adverse effects case that it has repeatedly advanced, and to which the United States has repeatedly responded. We address three of these mischaracterizations below.

184. First, the EC contention that “alleged price undercutting by Airbus is an essential element of all forms of adverse effects claimed by the United States”<sup>253</sup> is plainly incorrect. With regard to claims of displacement or impedance of imports and exports under Article 6.3(a)-(b), the United States relies primarily on the dramatic increase in Airbus’s market share – at the expense of Boeing’s market share – in the relevant markets. This claim is independent of any price undercutting. With regard to price suppression and price depression under Article 6.3(c), the

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<sup>250</sup> U.S. Answers to Third Panel Questions, paras. 122-130.

<sup>251</sup> EC Answers to Third Panel Questions, para. 191.

<sup>252</sup> EC Answers to Third Panel Questions, para. 190.

<sup>253</sup> EC Answers to Third Panel Questions, para. 193.

United States relies primarily on the trends in average prices for various U.S. LCA models, not prices in particular transactions.

185. The United States establishes price undercutting under Article 6.3(c), by contrast, with reference to the available evidence of price undercutting in particular transactions.<sup>254</sup> It is also true that the evidence demonstrates that price undercutting was a central factor in many, if not all, of the transactions that the United States has alleged as lost sales. However, lost sales also occur when subsidies enable Airbus to introduce particular LCA models to compete with particular Boeing LCA models at a certain time.<sup>255</sup> It is also true that pricing pressure from Airbus, including but not limited to price undercutting in the particular sales campaigns identified by the United States, has contributed to the decline in average prices received by Boeing for several LCA models and to the loss of Boeing market share to Airbus in various markets. However, this is not the only way that the subsidies have caused displacement or impedance of imports and exports, price suppression, or price depression. The existence and timing of Airbus launch decisions, as well as the additional pricing flexibility provided by Launch Aid at a more general level, also play a significant role in causing these forms of serious prejudice.<sup>256</sup> These claims are independent of the U.S. price undercutting claim and are in no way dependent upon it.

186. Second, the EC quotes with seeming approval an argument made in the U.S. first written submission:

When the evidence establishes that, in a particular LCA transaction, a customer concludes that Airbus, all other things being equal, offered a lower price than Boeing, the evidence constitutes *prima facie* evidence of price undercutting within the meaning of Article 6.5 and, therefore, of Article 6.3(c).<sup>257</sup>

According to the EC, if the “all other things being equal” condition is met, this U.S. statement is “accurate.”<sup>258</sup> In itself, this is an admission that the question is whether the evidence does, in fact, establish that Airbus offered a lower price, “all other things being equal,” and not whether a particular type of evidence – such as actual transaction prices – has been provided. The EC

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<sup>254</sup> This evidence was summarized in response to Question 236. U.S. Answers to Third Panel Questions, paras. 65-73.

<sup>255</sup> U.S. SWS, paras. 715-722.

<sup>256</sup> *E.g.*, U.S. Answers to Third Panel Questions, paras. 31-37.

<sup>257</sup> U.S. FWS, para. 800, quoted (with ellipses) in EC Answers to Third Panel Questions, para. 200.

<sup>258</sup> EC Answers to Third Panel Questions, para. 200.

suggests, however, that the United States “assumes away all complexities of LCA sales transactions” in its price undercutting allegations and thus fails to ensure that, in fact “all other things {are} equal.”<sup>259</sup>

187. However, as the United States has explained in considerable detail, the evidence of price undercutting provided in this case does take into account the great complexity of LCA sales transactions.<sup>260</sup> It is this very complexity that would make it impracticable for the Panel to base an assessment of price under cutting on its own comparison of actual transaction prices taken in isolation. Only the customer has actual knowledge of the offers of both Airbus and Boeing as well as all of the other factors it considers necessary to evaluate the relative pricing of the competing aircraft. In every case, the evidence provided by the United States is based on the customer’s assessment of all of these factors.

188. The example provided by the EC is a good illustration of this point. The EC hypothesizes that, if Airbus offers a 150-seat LCA for \$50 million and Boeing offers a 162-seat LCA for \$51 million, it may appear that Airbus is offering the lower price – but, in fact, on a per-seat basis, Boeing is probably offering “the better deal.”<sup>261</sup> The United States agrees. But this difference – and many other, far more technical and complicated differences – between Boeing and Airbus offers in any given transaction are precisely what customers take into account in evaluating offers.

189. So, when easyJet announced its order of 120 A319s in competition with the Boeing 737-700, stating that the Airbus price was so much lower than the Boeing price that “we would have been in breach of our fiduciary duty; it would have been an offence to buy Boeing,”<sup>262</sup> it is reasonable to assume that easyJet was aware of the difference in seating capacity – and other, far more complex differences – between the Airbus A319 and the Boeing 737-700 when it made its price evaluation. One would expect a customer to be aware of such matters when making a multi-billion dollar purchase of its most important business assets. In the particular case of easyJet, information before the Panel already establishes that, as a factual matter, easyJet was aware of and took account of all the differences, including differences in seating capacity, between the A319 and the 737-700 in evaluating the competing offers:

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<sup>259</sup> EC Answers to Third Panel Questions, para. 200.

<sup>260</sup> U.S. Answers to Third Panel Questions, paras. 125-133.

<sup>261</sup> EC Answers to Third Panel Questions, para. 199.

<sup>262</sup> easyJet chairman Stelios Haji-Ioannou, quoted in Kevin Done, *Airbus Beats Boeing in War over Big Order*, Fin. Times (Oct. 15, 2002) (Exhibit US-407).

Airbus has agreed to provide easyJet with A319 aircraft in a single class configuration with 156 seats which compares with the 149 seats of the Boeing 737-700 aircraft presently operated by easyJet. ... The Company believes it can now purchase Airbus A319 aircraft under the Airbus Contract (taking into account these substantial price concessions) at a price approximately a third per seat below the price for the Boeing 737-700 aircraft delivered to it under the Boeing Contract ....<sup>263</sup>

Based on this and other considerations, easyJet concluded that “the offer from Airbus was significantly better value than the offer received from Boeing.”<sup>264</sup>

190. In the case of easyJet, it happens to be the case that the customer not only stated publicly that the Airbus price, all factors considered, was lower than the Boeing price, but also stated publicly that it took the price per seat into consideration. However, even when a customer does not make particular public statements with respect to the factors it considered in its price comparison, the evident importance of such factors to the customer’s evaluation allows the Panel to conclude that, in each of the transactions identified by the United States, when a customer indicates its decision to purchase Airbus LCA was driven by Airbus’s pricing relative to that of Boeing, it has accounted for all relevant factors affecting comparability in making its purchase decision.

191. Article 6.5 provides that price undercutting “includes” a case in which price undercutting is demonstrated by comparing prices for the subsidized product and prices of the like product in the same market, at the same level of trade, and at comparable times, “due account being taken of any other factor affecting price comparability.” As the United States has explained, the evidence of price undercutting before the Panel in this dispute meets this standard.<sup>265</sup> The EC incorrectly states that Article 6.5 “directs that, in conducting a price undercutting investigation, the Panel must compare the price of the Airbus and Boeing offers, ‘due account being taken of any other factor affecting price comparability.’”<sup>266</sup> The EC is wrong, not simply because the Panel is not conducting an “investigation” of price undercutting, but because Article 6.5 only requires that due account be taken of factors affecting price comparability. It does not specify any particular way in which due account of these factors is to be taken, or who must do the arithmetic. In some

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<sup>263</sup> easyJet, *Proposed Purchase of Airbus Aircraft and Notice of Extraordinary General Meeting* (Feb. 25, 2003) at 2, [http://www.easyjet.com/EN/News/20030225\\_01.html](http://www.easyjet.com/EN/News/20030225_01.html) (Exhibit US-380).

<sup>264</sup> easyJet, *Proposed Purchase of Airbus Aircraft and Notice of Extraordinary General Meeting* (Feb. 25, 2003) at 4, [http://www.easyjet.com/EN/News/20030225\\_01.html](http://www.easyjet.com/EN/News/20030225_01.html) (Exhibit US-380).

<sup>265</sup> U.S. Answers to Third Panel Questions, paras. 60-64.

<sup>266</sup> EC Answers to Third Panel Questions, paa. 197.

cases – the panel report in *Indonesia – Autos*, previously addressed by the United States, would be one example<sup>267</sup> – the evidence consists of raw data, and a panel may find it necessary to adjust the data in order to take due account of certain factors affecting comparability. In other cases, such as the present dispute, the evidence already takes due account of these factors, and it is neither feasible nor necessary for the Panel to work its way through the specifics of the competing offers and confirm the customer’s judgment about price relative to value in order to conclude that the evidence supports the U.S. claim of price undercutting.

192. The EC’s third misstatement is its contention that the United States must demonstrate that any price undercutting is the direct result of the Launch Aid provided for the development of the particular Airbus model at issue. Thus, for example, the EC states that the United States can demonstrate that the price undercutting demonstrated by evidence in the 2004 AirAsia sales campaign is the effect of the subsidy only if it can prove that the residual benefit from Launch Aid for the A320, conceived as a lump sum grant provided to Airbus in 1984, caused Airbus’s prices to be significantly lower.<sup>268</sup> The EC provides no basis for this assertion, and the United States has not argued that the effect of the subsidy operates in the manner that the EC suggests.<sup>269</sup>

193. To the contrary, the evidence shows that the nature, and accordingly the effects, of Launch Aid differ greatly from the nature and effects of grants that do not “create supply, maintain uneconomic supply or are tied to the production or sale of a particular aircraft model.”<sup>270</sup> The United States has demonstrated that the nature of Launch Aid is precisely to create supply, maintain uneconomic supply, and to impact the marginal cost and revenue of particular aircraft sales.<sup>271</sup> The United States is not required – as the EC repeatedly asserts but never demonstrates – to prove that Launch Aid has the effects of subsidies with a very different nature and impact on the market.

**282. Both parties appear to acknowledge that customers monetize the specific attributes of different models of LCA they are considering for purchase. Is there any generally applicable basis upon which this calculation is made? Could the parties comment on how**

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<sup>267</sup> U.S. Answers to Third Panel Questions, paras. 63-64.

<sup>268</sup> EC Answers to Third Panel Questions, para. 202.

<sup>269</sup> See, e.g., U.S. SNCOS, paras. 173-175.

<sup>270</sup> Statement of Professors Joseph E. Stiglitz and Bruce C. Greenwald, *On the Question of the Impact of Subsidies on Supply and Prices in the LCA Market* (Jan. 21, 2008) at 1 (Exhibit US-676).

<sup>271</sup> E.g., U.S. Answers to Third Panel Questions, paras. 30-37 (summarizing evidence).

**this practice can be taken into account in assessing the information presented regarding price suppression, price depression, underselling, and lost sales?**

Comment:

194. The EC and the United States do not appear to differ in their understanding of how LCA customers quantify the attributes of different LCA models in evaluating competing sale offers.<sup>272</sup>

195. The EC further asserts that certain intangible factors, such as “chemistry between the parties,” “intuition,” and “unquantifiable judgments” also may affect certain sales.<sup>273</sup> The EC has not, however, demonstrated that such factors have broken the causal link between subsidies and their demonstrated effects in the LCA market. In particular, as the United States has shown, the alleged “arrogance” of Boeing cited by certain customers as a factor in certain sales amounts largely to Boeing’s unwillingness to decrease its prices in the face of price undercutting from Airbus.<sup>274</sup>

**283. Could the parties please address the discrepancy between the production data reported by the United States in Table 4, at paragraph 746 of its first written submission, and that reported by the EC at paragraph 2162, of its first written submission, in the table entitled "Trends in Boeing's LCA Operations"?**

Comment:

196. The United States has already explained the apparent cause of the discrepancy.<sup>275</sup> In any event, as both the United States and the EC note, the difference does not affect the results of the material injury analysis.<sup>276</sup>

**284. Could the parties please comment on the proposition that, in a duopoly market, subsidized imports will always cause material injury to the domestic industry producing the like product in the importing country, because in the absence of such imports, the**

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<sup>272</sup> EC Answers to Third Panel Questions, para. 205; U.S. Answers to Third Panel Questions, paras. 64, 124-128, 131-133.

<sup>273</sup> EC Answers to Third Panel Questions, paras. 206-207.

<sup>274</sup> *E.g.*, U.S. SWS, para. 709.

<sup>275</sup> U.S. Answers to Third Panel Questions, paras. 134-135.

<sup>276</sup> EC Answers to Third Panel Questions, para. 212; U.S. Answers to Third Panel Questions, para. 135.

**domestic industry would capture the entire market, thereby earning more revenue? In what circumstances might this not be the case?**

Comment:

197. The United States and the EC appear to agree, albeit for somewhat different reasons, that the SCM Agreement does not permit the conclusion that subsidized imports “always” cause material injury in a duopoly industry. No single factor, taken in isolation, can necessarily be decisive in a material injury analysis; rather the question of whether subsidized imports have caused material injury has to be established “on the facts” of a given case.<sup>277</sup>

198. The EC goes on to assert at some length that, in a duopoly market, competition between the producers is beneficial to both producers and to consumers.<sup>278</sup> Thus, according to the EC, the existence of competition – even subsidized competition – from Airbus cannot cause injury to Boeing. However, the data clearly show that subsidized competition from Airbus has not been good for Boeing, by all of the measurements prescribed by Article 15.4 of the SCM Agreement.

199. Moreover, as the United States has observed, at the time the Airbus governments provided the Launch Aid and other subsidies without which Airbus could not have launched the A300, A310, A320, A330, or A340, Boeing did not have a monopoly in the LCA industry. Rather, there was another U.S. LCA producer, McDonnell Douglas.<sup>279</sup> Thus, one cannot assume – as the EC does – that the use of subsidies to create Airbus was somehow necessary in order for Boeing to enjoy the benefits of market competition, and thus was ultimately a good thing for the U.S. LCA industry. In this dispute, the United States claims adverse effects to the interests of the United States, not to the interests of Boeing.

200. Finally, the EC repeats its prior arguments that a claim of material injury under Article 5(a) of the SCM Agreement requires a showing both that subsidized imports have caused material injury within the meaning of Article 15 and that such material injury is the “effect of the subsidy” itself.<sup>280</sup> The United States has already responded to this argument by the EC, and

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<sup>277</sup> EC Answers to Third Panel Questions, para. 217.

<sup>278</sup> EC Answers to Third Panel Questions, paras. 219-223. The United States fails to see how any alleged benefit that access to subsidized imports may provide to consumers is relevant to the analysis of whether the domestic industry producing like products is materially injured, and will not discuss that aspect of the EC answers further.

<sup>279</sup> U.S. FNCOS, paras. 147-151.

<sup>280</sup> EC Answers to Third Panel Questions, paras. 227-233.

refers the Panel to that response.<sup>281</sup> As the EC points out, the Appellate Body recently observed that an investigating authority in a countervailing duty context applying the material injury standard in Article 15 is not required to find that material injury is the “effect of the subsidy,” in the sense in which that term is used in the context of serious prejudice in Article 6.3, but only that material injury was caused by the subsidized imports.<sup>282</sup> However, it does not follow from the Appellate Body’s reasoning that the Article 6.3 standard must be taken into account in a claim of material injury under Article 5(a).

**285. Assuming that "the degree to which a market is limited by geography will depend on the product itself and its ability to be traded across distances", what are the relevant criteria for delimiting specific geographic markets for LCA for purposes of Article 6.3(c)? Do the parties consider it possible that, given that LCA are sold throughout the world under similar conditions of competition, there is in fact only one geographic market for LCA, namely, the world market? What would be the implications of such a conclusion for the parties' arguments and the Panel's analysis of both injury and serious prejudice in this dispute?**

Comment:

201. The parties appear to agree that there is a world market for LCA and that the U.S. claims of significant price undercutting, lost sales, price suppression, and price depression should be assessed with regard to a world market. Further, the parties appear to agree that Article 6.3(a)-(b) places certain geographical limits on the relevant markets for those claims, and that a material injury analysis under Article 5(a) focuses on the impact of subsidized imports in the U.S. market.<sup>283</sup>

202. However, the United States does not agree that there are several world LCA markets distinguished by LCA size. The Panel is familiar with the U.S. argument on this point, and we will not repeat it here. The United States also does not agree that displacement or impedance of imports or exports can only be shown by identifying particular lost sales in particular country markets.<sup>284</sup> Nothing in the SCM Agreement imposes such a requirement, and the EC refers to none.

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<sup>281</sup> U.S. SWS, paras. 739-742.

<sup>282</sup> EC Answers to Third Panel Questions (citing *Japan – DRAMS (AB)*, para. 272).

<sup>283</sup> U.S. Answers to Third Panel Questions, paras. 138-141; EC Answers to Third Panel Questions, paras. 234-235, 238, 240.

<sup>284</sup> EC Answers to Third Panel Questions, para. 239.

**286. If the Panel were to consider that 2001-2003 represented a "down" portion of the LCA business cycle, do the parties consider that the Panel would be in error if it examined the effects of the alleged subsidies over the period 2001 through 2006 in order to determine whether the alleged subsidies cause adverse effects to the interests of the United States? If the Panel were to undertake such an analysis, how should data for the "down" period 2001 through 2003 be assessed so as to account for dissimilar conditions in the market over the entire period.**

Comment:

203. The EC repeats at great length arguments that it has made several times before about the alleged irrelevance of the 2001-2003 period to a determination of “present” serious prejudice. The United States has already responded to and refuted each of these arguments. As there is nothing new in the EC’s latest version of its arguments, the United States will not repeat those refutations here.

204. The EC seeks to exclude any consideration of data from 2001-2003 on the basis of a single factor affecting competition – the level of demand – but ignores that the key conditions of competition that drive the economics of large civil aircraft production (heavy upfront development costs with a return over decades; the multi-year process of large civil aircraft development; etc.) and sales (long-term contracts frequently worth billions of dollars that involve deliveries over many years, switching costs, the factors that go into an airline's assessment of the net present value of Boeing and Airbus offers; the importance of price; etc.) were the same in 2004 and afterwards as they were in 2001-2003. In doing so, the EC would divert attention from fundamental facts demonstrating serious prejudice: that Airbus dramatically increased its share of all relevant markets from 2001 to 2003 and has maintained that increased share since then, that Boeing LCA prices [

], and that the sales Boeing has lost to Airbus since 2001 continue to significantly shape the LCA market.

205. If the decrease in demand in 2001-2003 were the cause of the serious prejudice to Boeing, the unprecedented recovery of demand that began in 2004 would have eliminated that serious prejudice. Boeing’s market share and delivery levels would have recovered; Boeing’s pricing levels would have recovered; Boeing would have recaptured key customers lost during the downturn and afterwards. None of these things have occurred. Thus, the serious prejudice triggered by the subsidized actions of Airbus, including actions in 2001-2003, continue in the present.

**287. What sort of temporal correlation between the level of subsidization and the adverse effects of such subsidization is to be expected in an industry such as the LCA industry, with long lead times for product development, sometimes significant intervals between orders and deliveries, and sometimes significant re-pricing during those intervals? Is the answer the same with respect to both injury to a domestic industry under Article 5(a) and serious prejudice under Article 5(c)?**

Comment:

206. The EC acknowledges that the relevance of a “temporal correlation between subsidies and adverse effects is necessarily fact-specific.”<sup>285</sup> The United States agrees, and has explained in its own response to this question the temporal correlation that would be expected, and in fact exists, between a subsidy with the nature of Launch Aid and the adverse effects in this dispute.<sup>286</sup>

207. As noted above in the U.S. comments on the EC’s answer to Question 281, the EC’s caricature of what it calls the U.S. “cash flow causation” argument bears no resemblance to the U.S. demonstration of how subsidies affect Airbus pricing. The EC analysis is based on the suppositions that (1) Launch Aid is in the nature of a grant that provides additional cash to the recipient at the time of launch but has no other effects on the supply or production of particular LCA products, and (2) the only effect of such a grant is to allow the recipient to “spend” the subsidy by “pricing down” the LCA model for which the grant was given.<sup>287</sup> Plainly, this is not the nature or effect of Launch Aid as shown by the United States, and therefore the type of temporal correlation that the EC forecasts for such a subsidy has no relevance for this dispute.

208. With regard to what the EC calls the U.S. “historical causation argument” – the impact of Launch Aid on the launch decisions, and therefore on the product offerings that Airbus sells in competition with Boeing – the EC simply repeats its assertion that the subsidies were provided too long ago to have present impact and states that, given the passage of time, these launches can no longer provide “any present performance advantages.”<sup>288</sup> The United States has already addressed these arguments.<sup>289</sup> In particular, the distortion caused by Launch Aid is not to give Airbus LCA particular “performance advantages” that last only until Boeing invests its own

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<sup>285</sup> EC Answers to Third Panel Questions, para. 257.

<sup>286</sup> U.S. Answers to Third Panel Questions, paras. 148-150.

<sup>287</sup> EC Answers to Third Panel Questions, paras. 259-261.

<sup>288</sup> EC Answers to Third Panel Questions, para. 267.

<sup>289</sup> U.S. SWS, paras. 584-587.

capital to develop a competing performance characteristic on its LCA. Instead, the distortion caused by Launch Aid is to create LCA supply that otherwise would not exist.

209. As the EC response is premised on false assumptions about the nature and effects of Launch Aid, it does not detract from or undermine the U.S. response in any way.

**288. What is the appropriate methodology for this Panel to adopt in determining whether the effect of the subsidy is significant price suppression, significant lost sales, or displacement or impedance of imports and exports under Article 6.3, in light of the Appellate Body's statement in *US – Upland Cotton*<sup>290</sup> that it is necessary to ensure that the effects of other factors on prices (in the context of a significant price suppression claim) are not improperly attributed to the challenged subsidies?**

- (a) (to the United States) Does the United States consider that the other factors cited by the European Communities in this context are not relevant to the non-attribution analysis to be conducted by the Panel in a serious prejudice claim under Articles 5(c) and 6.3?**

Comment:

210. The EC's response to this question does not propose a methodology for ensuring non-attribution of adverse effects caused by factors other than the subsidy. Instead, the EC mostly repeats the alleged other factors that it contends explain the adverse effects experienced by the United States. The U.S. answers make clear that the United States has already shown that all of these alleged other factors have, in fact, not caused any of the adverse effects on which the U.S. case is based. These answers also explain that the United States has ensured that any market impact that resulted from changes in the overall level of demand have not been attributed to the effects of the subsidy by focusing on relative, rather than absolute, changes in sales volumes.

211. The EC makes two new assertions of alleged other causes in its response. Neither has merit.

212. First, with regard to price suppression and price depression, the EC claims that reduced demand explains the drop in prices from 2001 to 2003, while Boeing itself is responsible for the [ ].<sup>291</sup> The EC's argument is contradicted by the evidence of what actually occurred: Boeing lost sales and market shares to

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<sup>290</sup> *US – Cotton Subsidies (AB)*, para. 437.

<sup>291</sup> EC Answers to Third Panel Questions, para. 281.

Airbus because Airbus lowered its prices to maintain its production levels and gain market share during the 2001-2003 downturn. As Mr. Scherer of Airbus explained at the second Panel meeting, Airbus was “sustaining a fairly stable level of output, contrary to our competitor who, well, the term may be slightly exaggerated, but fell off a cliff.”<sup>292</sup> Mr. Scherer also explained that Boeing reduced prices in 2004 as a direct response to this loss of market share overall as well as several major key lost sales campaigns.<sup>293</sup> It is clear that this significant decline was not a spontaneous, inexplicable decision on Boeing’s part to voluntarily reduce its prices – rather, it was a response to the effect that Airbus’s pricing actions had in the market.

213. That the pricing behavior of Airbus – not lower demand in the 2001-2003 period – caused LCA prices to decrease over the full reference period is clear because, notwithstanding record demand from 2005 onwards, [ ]. The change in LCA pricing levels may have been to the short-term benefit of Airbus, as Mr. Scherer asserted to the Panel,<sup>294</sup> but it has led to long-term, enduring losses of market share and long-term, [ ] LCA price declines for Boeing. Further, as the United States has shown, Airbus’s ability to adopt this pricing strategy is directly related to Launch Aid and other subsidies.<sup>295</sup>

214. Second, the EC asserts that price declines for the 767 and 747 during the reference period reflect the fact that these aircraft models had reached the end of their product cycle during this period, and are not caused by competition from Airbus.<sup>296</sup> However, [

[ ]. Specifically, from 2001 to 2006, when adjusted for the producer price index, Boeing LCA prices fell by [ ].<sup>297</sup> If the price decline for the 747 and 767 is caused, as the EC now suggests, by the alleged obsolescence of these models, why did prices for the [ ]?

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<sup>292</sup> EC FNCOS, para. 325 (revised version Dec. 7, 2007).

<sup>293</sup> EC FNCOS, paras. 325-326 (revised version Dec. 7, 2007).

<sup>294</sup> EC FNCOS, para. 325 (revised version Dec. 7, 2007).

<sup>295</sup> E.g., U.S. Answers to Third Panel Questions, paras. 24-28.

<sup>296</sup> EC Answers to Third Panel Questions, para. 281.

<sup>297</sup> U.S. SWS, para. 726.

215. Moreover, Boeing has not discontinued the 747, but in fact launched the revised 747-8 derivative in 2006. Orders for the 747-8 are included in the Boeing pricing trends data for the 747. Nor has Boeing discontinued the 767, which it continues to offer in both passenger and freighter versions. Although the 767 should be able to enjoy a long commercial life as a freighter, even as the 787 supersedes the passenger version of the 767, Airbus launched a freighter version of the A330-200 in 2007. The EC's newest alternative other causal factor therefore also fails to explain the adverse effects that have occurred.

**289. In which circumstances, if any, would it be reasonable to conclude that a subsidy that has the indirect effect of lowering a firm's costs of production will result in that firm lowering its prices?**

Comment:

216. The EC, like the United States, recognizes that LCA prices “are determined by supply and demand.”<sup>298</sup> Thus, as the statement of Professors Stiglitz and Greenwald makes clear, “subsidies that create supply, maintain uneconomic supply or are tied to the production or sale of a particular aircraft model” – in other words, subsidies that have a direct impact on supply, demand, or both – are likely to have effects on LCA prices, while subsidies that do not have any of these effects are far less likely to affect LCA prices.<sup>299</sup> That Launch Aid has this nature has already been demonstrated.<sup>300</sup>

217. The United States also identifies in the HSBI Appendix to this submission certain evidence in the business cases provided by the EC in response to Question 262 that confirms some of the ways in which Launch Aid affects LCA pricing.

218. In its response, the EC proposes an analytical framework for evaluating whether subsidies are likely to have current effects on LCA prices – whether the subsidies give the recipient the ability to lower prices, whether the recipient has the incentive to lower prices, and whether the recipient has the opportunity to lower prices. Nothing in the SCM Agreement requires this – or any other – particular analytical approach to demonstrating causation, and the EC offers no basis other than its own unsupported assertions for the usefulness of its proposed framework in analyzing causation in this dispute.

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<sup>298</sup> EC Answers to Third Panel Questions, para. 291.

<sup>299</sup> Statement of Professors Joseph E. Stiglitz and Bruce C. Greenwald, *On the Question of the Impact of Subsidies on Supply and Prices in the LCA Market* (Jan. 21, 2008) at 1 (Exhibit US-676).

<sup>300</sup> U.S. Answers to Third Panel Questions, paras. 30-36.

219. Moreover, the EC's application of its framework is incorrect. Even assuming *arguendo* that the EC's framework has any relevance, the evidence demonstrates that Launch Aid does give Airbus the ability, incentive, and opportunity to lower prices.

220. There is no question that Launch Aid has given Airbus the ability to sell and price aircraft in a way that would otherwise have been impossible. The EC does not dispute that Airbus would not have launched any of its basic models prior to the A380 (A300, A310, A320, A330, or A340) without Launch Aid. As Professors Stiglitz and Greenwald explain, in this circumstance Launch Aid “reduces the marginal cost of supply from an essentially prohibitive level (without the start-up development, no planes could be produced) to a potentially competitive level.”<sup>301</sup> This is confirmed by the NERA estimate of the current magnitude of the additional debt burden that Airbus would have to bear had it obtained Launch Aid at commercial rates, which is so large as to demonstrate that it would not have been economically feasible to launch these aircraft without subsidies.<sup>302</sup> The evidence also demonstrates that, in addition to its impact on Airbus's launch decisions, Launch Aid also provided Airbus with financial flexibility that gives it the ability to price differently.<sup>303</sup>

221. The EC asserts that the magnitude of the subsidy during the relevant period is too small to give Airbus any significant ability to affect pricing.<sup>304</sup> To demonstrate the error in this statement, we compare the benefit from Launch Aid provided for just one Airbus model – the original A330/A340 – to the profits reported by EADS. EADS provides public financial statements from 1997 forward on its web site. According to these statements, the aggregate pre-tax profit earned by EADS from 1997 to the third quarter of 2007 (the most recent data available) is 4.5 billion Euro.<sup>305</sup>

222. To show the benefit from A330/A340 Launch Aid over this period, we examine the A330/A340 repayments contemplated under the Launch Aid contracts with the amount by which each per-aircraft repayment would have to be increased in order to repay the Launch Aid at a

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<sup>301</sup> Statement of Professors Joseph E. Stiglitz and Bruce C. Greenwald, *On the Question of the Impact of Subsidies on Supply and Prices in the LCA Market* (Jan. 21, 2008) at 2 (Exhibit US-676).

<sup>302</sup> NERA Economic Consulting, *Quantification of Benefit of Launch Aid* (May 24, 2007) (Exhibit US-606); U.S. SWS, paras. 610-612.

<sup>303</sup> U.S. Answers to Third Panel Questions, paras. 23-29.

<sup>304</sup> EC Answers to Third Panel Questions, para. 292.

<sup>305</sup> EADS web site, <http://www.eads.net/1024/en/investor/ir.html> (last visited Feb. 7, 2008).

commercial rate. The EC has characterized the amount by which each per-aircraft Launch Aid repayment would have to increase to achieve a commercial return as the “benefit per aircraft.”<sup>306</sup> As the economists at NERA have calculated, in order to repay A330/A340 original Launch Aid at the Ellis benchmark rate, Airbus would have to increase each repayment to France by [ ] percent, each repayment to Germany by [ ] percent, each repayment to Spain by [ ] percent, and each repayment to the United Kingdom by [ ] percent.<sup>307</sup>

223. According to the analysis of the EC’s consultants at International Trade Resources LLC (“ITR”), on the projected delivery schedule for the original A330/A340 Airbus would have been required to make the following Launch Aid repayments from 1997 to 2007:

- France: [ ] Euro
- Germany: [ ] Euro
- Spain: [ ] Euro
- UK: [ ] pounds sterling.

224. Based on these figures, in order to repay A330/A340 Launch Aid at the Ellis rate, as calculated by NERA, over the 1997 to 2007 period Airbus would have had to repay:

- France: [ ] Euro
- Germany: [ ] Euro
- Spain: [ ] Euro
- UK: [ ] pounds sterling.

This means Airbus would have been required to repay an additional [ ] Euro to France, Germany, and Spain, plus an additional [ ] pounds sterling to the United Kingdom, had Launch Aid been provided at commercial rates. In other words, if Launch Aid for the original A330/A340 had been provided at commercial rates, over the period 1997 to 2007 the additional Launch Aid repayments for this one LCA program would have been greater than the *entire aggregate pre-tax profit* earned by EADS over these eleven years.

<sup>306</sup> EC SWS, para. 1027.

<sup>307</sup> Exhibit US-644 (BCI).

225. Moreover, this analysis considers Launch Aid for only one model; as the United States has shown, when the total savings from subsidized Launch Aid for all Airbus models is aggregated, the amount – however calculated – is a staggering sum.<sup>308</sup> It simply defies the evidence to contend that the benefit of Launch Aid to Airbus is too small to give Airbus the “ability” to launch the aircraft it has and to sell them at the prices that it has. Airbus simply would not have the resources to raise all of the launch funding that it needed to launch the LCA it has, if it had to do so at market rates.

226. The EC further asserts that, even if Airbus had the ability to use subsidies to lower prices, it currently has no incentive to do so, because it is currently operating at its maximum capacity.<sup>309</sup> Whatever the merits of this assertion, Airbus admits that it did have an incentive to lower prices in order to maintain its production levels in the post-2001 downturn. According to Mr. Scherer’s statement to the Panel, this was a “very very important consideration” for Airbus in this period.<sup>310</sup> And, as explained previously and in comments on the EC’s answer to Question 286 above, Airbus’s lowering of prices in this period has continuing effects on LCA prices and market share in the LCA market today. Thus, even on the EC’s own test, Airbus has the “incentive” to lower prices, and has in fact done so in a way that has continuing adverse effects on its competitor.

227. Finally, that Airbus has had the opportunity to rely on subsidies to lower prices is evident from the fact that it has in fact done so – the shifts in market share, lost sales, price undercutting, and suppressed and depressed pricing are evidence that Airbus has taken full advantage of the opportunities it has been given to make full use of the challenged subsidies.

**290. In *US – Upland Cotton*, the Panel noted that for a basic and widely traded commodity such as upland cotton, "a relatively small decrease or suppression of prices could be significant because, for example, profit margins may ordinarily be narrow, product homogeneity means that sales are price sensitive or because the sheer size of the market in terms of the amount of revenue involved in large volumes trade on the markets experiencing the price suppression."<sup>311</sup> Do the parties consider that, for a product such as LCA, a relatively small decrease or suppression of prices could be "significant" for purposes of Article 6.3(a)? Please explain why or why not, and indicate the factors that the**

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<sup>308</sup> NERA Economic Consulting, *Quantification of Benefit of Launch Aid* (May 24, 2007) (Exhibit US-606); U.S. SWS, paras. 610-612.

<sup>309</sup> EC Answers to Third Panel Questions, para. 293.

<sup>310</sup> EC FNCOS, para. 325 (revised version Dec. 7, 2007).

<sup>311</sup> *US – Cotton Subsidies (Panel)*, para. 7.1330.

**Panel should consider in determining whether the effect of alleged subsidies to Airbus is "significant" price suppression within the meaning of Article 6.3(c).**

Comment:

228. As the Appellate Body has observed, the ordinary meaning of “significant” is “important, notable, or consequential.”<sup>312</sup> A factor will therefore be useful in determining whether price suppression is “significant” if it illuminates whether price suppression is “important, notable, or consequential” in the context of a given situation or industry. None of the four factors that the EC suggests “might be considered” in determining whether price suppression is significant has a bearing on this analysis. Rather, each of them represents a different concept than “significance” and therefore has no basis in the SCM Agreement.

229. The first factor suggested by the EC in determining whether the *price effects* of the subsidy are significant is to ask whether the *magnitude* of the subsidy benefit is significant.<sup>313</sup> As explained in the comments to the immediately previous question, in this case, the magnitude of the subsidy is enormous both in monetary terms and in terms of its impact on Airbus’s commercial activity.<sup>314</sup> Nonetheless, whether the magnitude of the benefit is “significant” to its recipient does not necessarily determine whether the effect of the benefit on the prices of the recipient’s competitors will also be “significant.” As the Appellate Body has observed, the nature of the subsidy – and not merely the size of the benefit – must be considered in establishing the subsidy’s likely effects.<sup>315</sup> A very large benefit may be more likely to cause significant price suppression, but a mere observation about the size of the benefit does not clarify the analysis as to whether the price suppressing effect of that subsidy is “significant.”

230. The second factor suggested by the EC would involve a comparison of the impact of price suppression or depression to the impact of other potential factors affecting prices.<sup>316</sup> The fourth EC factor is similar, in that it involves comparing the relative importance of price and non-price factors to consumers in an industry.<sup>317</sup> Both of these tests purport to determine whether price

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<sup>312</sup> *US – Cotton Subsidies (AB)*, para. 426.

<sup>313</sup> EC Answers to Third Panel Questions, para. 302.

<sup>314</sup> U.S. Answers to Third Panel Questions, paras. 40-46.

<sup>315</sup> *US – Cotton Subsidies (AB)*, para. 461.

<sup>316</sup> EC Answers to Third Panel Questions, para. 303.

<sup>317</sup> EC Answers to Third Panel Questions, para. 305.

suppression is “significant” by determining whether price suppression is more or less important than some other factor unrelated to subsidies. However, it could well be the case that both the subsidy and some another factor are both “significant” in their own way. That one can be said to be more “significant” than another does not necessarily make the other factor not “significant.”

231. Finally, the EC suggests that the financial well-being of the industry of the complaining Member will determine whether price suppression is “significant.”<sup>318</sup> As the United States has explained, however, serious prejudice – unlike material injury – does not require a showing that the affected industry of the complaining Member is, in some absolute sense, suffering injury.<sup>319</sup>

232. As the United States has explained, the price suppression experienced by Boeing for the [ ] throughout the 2001-2006 period, as well as for the [ ], is so large as to be unquestionably “significant” for purposes of this dispute.<sup>320</sup> In the HSBI Appendix, the United States identifies additional evidence in the HSBI documents provided by the EC in response to Question 262 that is relevant to this point.

233. In these circumstances, it does not seem necessary or appropriate to go beyond the text of the SCM Agreement in order to devise a theoretical test for when price suppression is “significant” in a particular industry.

**291. How, if at all, should the Panel's assessment of whether specific sales campaigns provide evidence of price suppression, lost sales or displacement or impedance of imports and exports, be affected by the consideration that Boeing was the incumbent supplier to the purchaser in those campaigns?**

Comment:

234. As the U.S. response to this question demonstrates, both public and HSBI evidence shows that Boeing’s position as the incumbent supplier in a number of sales campaigns was plainly relevant to the pricing strategy that Airbus was adopted in order to induce the customer to switch to Airbus.<sup>321</sup> The EC identifies additional factors that may have played a role in convincing individual customers of the value of Airbus LCA. However, nothing identified in the EC

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<sup>318</sup> EC Answers to Third Panel Questions, para. 304.

<sup>319</sup> U.S. SWS, paras. 694-695.

<sup>320</sup> U.S. Answers to Third Panel Questions, paras. 162-165.

<sup>321</sup> U.S. Answers to Third Panel Questions, para. 167.

response contradicts the fact that certain customers would face switching costs if they ordered from Airbus, or that Airbus offered customers additional pricing incentives to overcome that disadvantage.

**292. In paragraph 1069 of the EC's SWS, the EC argues that "pricing is based on supply and demand". Would both parties please address the implications of this premise in a duopoly market where it appears that strategic interactions are of crucial importance? In their replies, would both parties please indicate how they consider pricing relates to costs in such a market?**

Comment:

235. The EC response to the Panel question can be summarized as follows: In 2001-2003, demand declined, so prices declined. Since then, demand has increased substantially.

236. Notably, the EC response does not draw the conclusion that one would ordinarily expect to follow from the argument that it develops. Because demand has increased substantially, one would expect that prices would have increased substantially. The EC does not, however, state that prices have increased substantially. That is because [ ].

237. Thus, it is not enough for the EC to say that, because LCA demand has risen since 2005, there can *ipso facto* no longer be any serious prejudice to the United States. Even if market developments after the establishment of the Panel were relevant to the Panel's evaluation of the U.S. claims in this dispute, the EC cannot show that serious prejudice does not continue to exist.

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**LIST OF ADDITIONAL U.S. EXHIBITS**

***European Communities and Certain Member States – Measures  
Affecting Trade in Large Civil Aircraft***

<u>U.S. Exhibit</u>	<u>Description</u>
685.	Spread to Benchmark Commercial Rates for Launch Aid Contract Rates and EC “IRRs” <b>(HSBI)</b>
686.	Amortization – Lease Payments <b>(BCI)</b>
687.	Andrew Chisholm, <i>An Introduction to Capital Markets</i> (2002)
688.	Moody’s Credit Rating screen-print
689.	Table: Airbus Entities Receiving Unknown Amounts of R&D Subsidies