

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

**Opening Statement of the United States
First Meeting of the Panel**

March 20, 2007

1. Good Morning, Mr. Chairman, members of the Panel. On behalf of the United States, we would like to begin by thanking the Panel and the Secretariat staff for taking on this task. As we have already seen, this dispute is requiring significantly more work of both the Panel and the Secretariat than the typical dispute, and we appreciate all the time and efforts to date and that will be required in the future.

2. The United States would also like to thank the Panel and the Secretariat for all of their hard work in making the arrangements for the public viewing of this session that will take place later this week. We believe that open meetings will bolster public confidence in the dispute settlement process of the WTO, thereby increasing support for the results of that process.

3. During our presentation this morning, we would first like to make a few general comments on the reasons why the United States has chosen to bring this dispute to the WTO. We will then highlight the arguments and factual evidence that the United States has presented in this case. We will then comment on the EC's written submission. However, given the length of the EC's submission and the fact that we have only two days for this hearing, much of our rebuttal to the EC position will necessarily take place in our second written submission. The

Panel should not view the fact that we address only some of the EC's arguments as an indication that we agree with the others; we will address them in due course.

I. Introduction

4. Mr. Chairman, members of the Panel, the United States has brought this dispute to the WTO because the EU has refused to stop providing massive amounts of prohibited and actionable subsidies to Airbus. The governments of France, Germany, the UK, and Spain have systematically subsidized Airbus for over thirty years. They have done so in a coordinated effort to ensure that at least one of the world's producers of large civil aircraft ("LCA") will be European. And they have succeeded. Subsidies have enabled Airbus to develop a full family of LCA targeted at its U.S. competitors, and they have made Airbus the world's largest producer of LCA.

5. The single largest category of subsidy, and the subsidy that has contributed the most to Airbus becoming the world's largest producer, is the \$15 billion in Launch Aid that the Airbus governments have provided to underwrite the development of Airbus's full family of LCA.

6. Launch Aid is highly preferential, non-commercial financing that the Airbus governments use to offset the enormous costs and extremely high risks that characterize the development of LCA. It always takes the same form: extremely long-term, unsecured loans at zero or below-market rates of interest, with back-loaded repayment schedules that allow Airbus to repay the loans through a levy on each delivery of the financed aircraft. If Airbus fails to sell

enough of the aircraft to repay the loan, the outstanding balances are indefinitely extended or forgiven. Repayment of the aid is entirely dependent on the success of the financed aircraft.

7. By providing Launch Aid on a back-loaded and success-dependent basis, the Airbus governments assume a substantial portion of Airbus's risk of developing new models of LCA. But unlike commercial lenders, they do not charge Airbus for assuming these risks. Instead, they provide the aid either interest-free or at interest rates that are substantially below the rates that commercial lenders would demand for financing with similarly advantageous characteristics. As one UK scholar has observed, "the distinctive risk-sharing feature of Launch Aid confers Airbus with an advantage over a rival who is constrained to debt and equity instruments alone."¹

8. Moreover, Launch Aid is not the only subsidy that the Airbus governments provide. As we demonstrated in our written submission, they also forgive Airbus's debt; fund the creation and expansion of Airbus's production sites; underwrite Airbus's LCA research and development efforts; provide subsidized loans through the European Investment Bank; and infuse equity into the company on noncommercial terms. These additional subsidies add to the benefits that Airbus receives from Launch Aid.

9. The systematic subsidization of Airbus has fundamentally distorted competition in the LCA market to the direct detriment of the United States and its LCA industry. This distortion

¹Kim Kaivanto, *Premise and Practice of UK Launch Aid*, *Journal of World Trade* 40(3) at 495, 517 (2006) (Exhibit US-2).

takes two principal forms. First, Launch Aid has enabled Airbus to launch a series of LCA models at a scale and a pace that would have been impossible without subsidies. Second, Launch Aid has enabled Airbus to pursue an aggressive strategy to increase its market share, likewise in a way that would be impossible without subsidies. All of the adverse effects that we described in our first written submission flow from the market distortions caused by these subsidies.

10. In 2004, the United States approached the EC to propose the negotiation of a new agreement to prohibit Launch Aid and other subsidies for the development and production of LCA. But the EU was unwilling to end the subsidies. Instead of agreeing to end Launch Aid, the Airbus governments committed new subsidies for Airbus's newest model, the A350. And the Airbus governments have confirmed that they plan to continue providing additional subsidies to Airbus for the foreseeable future. For example, just a few weeks ago, the French Prime Minister announced that France would provide 100 million euros to support research into new carbon-fiber composite technologies for Airbus. Remarkably, in the midst of this dispute, the Airbus governments are increasing their involvement in Airbus, not reducing it.

11. Mr. Chairman, members of the Panel, it is this unwillingness to end the subsidies that has led us to bring this dispute to the WTO. It is not tolerable that in a market as risky and competitive as the one for LCA, one producer should have ready access to billions of dollars in up front, risk-free financing for the development of new models of aircraft, while the other must fund the development of its new aircraft through its own cash flow or by raising funds in the

capital markets. The additional subsidies that Airbus receives compounds the problem.

12. Our written submission presented and documented the facts necessary to show that the subsidies the Airbus governments and the European Communities have provided to Airbus are inconsistent with the SCM Agreement. As we explained in our submission, the grants of Launch Aid that Airbus received for the A380, the A340-500/600, and the A330-200 aircraft are inconsistent with Article 3 of the SCM Agreement, because they are contingent upon export performance. In addition, the grants of Launch Aid for every Airbus model and major derivative, and all of the other subsidies that we have documented, are inconsistent with Articles 5 and 6 of the SCM Agreement because they cause or threaten to cause adverse effects to the United States.

13. Of course, the EC disagrees. But what is truly remarkable about the EC submission is how little time is spent on the treatment of Launch Aid under the terms of the SCM Agreement. The EC talks about agreements that are no longer in effect, such as the *Tokyo Round Subsidy Code* and the 1992 agreement, and it accuses the United States of trying to rewrite history.² But it is the EC that is trying to rewrite history, not the United States. The applicability of the SCM Agreement to civil aircraft subsidies was a topic of fierce debate during the Uruguay Round, ultimately resolved with a decision to include them under the Agreement's terms. Therefore, if Launch Aid is a "financial contribution" that confers a "benefit" within the meaning of Article 1 of the SCM Agreement, it is a subsidy. It is as simple as that. And if the subsidy is contingent

²EC Submission, para. 394.

on export performance, or if it causes or threatens to cause adverse effects, then it is inconsistent with the SCM Agreement. By bringing these issues to the Panel, the United States is neither seeking to rewrite history, nor seeking a retrospective remedy. To the contrary, we are merely exercising our right to challenge subsidies that are inconsistent with the SCM Agreement.

14. I will now turn to discuss the reasons why Launch Aid is a subsidy within the meaning of Article 1.1 of the SCM Agreement.

II. Launch Aid is a Subsidy Within the Meaning of Article 1.1 of the SCM Agreement

15. Mr. Chairman, members of the Panel, it would have been understandable if you had found yourself confused, while reading the EC's submission, about the identity of the relevant agreement for determining whether Launch Aid is a subsidy. The EC spends dozens of pages on a remarkable number of alternative legal theories that it wants the Panel to apply to resolve this fundamental issue, none of which has a basis in the SCM Agreement. And when the EC finally addresses whether Launch Aid confers a benefit within the meaning of Article 1.1 of the Agreement, the reasons for its approach become clear: Despite the best efforts of its paid consultants, and after decades of denials, the EC is unable to avoid conceding that Launch Aid is, in fact, a subsidy.

16. The EC is forced to make this concession because of the vast difference between the terms on which the Airbus governments provide Launch Aid and the terms that commercial

investors would demand for financing provided on a similar back-loaded, success-dependent basis. Page two of your materials illustrates this point by comparing the Launch Aid terms for one of the Airbus governments to both the U.S. commercial benchmarks and the EC's proposed alternative commercial benchmarks. As you see from the table, for each of the Airbus models, whichever benchmark you use, the terms of the Launch Aid contracts are below commercial benchmarks.

17. Faced with this reality, the EC focuses instead on trying to minimize the amount of the subsidies by downplaying the riskiness of developing and marketing new models of LCA. But as current events demonstrate, the development and production of LCA is an extraordinarily risky endeavor. A commercial investor providing financing on Launch Aid-type terms would demand a return commensurate with those risks.

18. In this portion of today's presentation, we will first explain the reasons why the Airbus governments' Launch Aid program is a measure that is subject to challenge under WTO rules. Next, we will explain why the EC's many alternative legal theories are not relevant to determining whether Launch Aid is a subsidy under Article 1.1 of the SCM Agreement. We will then discuss the reasons why the U.S. approach for calculating commercial benchmarks for Launch Aid is valid, and why the EC's criticisms of our approach are baseless. We will then explain why the EC's alternative methodologies for establishing benchmarks are unsound. Finally, we will explain why the grants of Launch Aid for the A380, the A340-500/600, and the A330-200 are contingent on export performance.

A. The Airbus Governments Maintain a Program to Support Airbus with Launch Aid

19. Mr. Chairman, members of the Panel, the United States challenges not only each individual grant of Launch Aid, but also the Launch Aid program as a whole. The EC's assertion that we have not challenged Launch Aid "as a subsidy programme" is wrong.³ Our first written submission demonstrates that the Launch Aid program is a measure in its own right.⁴

20. In our first submission, we have shown that for 38 years, in pursuit of an explicit "European industrial policy,"⁵ the Airbus governments consistently have provided to Airbus indispensable assistance consisting of long-term unsecured loans at zero or below-market rates of interest, with back-loaded repayment schedules that allow Airbus to repay the loans, if at all, through a levy on each delivery of the financed aircraft.

21. The evidence that shows the existence of the Launch Aid program includes the inter-governmental agreements in which the Airbus governments steadfastly committed to provide Launch Aid for the A300, A310, A320, and A330/340, as well as the agreement pertaining to the A380 that we referenced in our submission at paragraphs 94 and 101.⁶ Our evidence also includes actual Launch Aid contracts between the governments and Airbus that consistently set

³See EC Submission, para. 343.

⁴See U.S. Submission, paras. 85-106.

⁵Exhibit US-44 (statement of French President Jacques Chirac).

⁶See U.S. Submission, paras. 94, 101; *cf. US - Zeroing (EC) (AB)*, para. 193; *id.*, paras. 198-204; *EC - Biotech (Panel)*, paras. 7.1271-7.1284, 7.1288-7.1295.

forth Launch Aid's characteristic terms.⁷ This evidence shows the “systematic application”⁸ of Launch Aid each time Airbus has undertaken to develop a significantly new LCA model. This systematic application is supported by a network of intergovernmental institutions, most of which were set up under the 1969 French-German government agreement to provide the first grant of Launch Aid, as well as dedicated national bureaucracies within each of the Airbus governments that manage and coordinate the Launch Aid system.⁹

22. The EC accuses the United States of “attempt{ing} to portray {Launch Aid} as a cross-country ‘program’ or system.”¹⁰ But the United States did not invent this portrayal of Launch Aid. We simply repeated the portrayal routinely expressed by those who speak for the governments and for Airbus. As recently as last July, the Airbus Ministers reinforced this portrayal by “reaffirm{ing} their agreement to support Airbus to continue to innovate and to develop programmes in the context of international competition.”¹¹ That reaffirmation was entirely consistent with numerous other references by the Airbus governments to the Launch Aid “system,” as detailed in our first submission.¹² The European Commission put it well in stating that Launch Aid is “part of the commercial landscape of aircraft development” in Europe.¹³

⁷See U.S. Submission, paras. 168-297.

⁸*US - Zeroing (EC) (AB)*, para. 198.

⁹See EC Submission, paras. 95-101.

¹⁰EC Submission, para. 342.

¹¹Exhibit US-63.

¹²U.S. Submission, paras. 100-104.

¹³See, e.g., *EU backs new Airbus aid request, despite US opposition*, Agence France Presse (May 19, 2005) (Exhibit US-60); U.S. Submission, para. 103.

23. That understanding of Launch Aid is also confirmed by the decision of the Airbus governments to provide “legally binding” commitments of at least \$1,700,000,000 in Launch Aid for Airbus’s newest aircraft, the A350 XWB.¹⁴ In fact, only days ago, in discussing consideration of other financing options for the A350 XWB, Airbus CEO Louis Gallois stated, “We are not putting away refundable launch investment.”¹⁵ Likewise, as an Airbus spokesman recently acknowledged, “Launch aid is the only available system right now.”¹⁶

24. But perhaps most revealing of the existence of Launch Aid as a program is the value that market actors place on it. Consider, for example, the explanation that Moody’s recently gave for confirming an A1 credit rating for EADS’s long-term debt, rather than downgrading it:

Moody’s has raised the level of potential support from medium-high to high to reflect the accumulation of indices that Airbus is perceived as economically, socially and politically critical for a wide range of stakeholders.

The rating agency went on to note “an entrenched inclination for state protection.”¹⁷ Page 1 of the handouts reproduces quotes of Moody’s and others reflecting the perception that market actors have of Launch Aid.

¹⁴See, e.g., U.S. Submission, para. 305; *Airbus: Government aid pledges are ‘legally binding’*, Associated Press (Oct. 7, 2005) (Exhibit US-48).

¹⁵AFP, *Airbus weighing up state-backed loans for A350: Gallois* (Mar. 9, 2007) (Exhibit US-449).

¹⁶Katrin Bennhold, *Airbus looks likely to seek state assistance*, International Herald Tribune (June 19, 2006) (Exhibit US-62).

¹⁷Moody’s Investor Service, *Moody’s confirmation of EADS highlights government’s role as odd rescuers* (Mar. 12, 2007) (Exhibit US-450); see also Moody’s Investor Service, *Moody’s Assigns A3 Rating to New Euro Mtn Program of European Aeronautic Defence and Space Company EADS N.V.* (Feb. 6, 2003) (Exhibit US-56); Moody’s Global Credit Research, *Moody’s confirms EADS A1 rating*, (Mar. 9, 2007) (Exhibit US-464); CreditSuisse, *Value versus Risk*, EADS upgrade rating, at 14 (June 15, 2006) (Exhibit US-465).

25. This perception of Launch Aid by credit rating agencies is quite significant, Mr. Chairman. The markets rely critically on every utterance by these entities. Fortunes rise and fall based on their exercise of sound judgment. The fact that Moody's views Launch Aid as part of the landscape to be taken into account in assessing the economic strength of Airbus should leave no doubt that Launch Aid is a program, and not just merely some *ad hoc* benefit that may or may not be given in any particular case. In other words, the Launch Aid program "creates expectations among the public and among private actors," demonstrating that it has "normative value" and should be considered as a measure in its own right.¹⁸

26. Accordingly, the United States challenges Launch Aid writ large as a measure in breach of the EC's obligations under Articles 5 and 6 of the SCM Agreement and Article XVI of the GATT 1994, in addition to challenging the individual grants of Launch Aid that Airbus has received. Later in our statement, we will discuss how the Launch Aid program causes adverse effects to the interests of the United States.

B. The Panel Should Reject the EC's Efforts to Shield Launch Aid from Scrutiny Under the SCM Agreement

27. I will turn now to discuss the several alternative legal theories that the EC tries to use to shield Launch Aid from scrutiny under the SCM Agreement. As I will explain, none has merit.

- (1) *Launch Aid for the A300, A310, and A320 is Subject to the SCM Agreement*

¹⁸US – OCTG Sunset Reviews (AB), para. 187.

28. The EC continues to argue that Launch Aid for the A300, the A310, and the A320 is outside the temporal scope of this dispute. We explained in our response to the Panel's first set of written questions why the EC's theory is wrong. Here, we simply note that the EC has yet to provide any evidence in support of its position. For example, the EC continues to withhold the A300 and A310 Launch Aid contracts and the product-specific disbursement and repayment information for those models, even though the A300/A310 program will not end until this July.

29. In evaluating the EC's approach, the Panel should keep in mind that, for accounting purposes, Launch Aid is treated like a loan until it is repaid or forgiven. If it is not repaid, the outstanding balances become grants. The EC has provided no evidence that Airbus has repaid the A300 and A310 Launch Aid, much less that it repaid the Launch Aid at commercial rates of interest. Therefore, because deliveries of the A300 and A310 end in July, it is likely that the outstanding balances are about to become grants, which may explain the EC's unwillingness to provide the relevant information to the Panel.

(2) *The Tokyo Round Subsidy Code is Irrelevant to this Dispute*

30. The EC's second alternative theory is that the Panel should review the Launch Aid that Airbus received for the A320, the A330, and the A340 under the standards of the *Tokyo Round Subsidy Code* instead of the SCM Agreement.

31. The EC's theory is baseless, because the Panel's terms of reference in this dispute are to

examine the matter in light of the covered agreements cited in the U.S. panel request. The *Tokyo Round Subsidy Code* is not a covered agreement, and there is no legitimate basis for examining Launch Aid under the standards of that agreement. To the contrary, the relevant provisions for determining whether Launch Aid is a subsidy under the SCM Agreement are the provisions of the SCM Agreement.

32. However, it is significant that in this part of its submission, the EC concedes that the Airbus governments did not seek a commercial return on the Launch Aid they granted for these models. Specifically, the EC admits that Germany and Spain provided their Launch Aid interest-free, and the French and UK governments sought at most to recover their cost of funds.¹⁹ The Panel in the *Canada – Aircraft* dispute treated a similar admission by Canada as dispositive with respect to the existence of a benefit, and thus a subsidy, and this Panel should do the same with respect to the EC admission.²⁰

(3) *The 1992 Agreement Does Not Provide Relevant Context for Interpreting the SCM Agreement*

33. The EC's third alternative theory is that the Panel should review the Launch Aid for the A330-200, the A340-500/600, and the A380 for compliance with the terms of the 1992 agreement instead of the SCM Agreement. We explained in our responses to the EC's preliminary ruling requests why the 1992 agreement does not provide relevant context for

¹⁹EC Submission, paras. 388-89.

²⁰*Canada – Aircraft (Panel)*, para. 9.312-313.

interpreting the SCM Agreement.

34. It is abundantly clear from the EC's submission that the EC is seeking nothing less than the interpretation and enforcement by this Panel of the 1992 agreement, notwithstanding the Appellate Body's clear statement in the *Mexico – Soft Drink Taxes* report that WTO dispute settlement panels may not adjudicate non-WTO disputes.²¹ And for the record, the United States does not accept that the EC has complied with the terms of the 1992 agreement.

(4) *Sales Forecasts Are Not the Correct Benchmark for Determining the Existence of a Benefit under the SCM Agreement*

35. The EC's final alternative legal theory is that footnote 16 of the SCM Agreement establishes a special rule for evaluating whether Launch Aid confers a benefit within the meaning of the SCM Agreement. But the EC is wrong.

36. First, footnote 16 of the SCM Agreement is no longer in effect, by operation of Article 31. And when it was in effect, it only spoke to when serious prejudice could be "deemed" as opposed to needing to be proven.

37. Furthermore, there is no basis in the text of footnote 16 for the EC's theory that the repayment of a grant of Launch Aid "excludes" a finding of serious prejudice. To the contrary, footnote 16 stands for the proposition that a failure to repay Launch Aid is debt forgiveness – a

²¹*Mexico – Soft Drink Taxes (AB)*, para. 56.

particularly distortive type of subsidy, as Article 6.1(d) reflects.

38. Similarly, there is no basis in the text of footnote 16 for the EC's theory that sales forecasts are relevant to determining the existence of a "benefit" under Article 1.1(b) of the SCM Agreement. To the contrary, footnote 16 explicitly deals not with "benefit" but with one category of adverse effects – serious prejudice – and then only "for the purposes of this subparagraph." Footnote 16 demonstrates that if the drafters of the SCM Agreement had wanted to make sales forecasts a relevant factor under Article 1.1(b), they would have included a footnote to Article 1.1(b) making that point. Or, they could have included text in footnote 16 like the text in the *chapeau* of Article 14 that creates an explicit textual link between Article 14 and the definition of benefit in Article 1.1(b).

39. The absence of any such language in footnote 16 or in Article 1.1(b) demonstrates that the SCM Agreement does not contain a "special rule" for determining whether Launch Aid confers a benefit, and thus a subsidy. Instead, the same rule that applies to every other financial contribution covered by the SCM Agreement also applies to Launch Aid: did the recipient obtain the contribution on better than commercial terms?

40. The EC's theory about sales forecasts asks the wrong question. A government may expect to receive full repayment of a grant of Launch Aid over the course of 400 deliveries. But if the government provides the Launch Aid at its own borrowing rate, and if that rate is lower than commercial, there is a subsidy, irrespective of the reasonableness of the government's

expectation.

41. Since sales forecasts are not the correct benchmark for determining the existence of a benefit, the EC's extended discussion of the forecasts for the A330-200, the A340-500/600, and the A380 is irrelevant. Therefore, we will not discuss it further, except to note for the record that we do not accept the EC contention that the forecasts were "based on conservative assumptions and reasonable."

C. The EC Concedes That Launch Aid is a Subsidy Under the Terms of the SCM Agreement

42. I will turn now to what the EC describes as its "alternative" legal argument on Launch Aid – which is, in fact, its analysis of Launch Aid under the terms of the SCM Agreement. As I have already noted, the ultimate conclusion – after years of public denials – is that Launch Aid is, in fact, a subsidy.

43. The EC has designated substantial portions of this section of its submission as BCI and HSBI. Therefore, it will not be possible to address the EC's arguments in detail in this public hearing. We will make some general observations now, and then return to those issues in the non-public session.

(1) *Launch Aid is Not a Pure Debt Instrument*

44. The EC Submission begins its analysis of Launch Aid under the SCM Agreement by

criticizing the U.S. methodology for determining commercial benchmarks. But it mischaracterizes the U.S. methodology by pretending that we conceive of Launch Aid as a pure debt instrument. In fact, the U.S. methodology recognizes – as do independent scholars, the panel in the *Canada – Aircraft* case, and commercial rating agencies – that Launch Aid is a hybrid instrument that has characteristics of both debt and equity.

45. The EC mischaracterizes the nature of Launch Aid by denying that it has any equity-like qualities and asserting that it is properly classified simply as debt.²²

46. The EC thus ignores the fact that the Airbus governments – like shareholders and unlike ordinary creditors – have no claim to repayment of an amount certain over a fixed amount of time. A debt-holder knows that it is entitled to receive repayment of a specific amount by a specific date and that a failure of the debtor to make repayment under those terms can trigger default, with potentially devastating consequences for the company. An equity-holder has no such entitlement. If the company fails to pay a dividend in a given quarter, the equity-holder has no claim whatsoever on the company.

47. In addition, like shareholders and unlike creditors, the Airbus governments have no recourse to obtain repayment if Airbus fails to make sales of the financed aircraft. Similarly, like shareholders and unlike creditors, it is the Airbus governments that bear the risk of low returns or losses when the aircraft market is weak. If sales are less than expected, Airbus has no

²²EC Submission, para. 484.

obligation to repay a fixed amount of Launch Aid as it would have to pay a fixed amount of interest on a bond. Like shares of stock and unlike typical bonds or pure debt instruments, Launch Aid has no fixed maturity.

48. As the credit rating agency Fitch has explained, because of Launch Aid’s repayment structure, “Fitch does not treat launch aid as debt.”²³

49. On the other hand, the EC is correct when it notes that the Airbus governments are not guaranteed a share in the upside rewards afforded to equity holders when profit margins are high.²⁴ This is one of the non-commercial elements of Launch Aid – the Airbus governments take a risk similar to that of an equity holder, but they settle for a potential return, if any, that is below the return that a secured creditor would demand.

50. For all of these reasons, the Panel should reject the EC’s request to treat Launch Aid as a pure debt instrument for purposes of determining whether it confers a benefit, and thus constitutes a subsidy.

(2) *The EC’s “Alternative Market Benchmark Rates” Are Flawed*

51. The Panel should also reject the EC’s proposed “alternative benchmark rates” for Launch Aid. The EC calculates its alternative benchmarks by first deriving a project-specific risk

²³Fitch Ratings, Special Report, *Diverging Flight Paths: Boeing and Airbus Large Commercial Aircraft Industry Update* (Nov. 15, 2006), at 6 (Exhibit US-451).

²⁴EC Submission, para. 485.

premium based on expected returns for Airbus risk-sharing suppliers, and then adding that premium to the risk-free rate and the premium for general corporate risk that appears in the Ellis report. Because the EC has designated most of its discussion of the methodology as HSBI, I cannot discuss it in detail in this public session. But I will make two general points.

52. First, the EC's methodology is seriously flawed, due in part to its assumption of a grossly understated risk premium. We will explain these flaws, as well as the flaws in the EC's so-called "corroborating evidence," in the non-public session.

53. Second, and more important, even under the EC's "alternative" approach, there is a substantial spread between the borrowing rates in the Launch Aid contracts and the rates that the EC says Airbus would have received in the market. Therefore, the EC's own methodology confirms that Launch Aid confers a benefit, and thus constitutes a subsidy. Mr. Chairman, this was shown in the table that we referred to earlier.

(3) *The EC's Alternative Calculation of the Interest Rates on Launch Aid is Flawed*

54. Finally, I will address the EC's alternative calculations of the interest rates on the Launch Aid contracts.

(a) *The EC's So-Called "Internal Rates of Return" Methodology is Not an Appropriate Measure of the Benefit of Launch Aid*

55. The EC asserts that our submission underestimates the potential returns on the Launch Aid contracts. But we took the figures in our submission directly from the Launch Aid contracts themselves, which clearly state the relevant interest rates.²⁵ Indeed, the EC’s own submission confirms that the rates in our submission are correct.²⁶

56. Moreover, the EC has failed to disclose the calculations on which its alternative rates are based. The HSBI version of the Ellis Report calculated the potential maximum return under the French A340-500/600 Launch Aid contract, and the outcome was substantially below the corresponding figure in the EC submission.²⁷ Similarly, the French project appraisals for the A330-200 and the A340-500/600 identify the returns on the French A330, A340 and A330-200 Launch Aid. Once again, the returns are substantially below the figures in the EC’s submission.²⁸

57. Finally, the EC has failed to provide any of the underlying evidence that the Panel would need to verify its calculations. For example, the EC has redacted the delivery schedules from the Launch Aid contracts²⁹ – and we have provided illustrative examples in a footnote of where the EC has used white-out to redact information – and it has refused to provide copies of the business cases that allegedly formed the basis for its calculations. Thus, the EC’s assertions

²⁵See, e.g., Exhibit US-35 (BCI), at 3; Exhibit US-72, Art. 6.1; Exhibit US-77 (BCI), Art. 4.1.

²⁶See, e.g., EC Submission, paras. 410, 413, 416, 422, 429, 435 (confirming the “contractual rates of return” in the various contracts).

²⁷U.S. Full HSBI Version Appendix, para. 19.

²⁸See DS316-EC-HSBI-0001199; DS316-EC-HSBI-00001143.

²⁹See, e.g., Exhibit EC-87, at 6 (Quinta).

regarding potential returns remain just that – mere assertions.

(b) *Taxes Are Irrelevant to Determining Whether a Financial Contribution Confers a Benefit under the SCM Agreement*

58. The EC also criticizes the United States for comparing the potential returns in the Launch Aid contracts to the U.S. commercial benchmarks because the EC says the interest rates in the contracts do not account for the effects of taxation. We will explain in our second submission why the EC's argument is without merit. And in any event, even if the EC's alternative interest rate calculations were valid, they are still below the commercial benchmarks proposed by the United States and the EC, as the tables in paragraphs 510 and 546 of the EC's submission confirm.

D. Conclusion on Launch Aid

59. In conclusion, our written submission established a *prima facie* case that the provision of Launch Aid to Airbus, including each individual provision of Launch Aid that Airbus has received, is a specific subsidy within the meaning of the SCM Agreement. The EC's written submission has not only failed to rebut the U.S. *prima facie* case; it has confirmed it.

III. The Launch Aid That Airbus Received for the A380, A340-500/600 and A330-200 Projects are Prohibited Export Subsidies

60. Mr. Chairman, members of the Panel, I will turn now to discuss the reasons why the grants of Launch Aid that Airbus has received for the A380, the A340-500/600, and the A330-200 are prohibited export subsidies.

61. As we have just explained, even with its flawed, alternative benchmarks, the EC was unable to avoid conceding that Launch Aid is a subsidy. In this sense, the EC has made the Panel's task easier, including with respect to the export subsidy claims. The only question is whether the subsidies are contingent on export performance.

62. As the Appellate Body explained in the *Canada – Aircraft* dispute, Article 3.1(a) of the SCM Agreement, including footnote 4, sets out a three-part test for evaluating a claim of export contingency: (1) the “granting” of a subsidy; (2) that is “tied to”; (3) “actual or anticipated exportation or export earnings.” We demonstrated in our written submission that each element is present in each of the grants of Launch Aid at issue. The EC has failed to rebut our *prima facie* case. Since the EC focused its submission almost entirely on the UK Launch Aid for the A380, we will do the same.

63. First, as I have already noted, the EC concedes that the Launch Aid for the A380 is a subsidy, even under its flawed, alternative benchmarks.

64. Second, the EC apparently concedes that the Airbus governments anticipated exportation or export earnings, since it has provided no rebuttal to our demonstration of this point.

65. Finally, although the EC does contest the “tie” between the grant of the subsidies and anticipated exportation and export earnings, it misstates the relevant legal standard and it fails to

apply the evidence to that standard.

66. For example, the EC argues at length that the terms of the A380 contracts do not “vary by reference to the EC or the rest of the world.”³⁰ But the relevant test under the SCM Agreement is whether the grant of the subsidy is “tied to” actual or anticipated exportation or export earnings, not whether the terms of the measure vary by reference to the EC and export markets.

67. Similarly, the EC says the UK was being “prudent” in assessing Airbus’s sales predictions and that it would have been “fiscally irresponsible” for the UK not to assess the commercial viability of the A380 program when it established the terms of the Launch Aid.³¹ The EC also asserts that the UK took Airbus’s sales forecasts into account in deciding to provide the Launch Aid, and that the government’s decision to tie repayment of the Launch Aid to sales served to allocate risk between the company and the UK.³²

68. But the EC is only proving our point: Launch aid is unsecured, so repayment depends entirely on sales. And given the nature of the A380 and its potential market, the UK was only willing to allow Airbus to repay the aid over the number of sales that it did – and thereby assume the level of risk that it did – because it was anticipating that Airbus would make enough export sales to compensate for the low level of domestic demand. If not for actual or anticipated export performance, the UK would have required Airbus to repay the Launch Aid over a much smaller

³⁰EC Submission, paras. 620 *et. seq.*

³¹EC Submission, para. 638.

³²EC Submission, paras. 662-63.

number of sales, or it would have eliminated the tie to sales. Either way, the benefit of the subsidy would have been substantially reduced, because the UK would have assumed much less of Airbus's risk.

69. Moreover, the EC also argues that “any ‘choice’ the company has between export *versus* domestic sales” is driven by the location of customers.³³ But in actuality, as page three of your materials illustrates, Airbus has no choice. Page three incorporates evidence from page 4 of the 1999 Airbus Global Market Forecast. The evidence demonstrates that, from the outset, the A380 was conceived primarily as a product for export markets in Asia. The other evidence we have cited in our written submission shows this, as well. The success of the project relies overwhelmingly on exports. And the UK and the other Airbus governments tied their provision of the financing to terms they knew Airbus could satisfy only with substantial levels of exports.

70. Mr. Chairman, members of the Panel, this is precisely the type of subsidy that Article 3 of the SCM Agreement is meant to prohibit. It is not a subsidy for domestic production that might incidentally have an impact on export markets. To the contrary, it is a subsidy whose express purpose from the outset was to make it possible for Airbus to launch a product that was aimed at export markets, and the terms and conditions of the subsidy are tied explicitly to those anticipated exports.

71. The EC says our position on this issue creates an incentive for Members to make outright

³³EC Submission, para. 665.

subsidy grants instead of loans.³⁴ But the EC is wrong. As the *Australia Leather* dispute illustrates, the status of a particular grant or loan under Article 3 of the SCM Agreement depends entirely on the terms and conditions of that particular measure.³⁵ To recall, the panel in that dispute found the grant contingent upon export and the loan not contingent. We explained in our submission how Launch Aid is different from the loan at issue in *Leather*.

72. In the present case, the Airbus governments provided unsecured, subsidized loans on the condition that Airbus repay the funds through levies on sales. The facts demonstrate that, due to the nature of the product and the nature of the market for that product, Airbus can only meet that condition by exporting. Therefore, the granting of the subsidies is impermissibly tied to actual or anticipated export performance.

73. Furthermore, the EC's assertion that BAE Systems provided a guarantee to the UK government does not change the analysis,³⁶ because the guarantee provision only provides for BAE to pay such sums that Airbus "shall be liable to pay." It is not a guarantee against the risk of non-repayment due to lack of sales. If Airbus fails to make the necessary sales, it is not liable to repay the Launch Aid, and BAE is not liable to do so either. And the EC has provided no evidence that the other Launch Aid contracts were guaranteed at all.

74. Finally, the EC also implies that the UK's A380 Launch Aid contract places no

³⁴EC Submission, para. 645.

³⁵See U.S. First Submission, para. 358-59.

³⁶EC Submission, para. 673.

obligation on Airbus to sell and export A380s.³⁷ But the EC ignores that the contract requires Airbus to “proceed with the {A380} program” and to “use all reasonable endeavours” to achieve its objectives.³⁸ As the Airbus Global Market Forecasts and the A380 business case make clear, those objectives include making substantial numbers of export sales, because the A380 is a product whose success depends overwhelmingly on exports. And as the panel found in the *Canada – Aircraft* dispute, even if the EC’s argument “were relevant in determining whether a subsidy would not have been granted but for actual exportation or export earnings,” it is “insufficient to rebut a *prima facie* case that a subsidy would not have been granted but for anticipated exportation or export earnings.”³⁹

75. In sum, the EC has failed to rebut our *prima facie* case that the Launch Aid for the A380, A340-500/600, and A330-200 is inconsistent with Article 3.1(a) of the SCM Agreement because it is contingent upon export performance.

76. I will now turn to my colleague, Mr. Posner, to discuss the remaining subsidy measures.

IV. The German, French, UK, and Spanish Governments Have Subsidized Airbus Through the Provision of Infrastructure and Infrastructure-Related Grants

77. Mr. Chairman, members of the Panel, I am going to shift our focus now from Launch Aid to the enormous subsidies that Airbus has received to develop, upgrade, and expand Airbus

³⁷EC Submission, para. 609.

³⁸UK A380 Launch Aid Contract, Art. 4.1 (Exhibit US-79).

³⁹*Canada – Aircraft (Panel)*, para. 9.343.

production and other facilities. I will limit my comments to a few key issues; we will return to this topic in our second submission. I will begin my discussion with Hamburg.

A. German Authorities Subsidized Airbus by Creating an Industrial Site for Airbus in Hamburg

78. The EC concedes that Hamburg spent at least €95 million to create an industrial site for Airbus at Mühlenberger Loch. However, the EC argues that the creation of the site is not subject to WTO rules because it qualifies as “general infrastructure” within the meaning of Article 1.1(a)(1)(iii) of the SCM Agreement. The EC’s argument is wrong in several respects.

79. First, the EC relies on an erroneous interpretation of the term “general infrastructure.” The EC asserts that the ordinary meaning of the term “general” is “the opposite of specific.” In actuality, the ordinary meaning of the term is “{i}ncluding, involving, or affecting all or nearly all the parts of a . . . whole, as a territory, community, organization, etc; completely or nearly universal; not partial, particular, local, or sectional.”⁴⁰ Thus, viewed in context, the term “general infrastructure” means infrastructure that is open to all or nearly all users on a universal, non-discriminatory basis, where there are no *de jure* or *de facto* limitations on use. Contrary to the EC’s assertions, the mere fact that a government creates infrastructure for reasons of “public policy” or to “foster economic development” or to perform a “public task” does not make it “general” within the meaning of the SCM Agreement. Were it otherwise, virtually any infrastructure a government creates would be “general” infrastructure.

⁴⁰*New Shorter Oxford English Dictionary* at 1073 (emphasis added).

80. Second, the EC’s argument is based on a false premise. The EC argues that the creation of the site is general infrastructure because Hamburg’s “law on the development of the port” required the City to reclaim the land from Mühlenberger Loch.⁴¹ But the EC’s submission misquotes the port law by omitting relevant text.⁴² Quoted properly, the text of the law makes clear that its requirements apply only to sites within the Harbor Area. Neither the existing Airbus site, nor the newly created site, nor any other portion of the Mühlenberger Loch is located within the Harbor Area. In fact, Hamburg has explicitly excluded each of these areas from the Harbor Area, and thus from the scope of the law.

81. In light of these facts, there is no argument to be made that the creation of the land at Mühlenberger Loch was a “public task” relating to the development of the Port of Hamburg.

82. Mr. Chairman, members of the Panel, Hamburg did not create general infrastructure when it filled in Mühlenberger Loch. To the contrary, it created an industrial site for Airbus, adjoining the existing Airbus site, for the explicit purpose of supporting the production of the A380. The evidence could not be clearer on this point. For example, in February 2001, the Administrative Appeals Court of Hamburg explained the purpose of the project in the following way:

The major reason cited for filing the requests was that the existing site and runway were

⁴¹EC Submission, paras. 777-78.

⁴²EC Submission, para. 777.

inadequate for the construction and delivery of the proposed A3XX jumbo aircraft. . . .
‘The additional need for land results from the required assembly halls, parking positions, the apron and the towing routes, a de-icing and cleaning area, a second compensation wheel and new taxiways. The runway must be extended and broadened so as to allow for the safe take-off and landing of the A3XX aircraft. The construction of a peninsula in the Elbe river and the relocation of the Rüschanal are essential for the extension of the runway. The construction of a 320-meter-long quayside is necessary in order to enable aircraft components to be delivered by water. The production of a jumbo aircraft having the capacity to carry up to 800 passengers is necessary in order to remain competitive with rival Boeing. . . .’⁴³

83. Page four of your materials is a satellite photo of the Airbus facility in Hamburg, including the new land that was created from the Mühlenberger Loch. The photo graphically demonstrates that there is no public access to the newly-created site, which is surrounded on three sides by water and on the fourth by Airbus’s existing facilities and runway.

84. Because the creation of the site and its provision to Airbus is not general infrastructure, the EC is wrong when it asserts that the Panel should ignore the costs of creating the land when it performs its benefit analysis. The evidence demonstrates that Hamburg spent €751 million to transform a protected wetland area into an industrial site for Airbus, knowing that the project would result in a several hundred million euro loss. A private investor would not have made such an investment. By enabling Airbus to avoid spending the €751 million itself, the Hamburg government conferred a benefit, and thus a subsidy, on Airbus.

B. French Authorities Subsidized Airbus by Creating an Industrial Site for Airbus in Toulouse

⁴³Oberverswaltungsgericht Hamburg, Judgement of 19 February 2001, Case No 2 Bs 370/00, para. 13 (at Juris) (Exhibit US-452).

85. I will turn now to briefly discuss the development of the AéroConstellation site in Toulouse and the provision of the site to Airbus for less than adequate remuneration. I will focus my comments today on Airbus's purchase of 51 hectares of land on the site.

86. We demonstrated in our first submission that French authorities spent at least €78 million to develop the AéroConstellation site, which amounts to a cost of €2 per square meter, plus another €80 million to develop facilities on the site. The EC, in fact, does not contest these facts. In addition, the EC's submission states that Airbus purchased at least 51 hectares of the site, and it identifies the per square meter price that Airbus supposedly paid for the land it bought. Since the EC has designated the price as BCI, I cannot identify it in this public session. It is, however, well below the amount the French authorities spent to develop the site.

87. The EC's written submission confirms that the sale of the land to Airbus is a subsidy, because the facts in Toulouse are extremely similar to the facts at issue in the *Scott Paper* case, a case that the EC agrees did not involve the creation of general infrastructure. To quote the EC's submission at paragraph 790:

Scott Paper . . . analyses the sales conditions of a tailor-made site for a specific company. The Commission saw no public policy reason why the French authorities were spending money on the development of a site that was *ab initio* dedicated for sale to a private company. Rather than providing general infrastructure, the French authorities acted in favour of one specific company to whom ownership of the tailor-made industrial site including specific buildings for the factory was transferred with a sales price that did not cover the investment costs. No private investor would have acted in such a manner."⁴⁴

⁴⁴EC Submission, para. 790 (emphasis in original; footnotes omitted).

88. Like the *Scott Paper* project, the AéroConstellation project involved a decision by French authorities to transform agricultural land into an industrial site that was intended from the outset to benefit primarily a specific company – Airbus – and the sale of a portion of the site to Airbus for a price that did not cover the investment cost. As the EC correctly recognizes, a private investor would not have acted in such a manner. Therefore, by so doing, the French authorities conferred a benefit, and thus a subsidy, on Airbus.

C. German and Spanish Authorities Subsidized Airbus in Nordenham and in Several Sites in Spain

89. I will now touch briefly on the grants that Airbus received in Nordenham and Spain.

90. The EC concedes that the Nordenham and Spanish grants are subsidies, and it mostly concedes that the subsidies are limited to enterprises located in designated geographic regions within the jurisdictions of the relevant granting authorities in Germany and Spain.⁴⁵ The EC asserts that the subsidies are not specific, however, unless they are further limited to a subset of the enterprises within the relevant geographical regions.

91. The EC's two-step regional specificity test is based on a flawed interpretation of Article 2.2 of the SCM Agreement, particularly when viewed in the context of Articles 2.1(a) and 8.2(b).

92. As the Appellate Body has stated, a fundamental tenet of treaty interpretation is that the

⁴⁵See, e.g., EC Submission, paras. 891, 965.

interpreter “must give meaning and effect to all the terms of the treaty. An interpreter is not free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility.”⁴⁶ The EC’s interpretation violates this rule, because it makes Article 2.2 duplicative of Article 2.1(a), and it makes Article 8.2(b) superfluous.

93. The only interpretation of Article 2.2 that gives meaning and effect to all the terms of the treaty is the interpretation that the drafters intended: Namely, a subsidy that is limited to enterprises located in a designated geographical region within the jurisdiction of the granting authority is specific, even if all enterprises within the region are eligible for the subsidy, unless the subsidy meets the criteria set out in Article 8.2(b).

94. Indeed, this is precisely how the EC interprets Article 2.2 for purposes of its own domestic countervailing duty law.

V. The German Government Subsidized Airbus by Forgiving At Least DM 7.7 Billion of Deutsche Airbus’s Government Debt

95. Mr. Chairman, members of the Panel, we will now speak briefly to the issue of the German government’s forgiveness of DM 7.7 billion in debt owed to it by Deutsche Airbus.⁴⁷ The EC concedes the essential facts concerning this claim. It does not dispute that in 1998, Deutsche Airbus owed the German government at least DM 9.4 billion, and it acknowledges that in that year, the company made a “lump sum” payment of DM 1.7 billion, which “discharged *all*

⁴⁶*Japan – Alcoholic Beverages (AB)*, at 12.

⁴⁷*See* U.S. Submission, paras. 516-536.

of the remaining obligations of the German government against Deutsche Airbus.”⁴⁸

96. Where the EC disagrees with the United States is in the characterization of this transaction. In the EC’s view, there was no debt forgiveness but, rather, payment to the German government of the “fair value of its claims.”⁴⁹

97. However, characterizing the transaction as payment to the government of the “fair value of its claims” does not affect the economic reality of what occurred. In particular, it does not change the fact that Deutsche Airbus received a substantial financial benefit. This is so, because the “fair value of {the German government’s} claims” already embedded a substantial benefit to Deutsche Airbus in the form of an interest rate of zero.

98. Had Deutsche Airbus’s DM 9.4 billion obligation to the government remained on the company’s books, the company would have continued to receive an interest rate benefit for many years to come. That is, it would have had the use of DM 9.4 billion for no interest rather than for the market rate of interest. Settling the debt was simply a matter of determining the present value of that future benefit – that is, converting it into a lump sum that Deutsche Airbus was permitted to keep, while paying the difference between that amount and the face value of the debt to the government.

⁴⁸EC Submission, para. 1194 (emphasis in the original).

⁴⁹EC Submission, para. 1202.

99. In short, whether this transaction is called debt forgiveness or a settlement for fair value does not matter. Either way, it is a benefit to Deutsche Airbus – and, therefore, a subsidy – because the underlying debt was repayable on terms vastly more favorable than the market would have provided.

VI. The European Investment Bank Has Repeatedly Subsidized the Development of Airbus Large Civil Aircraft

100. I will turn now to briefly discuss the subsidies that Airbus received from the European Investment Bank (“EIB”). I will focus my comments on the EC’s argument that EIB loans are not specific.

101. The EC’s argument that the Panel should judge specificity by examining the total sum of the loans that the EIB has provided to all sectors since its founding would, if accepted, enable massive circumvention of the SCM Agreement. Members could engage in short-term, intense targeting of favored industries without any fear of repercussion, because the relevant measure of specificity would be all subsidies over the course of decades. Perversely, serial subsidizers would be treated more leniently than Members who only provide subsidies on occasion. And the perversity is compounded when one considers that the rule would put developed country Members in a more favorable position than developing country Members.

102. Furthermore, the EC has failed to demonstrate that the EIB’s loans are non-specific within the meaning of Article 2.1(b) of the SCM Agreement. Its own description of the EIB’s

loan approval process makes clear that its loans are discretionary, not automatic.⁵⁰

103. The facts demonstrate that the challenged loans were specific to Airbus. For example, the EC argues that it is not appropriate to focus solely on 2002 to determine the specificity of the €700 million loan to EADS for the A380. We disagree. But even if one examines the total loans under the i2i program between 2000 and 2003, the A380 loan is still 18 percent of the €3.8 billion total, and it is the highest amount provided to any single company across that three year span.

104. We will discuss the EIB's loans in greater detail in our second submission.

VII. Equity Infusions

105. I will now briefly address the equity infusions that the French government provided to Aérospatiale in 1987, 1988, 1992 and 1993/94, and the transfer of the French government's 45.67 percent share of Dassault's capital to Aérospatiale in 1998.

106. The EC explains clearly why Aérospatiale was in critical need of additional funds in the 1987 to 1994 time period, but it does not explain why a private investor with alternative uses for its capital would have provided them.⁵¹ Its justifications are based for the most part on *ex post*

⁵⁰EC Submission, paras. 1017-1023.

⁵¹*See, e.g.*, EC Submission, paras. 1127-1129.

information.⁵² It has provided no evidence of contemporaneous, independent analyses of Aérospatiale’s financial health and prospects. Its 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.⁵³

107. Furthermore, the EC’s description of Boeing as a virtual “case study in the importance of sustaining investment in LCA product development even during periods of weak demand” only proves our point. While Aérospatiale was able to obtain billions of francs in subsidized capital, Boeing was forced to assume “significant additional debt.”⁵⁴

108. Finally, the EC argues that “nothing of economic significance occurred” when France transferred its 45.67 percent share of Dassault’s capital to Aérospatiale.⁵⁵ While the EC may believe this is true from the perspective of the French government, the transaction provided a significant benefit to Aérospatiale, as our written submission demonstrates.⁵⁶

VIII. The EC and the Airbus Governments Subsidize Airbus by Providing Grants to Underwrite Its Research and Development Expenses

109. The final category of subsidy that I will discuss today involves the grants that the European Commission and the Airbus governments provide to Airbus to underwrite its research

⁵²See, e.g., EC Submission, paras. 1112-13, 1116.

⁵³See, e.g., EC Submission, paras. 1108-10, 1133.

⁵⁴EC Submission, para. 1136.

⁵⁵EC Submission, para. 1161.

⁵⁶See, e.g., U.S. Submission, paras. 614-619.

and development efforts. Given the number of programs and their complexity, and the fact that the EC has designated much of the relevant information as BCI, I will not try to discuss the programs in detail in this oral statement; we will address the details in our second written submission. Instead, I will make a few, brief comments of a general nature.

110. First, the EC concedes in its written submission that Airbus has received at least €648.9 million in subsidies for R&D. Since the EC has an obvious incentive to under-report the actual numbers, the Panel should view this figure as the bare minimum.

111. Second, the €648.9 million figure includes only the subsidies granted to what the EC describes as the “relevant companies,” which it defines as Airbus SAS, Airbus France, Airbus Germany, Airbus Spain, and Airbus UK. The figure does not include the subsidies received by other Airbus entities, such as Airbus’s parent company EADS, or its former parent company BAE Systems, or Airbus GIE, or EADS Germany, even though the subsidies to those entities are plainly within the Panel’s terms of reference. Nor has the EC explained why the Panel should disregard those subsidies, particularly when they are for projects that are plainly LCA-related.

112. Third, the €648.9 million does not include the R&D subsidies that Airbus receives from Spain in the form of interest-free loans.⁵⁷ Since interest-free loans are not available in the market, they are subsidies by definition.

⁵⁷EC Submission, footnote 966.

113. Finally, the EC asks the Panel to disregard a substantial amount of the subsidies that the German Federal government provided to Airbus on the grounds that they were committed, but not yet disbursed, by July 1, 2005.⁵⁸ The EC implies that the United States meant to exclude such subsidies from the Panel’s examination. To clarify, we view all subsidies committed to Airbus under the LuFo programs as within the scope of this dispute, irrespective of their disbursement date.

114. Mr. Chairman, members of the Panel, before concluding our discussion of the subsidy measures, we will discuss the EC’s arguments about alleged “extinction” and “extraction” of subsidies.

IX. The EC’s Arguments About “Extinction” and “Extraction” Are Baseless

115. In a last ditch effort to circumvent its obligations under the SCM Agreement, the EC asks the Panel to believe that a series of transactions – several of which the EC misleadingly refers to as “privatizations,” and none of which eliminated the extraordinary degree of government influence in the affairs of Airbus – had the effect of eliminating “the majority of any alleged subsidies.”⁵⁹ The Panel should reject the EC’s argument.

116. The Appellate Body has found – at least in the context of countervailing duty determinations covered by Part V of the SCM Agreement – that a full privatization may

⁵⁸EC Submission, para. 1250.

⁵⁹EC Submission, para. 284.

extinguish a pre-privatization subsidy “where the government retains ‘no controlling interest in the privatized producer’ and transfers all or substantially all the property.”⁶⁰ In fact, the EC itself has argued that “the change in ownership must be of a sufficient magnitude so as to change the control of the enterprise and thus trigger a re-evaluation of the conditions of application of the SCM Agreement.”⁶¹

117. The EC has called attention to several transactions which, in its view, had the effect of eliminating previously granted subsidies. None of these transactions involved a transfer of “all or substantially all” of the subsidized entity to private interests, and none involved relinquishment of a “controlling interest in the privatized producer.” Indeed, there is good cause to question whether the sales at issue were even made on an arm’s-length and fair market value basis.

118. For example, the EC refers to what it calls the “privatization” of Aérospatiale. That transaction entailed a merger with a hand-picked partner – the Lagardère company – in which the French government retained a 48 percent stake and a “golden share” in the resulting enterprise.⁶² Entirely lacking were the “unfettered interplay of supply and demand” and “broad-

⁶⁰US – *Certain EC Products (AB)*, para. 85 (emphasis added).

⁶¹US – *Certain EC Products (Panel)*, para. 7.62; *see also id.*, para. 7.2, n.274 (“European Communities referred to concepts of ‘control’ as a criteria to determine which change of ownership calls for such re-examination of the conditions of application of the SCM Agreement.”).

⁶²EC Submission, para. 232; Décret no. 99-97 du 15 février 1999 instituant une action spécifique de l’Etat au capital de la société Aérospatiale, société nationale industrielle, Journal Officiel de la République Française (Feb. 16, 1999), at 2428 (Exhibit US-453); *see also* Reuters, *France publishes AS/Matra “golden share” decree* (Feb. 16, 1999) (Exhibit US-454).

based access to information on equal terms” – that is, the conditions which, according to the Appellate Body, should cause prices to “reflect the relative scarcity of goods and services in the market.”⁶³ It is no surprise, therefore, that in the aftermath of the deal, French officials lamented the lack of “a realistic valuation.”⁶⁴

119. Other transactions cited by the EC involved small public offerings of shares in EADS. None of these offerings involved more than ten percent of the outstanding shares of EADS, and none involved a transfer of control.⁶⁵ In short, none of these transactions amounted to a full privatization of the type the Appellate Body has found could extinguish a subsidy.

120. Likewise, the exercise of a put option by BAE Systems amounted to the exact opposite of a privatization carried out at arm’s-length and for fair market value. Rather, it was a sale by one co-owner of Airbus to another co-owner of Airbus, pursuant to terms negotiated years earlier, which resulted in the consolidation by EADS of control over the subsidized entity – that is, Airbus.

121. The EC has produced no evidence of any privatization involving a transfer of control in

⁶³*Certain EC Products (AB)*, para. 122.

⁶⁴Assemblée Nationale, Avis No. 1866, Chapter III, part II.C (Exhibit US-455) (“D’après M. Elie Cohen, membre du Conseil d’analyse économique, une valorisation réaliste devait donner à Lagardère SCA 20 % du capital d’Aérospatiale. Dans de telles conditions, on ne peut que s’interroger quant à une éventuelle sous évaluation d’Aérospatiale lors de l’opération de fusion.”); *see also* Sénat, No. 414 (session ordinaire 1998-1999), Rapport d’Information, Commission des Finances, du Contrôle Budgétaire et des comptes Économiques de la Nation sur la restructuration de l’industrie aéronautique européenne, at 155 (Exhibit US-456) (“Dans une perspective patrimoniale et stratégique, il aurait été souhaitable de mieux valoriser le nouveau groupe.”); Economist, *The Making of a Jumbo Problem* (Nov. 9, 2006) (Exhibit US-457).

⁶⁵*See* EC Submission, paras. 261, 263, 264.

any of the transactions at issue. Therefore, the Panel need not and should not reach the question of whether privatization could have extinguished the subsidies at issue here.

122. The EC also claims that subsidy amounts were eliminated by transfers of cash between related parties – transactions that the EC labels as “extractions.” The concept of “extraction” of subsidies is one that the EC has invented. As the EC acknowledges, “this circumstance has not been addressed by the WTO.”⁶⁶

123. Cash transfers between related parties bear no resemblance at all to “arm’s-length, fair market value sales or direct repayment to a government.”⁶⁷ Such transfers amount to a bookkeeping exercise. A subsidized entity – DASA, for example – moves money to the coffers of its corporate parent, DaimlerChrysler.⁶⁸ If this simple accounting step caused subsidies to disappear, the disciplines of the SCM Agreement could be easily circumvented.

124. Additionally, the EC offers no basis for the suggestion that the amount of “disappearing” subsidy in a transfer between related entities is equal to the “full amount” of the “cash extractions.”⁶⁹ That proposition inexplicably assumes that every dollar moved from the books of a subsidized entity to the books of its parent or other related entity is a dollar of subsidy, as opposed to a dollar of non-subsidized capital.

⁶⁶EC Submission, para. 225.

⁶⁷EC Submission, para. 225.

⁶⁸EC Submission, para. 254.

⁶⁹EC Submission, para. 255.

125. The EC has not proven the validity of its concepts of extinguishment or so-called extraction of subsidies, nor has it demonstrated facts that might support its theories. The EC's arguments therefore should be rejected.

126. At this point, we will shift our focus to the adverse effects that the subsidies to Airbus have caused, and for this portion of our presentation, I will turn to my colleague, Mr. Yocis.

X. The Subsidies Have Caused Adverse Effects to the Interests of the United States

127. Mr. Chairman, members of the Panel, the EC and the Airbus governments have caused adverse effects to the interests of the United States within the meaning of Part III of the SCM Agreement through the use of the subsidies that my colleagues have described. These subsidies – especially, but not only, Launch Aid – have distorted competition in the LCA market to the direct and significant detriment of the United States and its LCA industry.

128. The EC submission recognizes that the LCA industry is profoundly shaped by the “enormous start-up costs for new LCA models” and the fact that these costs require major investments to be made “a long time before revenue is generated.”⁷⁰ Although the number of individual launch decisions that an LCA producer makes is relatively small, the consequences of these decisions are not. Indeed, it is widely recognized that “the commercial aircraft industry

⁷⁰ EC Submission, para. 27.

may, more than most, be one in which outcomes are largely determined by a few strategic commitments.”⁷¹ By influencing and distorting the outcome, timing, and content of these “strategic commitments,” Launch Aid profoundly distorts competition in the LCA market in ways that other forms of government support do not.

129. The United States demonstrated in its first written submission that the Airbus governments have inserted themselves into each and every one of the key “strategic commitments” in the history of Airbus by providing subsidies that were decisive to the launch of every Airbus LCA model: the A300, A310, A320, A330/340 “basic,” the A330-200 and A340-500/600 derivatives, the A380, and now the A350.⁷² The EC contests this showing only for the A380.⁷³ We will have more to say later about why the EC position on the A380 is wrong; in fact, Launch Aid played an indispensable role in the development of the A380. Nonetheless, it is worth noting at the outset that the EC, by its silence, has left uncontested one of the most important elements of the U.S. adverse effects case – that Airbus and its entire product line would not be what it is today, but for the provision of Launch Aid and other subsidies by the EC and the Airbus governments.

130. Launch Aid also has a major impact on the profitability and cash flow of Airbus, which in turn allows Airbus to sell and price its aircraft in a way that it could not do without the

⁷¹ Benjamin Esty & Pankaj Ghemawat, *Airbus vs. Boeing in Super Jumbos* (Harvard Business School Strategy Working Paper No. 02-061, Feb. 2002) at 1 (Exhibit EC-344).

⁷² U.S. Submission, paras. 830-834.

⁷³ EC Submission, paras. 1759-1775.

subsidy. The adverse effects that flow from this are also undeniable. Let us turn for a moment to the chart at page 5 of your materials. In that chart, Airbus points with pride to the steady increase of its share of the global LCA market.⁷⁴ Over time, these gains first came largely at the expense of McDonnell Douglas and, since the exit of McDonnell Douglas from the LCA market, exclusively at the expense of Boeing. Airbus has built and delivered more aircraft than Boeing in each year since 2003 – including, it should be added, in 2006.⁷⁵ The subsidies have enabled Airbus to accelerate aircraft development and aggressively price its LCA family and therefore have played a central role in Airbus's winning, and Boeing's losing, major sales.

131. In fact, each form of serious prejudice alleged by the United States – displacement and impedance of U.S. LCA imports into the European Communities, displacement and impedance of U.S. LCA exports to third country markets, lost sales, price undercutting, price suppression and price depression in the world market – each of these flows directly from the market distortions caused by Launch Aid. Without these subsidies, Airbus would have fewer and different LCA models and could not price the ones it has so aggressively. In this duopoly market, that means that the U.S. LCA industry would produce and sell more aircraft at higher prices than it does in the face of subsidized competition. Launch Aid and the other subsidies have the effect – indeed, are well designed precisely in order to have the effect – of shifting more of the global LCA industry to the EC than the EC could achieve in the market.

⁷⁴ Airbus SAS, *An Airbus Product Review*, July 15, 2006, at 5, available at [http://www.jeeham.net/filelib/Airbus%20\(Williams\).pdf](http://www.jeeham.net/filelib/Airbus%20(Williams).pdf) (Exhibit US-458).

⁷⁵ Airclaims database (Exhibit EC-21).

132. The 362 pages of the EC's first written submission that are devoted to the topic of adverse effects are impressive only in their length. It is remarkable how little the EC has said in all these pages in response to the core of the U.S. adverse effects case, and indeed how much of the U.S. case is not only uncontested by the EC's submission, but actually is supported by the evidence contained in it.

133. In the remainder of our statement, we will set forth the key elements of its argument. First, we will show how Launch Aid distorts the LCA market to the advantage of Airbus. Second, we will explain why the effect of the subsidy must be measured with respect to the LCA market as a whole. Third, we will briefly review the evidence from our written submission with regard to the several types of serious prejudice and respond to the methodological issues raised by the EC. Finally, we will address the relevance of recent market developments to the U.S. claims of serious prejudice and, in particular, the claim of material injury.

A. EC Launch Aid Has Significantly Distorted Airbus Product Development and Pricing Practices

(1) *The Effect of Launch Aid on Airbus Product Development*

134. Launch Aid is the primary vehicle by which the Airbus governments absorb much of the cost and risk that Airbus would otherwise have to bear in order to market new aircraft. Dr. Gary Dorman, an economist with extensive experience in the LCA industry, has prepared an illustrative business case – that is, an evaluation of the likely costs and benefits of a project that

any business would undertake before undertaking a major investment – for a typical widebody aircraft program to show how Launch Aid affects the business case for a launch decision.⁷⁶ The “bottom line” results of this illustrative business case are reproduced on page 6 of your materials.⁷⁷ This business case makes assumptions about development cost (here, \$10 billion in non-recurring costs), deliveries (here, 850 over the life of this hypothetical program), and other relevant parameters. In the closed session, we will have an opportunity to compare Dr. Dorman’s analysis to an actual analysis that Airbus performs of the business case for an actual LCA launch.

135. In the table on page 6, Cell (1)(a) shows that the “net present value” in the base case for this program, without subsidies, is a positive \$1,350 million. It is worth taking a few moments to understand what this figure means. Over the expected 20-year life of the program, there will be revenues from aircraft sales, and there will be costs – a large \$10 billion development cost incurred in the first few years, and then production costs going forward as aircraft are built and delivered. When the expected revenue stream and the expected cost stream are both discounted back to the date of launch, using a discount rate of 10% per year, the present value of the revenue stream is \$1,350 million greater than the present value of the cost stream.

136. Provided that everything goes according to plan, the net present value of the program is positive, and therefore this project is viable from a business perspective. The “plan,” in this

⁷⁶ Gary J. Dorman, *The Effect of Launch Aid on the Economics of Commercial Airplane Programs* (Nov. 6, 2006) (“Dorman Report”) (Exhibit US-70).

⁷⁷ Dorman Report at 12 (Table 1).

case, involves forecasts of things like customer demand, cost structures, and market pricing over a period of 20 years.⁷⁸ However, even a casual observer of the LCA industry over the last year can attest that things in this industry do not always go according to plan. The inherent uncertainty in 20-year market forecasts means that any rational LCA producer will consider not only the “base case” but also a number of other scenarios in which things do not necessarily go according to plan.

137. The table on page 6 shows how the net present value of this program is diminished if any of the main parameters – total sales volume, average production costs, and average unit price – fail to meet the 20-year targets in the “base case.” For example, cell (2)(a) shows that if costs and prices meet expectations, but total deliveries fall 5% short of the projected 850 sales, the net present value falls from \$1,350 million to \$616 million. Cell (1)(b) shows what happens if total sales and prices meet expectations, but production costs are 5% higher than expected – the net present value is only \$199 million. And if total sales and production costs meet expectations, but prices are 5% lower than expected, cell (6)(a) shows that the net present value is a *negative* \$191 million.

138. Undertaking such a project, even if the net present value of the “base case” is positive, thus entails substantial risk. But now, let us add Launch Aid to the model. Page 7 of your materials reproduces another chart from the Dorman report.⁷⁹ The first three columns of

⁷⁸ See also EC Submission, paras. 27-30 (making many of the same points).

⁷⁹ Dorman Report at 15 Table 3 (Exhibit US-70).

figures – (a), (b) and (c) – are identical to the “no Launch Aid” scenarios we have just been examining, and the next three columns of figures show the same scenarios with Launch Aid. For the sake of simplicity, the Launch Aid stream in this chart is modeled on the publicly known terms of the Spanish Launch Aid for the A380. There are other scenarios using terms and conditions of other grants of Launch Aid that are included in the BCI version of the Dorman report.⁸⁰

139. The first point to make about this chart is that Launch Aid increases the net present value of the “base case” from \$1,350 million in cell (1)(a) to \$2,386 million in cell (1)(d). In other words, the present value of the extra profits received because of Launch Aid if the “base case” assumptions turn out exactly as expected is more than \$1 billion, fully 77 percent of the net present value without Launch Aid. Keep in mind that this is just the discounted present value of the extra profits to be received over the life of the program. Because of the time value of money, the \$1 billion current value of extra profits to be received over the 20-year period is the equivalent of a much larger face value of those extra profits over the 20 years.

140. But the impact of Launch Aid, however, goes far beyond the increase in the value of the project if all goes well. For example, again referring to the chart on page seven of your materials, if the total sales volume reaches only 85% of forecast levels, the net present value of the program in cell (4)(a) without Launch Aid is a *negative* \$744 million, but with Launch Aid in cell (4)(d), the net present value is a *positive* \$662 million. In fact, you will not from the column

⁸⁰ *Id.* at 13-14 Table 2.

on the right that when the volume of sales fails to reach the expected target, the subsidy results in even more extra present value. This is because the repayment of Launch Aid is tied to sales; if sales do not meet the target forecast, some of the Launch Aid will be forgiven. In fact, Launch Aid is always backloaded, so that the last repayments are also the largest. If the final 15% or 20% of the expected volume of aircraft are never built and sold, the portion of the Launch Aid that is forgiven is even greater.

141. Put another way, when Launch Aid is provided, the decision to launch a new aircraft model is much less sensitive to the level of confidence in the accuracy of the target assumptions for cost, for price, and especially for sales volume. Thus, the effect of Launch Aid is not only – and not even primarily – to bestow extra money on the LCA manufacturer when it launches. The effect is also to shift much of the risk of launch to the government – and therefore to make the very fact of launch more likely.

142. Further, because Launch Aid reduces the risk of projects to Airbus, Launch Aid makes it easier for Airbus to attract other investors at lower cost. My colleague has already observed that the recent announcement by Moody's Investors Service to reaffirm its high credit rating for EADS cited the promise of continuing government support that "reflects an entrenched inclination for state protection and a low appetite for exposing private bond holders to losses."⁸¹ By lowering the risk to these other investors, the Airbus governments leverage the provision of

⁸¹ Moody's Investors Service, *Moody's Confirmation of EADS Highlights Governments' Role as Odd Rescuers*, Mar. 12, 2007, at 1 (Exhibit US-450).

Launch Aid so that it has even greater effects than the direct impact modeled in the Dorman report.

143. The British economist Kim Kaivanto confirms that Launch Aid distorts the LCA market by changing the way that Airbus approaches launch decisions. He writes:

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.⁸²

And this is exactly what Airbus has done. As we have already pointed out, with the sole exception of the A380, the EC does not contest that Airbus would not have launched *any* of its LCA models when it did, if the Airbus governments had not provided Launch Aid. And as far as the A380 is concerned, the public statements of the Airbus governments contradict the EC claim that Airbus would have launched the A380 as it did without subsidies.⁸³

(2) *EC Launch Aid on the Launch Decisions of Airbus Significantly Distorts Competition in the LCA Market*

144. Rather than contest the direct impact of Launch Aid that is demonstrated in the Dorman report, the EC argues, based on a short paper by Dr. Wachtel,⁸⁴ that even if Airbus was not able

⁸² Kim Kaivanto, *Premise and Practice of UK Launch Aid*, 40 Journal of World Trade 495, 498 (2006) (Exhibit US-2).

⁸³ U.S. Submission, para. 833.

⁸⁴ Paul Wachtel, *Critique of “The Effect of Launch Aid on the Economics of Commercial Airplane Programs” by Dr. Gary J. Dorman*, Jan. 31, 2007 (“Wachtel”) (Exhibit EC-12).

to launch any of its LCA models when it did, sooner or later Airbus or some other competitor would have done so, so Boeing is not harmed anyway. Dr. Wachtel claims that, although Launch Aid may well create *aircraft* that would not otherwise exist, it does not create *competition* that would otherwise not exist.

145. As a preliminary matter, it should be noted that Professor Wachtel is a macroeconomist with a specialization, according to his website, in “monetary policy, central banking, and financial sector reform in economies in transition.”⁸⁵ The EC does not assert that he has any particular experience or expertise in the specific economics of the LCA industry. Indeed, the method of analysis in his paper is to “apply the spirit of the Bresnahan and Reiss approach.”⁸⁶ By this, he refers to a study of the number of participants in local markets for doctors, dentists, druggists, plumbers, and tire dealerships⁸⁷ – markets that are hardly comparable to the global market for LCA.

146. In our rebuttal submission, we will show how many of the conclusions Dr. Wachtel reaches are incorrect because he fails to take into account the particular economics of the LCA market. For example, he cannot support his conclusion that “if Airbus had not entered the market, it is more than likely that Boeing would have faced another competitor,”⁸⁸ let alone his conclusion that the impact of that “other competitor” would have been the same as that of

⁸⁵ Faculty biography at <http://w4.stern.nyu.edu/faculty/facultyindex.cgi?id=53> (last visited Mar. 15, 2007).

⁸⁶ Wachtel, para. 5 (Exhibit EC-12).

⁸⁷ Timothy F. Bresnahan & Peter C. Reiss, *Entry and Competition in Concentrated Markets*, 99 Journal of Political Economy 977, 991 tbl.3 (1991) (cited in Exhibit EC-19 note 2).

⁸⁸ Wachtel, para. 8.

subsidized competition from Airbus. For example, Dr. Wachtel does not, and cannot, say when that “other competitor” would have entered the market, or what the technical capabilities and prices of the LCA produced by that “other competitor” would be. A study of the number of participants in local markets for dentists and plumbers cannot answer these questions.

147. Nonetheless, to the extent that Professor Wachtel is correct in his speculation that without Airbus there would be “another” equivalent competitor to Boeing, it is not difficult to continue that speculation and wonder who that competitor might be. After all, at the time Airbus launched the A300, A310, A320, A330, and A340, there already was “another competitor” to Boeing, namely McDonnell Douglas, a U.S. company. The EC submission explicitly links the emergence of Airbus to the disappearance of McDonnell Douglas when it notes the preference of consumers for a competitive LCA market and states: “The Boeing-McDonnell Douglas merger would never have been allowed if these were the only two participants in the sector – that is if the EC LCA industry [that is, Airbus] had not existed.”⁸⁹

148. The EC also points out that McDonnell Douglas exited the LCA market as an independent competitor when its shareholders refused to make the \$12 billion investment that its management said would be required in order to remain competitive.⁹⁰ Understandably so, as the Airbus governments were simultaneously providing Launch Aid and other subsidies to ensure that Airbus would succeed as the second supplier in the market. As a European Commission

⁸⁹ EC Submission, para. 31.

⁹⁰ EC Submission, para. 1388.

aerospace expert said publicly at the time of the launch of the A320: “We see room for only two planes in this market, and one of them will certainly be Airbus.”⁹¹ Why “certainly” Airbus and not McDonnell Douglas or Boeing? Because of the commitment of the Airbus governments to provide the subsidies needed to guarantee that aircraft would be launched, infrastructure would be built, and balance sheets would be cushioned.

149. The economic effect of the subsidized entry of Airbus as the third producer in the LCA market has been modeled by two European economists, acting on behalf of one of the Airbus governments.⁹² Their paper takes into account all of the issues that Dr. Wachtel says are relevant – the size of the relevant market, the impact of price competition on demand, and so forth – in a detailed simulation model specific to the LCA industry (not a model created in the “spirit” of studies of markets for dentists and plumbers). They concluded:

Consumer surplus benefits from a challenge to Boeing have certainly been substantial but most of them could have been achieved by McDonnell Douglas on its own. ... [T]he loss of scale and scope economies by Boeing as a result of the Airbus entry has substantially raised the cost to Boeing of producing the 777 Finally, we find that the presence of Airbus reduces Boeing’s profits by at least \$100 bn [and this only through 1995] and McDonnell Douglas’s by two-thirds. ... If we give the same weight to profits and consumer surplus, this implies that Airbus has had a large negative impact on world welfare but a comfortably positive impact on European welfare.⁹³

150. This is not a dispute about adverse effects to the interests of Boeing. It is a dispute about

⁹¹ U.S. Submission, para. 831 (quoting Ernesto Previdi (Exhibit US-435)).

⁹² Damien Neven & Paul Seabright, *European Industrial Policy: The Airbus Case* (1995) (Exhibit US-382).

⁹³ *Id.* at 2-3.

adverse effects to the interests of the *United States*. If we are going to follow Dr. Wachtel and believe that, if Airbus had not received the Launch Aid necessary for it to have launched all of its existing LCA models, some other company would be competing with Boeing, it is very likely that this other company would be a U.S. producer.

151. To be clear, the United States does not contend that the LCA industry should be a Boeing or even a U.S. monopoly. No one can say with certainty how the LCA industry would have developed over the last 40 years without the EC and Airbus government subsidies designed to ensure that Europe would be the home of one producer in a competitive duopoly. But for the EC provision of Launch Aid, surely there would nonetheless have been competition. But the nature and type of that competition would surely have been different. The United States seeks only what the SCM Agreement seeks – that the competition not be *subsidized* competition.

152. Before moving on, I would like to draw attention to one additional point in Dr. Wachtel’s paper. He asserts that “the most likely counterfactual of no launch aid is that Airbus would delay the decision of whether to launch new aircraft.”⁹⁴ Even if it were true that the only effect of Launch Aid is to accelerate LCA launches that would occur eventually – just later – this alone can have a significant impact. For example, the EC submission states that Airbus’s success in winning a 2003 campaign at Thai Airlines was the result of its ability to deliver an ultra-long-range Airbus A340-500 before Boeing was able to deliver its ultra-long-range 777-200LR.⁹⁵ But

⁹⁴ Wachtel, para. 16 (Exhibit EC-12).

⁹⁵ EC Submission, para. 2109.

Airbus would not have had an A340-500 to offer Thai Airlines in 2003 without the Launch Aid provided for the development of that aircraft. As the then-European Commissioner for Transport stated in a letter to the then-French Foreign Minister:

Aérospatiale could not finance the costs connected with the development of the Airbus A340-500/600 by itself or with the help of bank loans.⁹⁶

153. Moreover, the impact of the subsidy is not eliminated when Boeing launches a competitor plane, as the EC argues.⁹⁷ Once an airline has an installed fleet from one manufacturer, it is more likely to make follow-on orders from the same supplier.⁹⁸ The EC recognizes this effect when, for example, it argues in its submission that Iberia Airlines would more likely (and ultimately did) purchase A340s instead of 777s because it already had some A340s and A320s in its fleet.⁹⁹ Further, even after a new Boeing model becomes available, Airbus can continue to offer its aircraft at a price that reduces the revenue Boeing receives from its new model. The A340 is an excellent example. When customers choose between the 777 and the A340, they generally prefer the 777 because of, among other things, its superior fuel economy.¹⁰⁰ However, Airbus has publicly stated that it competes by calculating the burden of extra fuel costs on A340 customers and reducing the A340 price by an equivalent amount, thus

⁹⁶ Exhibit US-3 at 8 (English version), at 5 (original version) (“Aérospatiale ne pourrait pas financier seule, ou par le recours à des emprunts bancaires, ses coûts liés au développement de l’A340/500-600.”).

⁹⁷ *E.g.*, EC Submission, paras. 2288-2305.

⁹⁸ U.S. Submission, para. 712.

⁹⁹ EC Submission, para. 2096 (quoting Iberia President Xabier de Irala).

¹⁰⁰ *See* U.S. Submission, para. 808 & n.1018.

putting continued pricing pressure on Boeing.¹⁰¹

(3) *The Effect of Launch Aid on Prices in the LCA Market*

154. The primary market-distorting effect of Launch Aid is to allow for the launch of aircraft that would not otherwise occur, and therefore fundamentally and structurally to distort the basic framework of competition in the LCA market. Launch Aid also has a second and independent market-distorting effect on the costs and cash flow of Airbus that gives Airbus an advantage in pricing, particularly in LCA campaigns of strategic importance.

155. With respect to costs, as we have already observed, the impact of the subsidies on the market's perception of the creditworthiness of Airbus is substantial. The subsidies thus have a direct impact on Airbus's ability to raise additional capital, and thus on its marginal cost of capital. This allows Airbus to meet its profitability targets while still reducing price to win sales.¹⁰² With respect to cash flow, Launch Aid reduces the cash drain on Airbus in the initial years of an aircraft project, allowing Airbus to be more flexible in pricing all of its LCA while still maintaining a rapid pace of project development.

156. The EC submission does not deny that, in principle, the availability of additional cash

¹⁰¹ See *id.* para. 808 & n.1019.

¹⁰² See Airbus Annual Review 2005 (Jan. 2006) at 18 (“{T}o Airbus, one percent in profitability matters more than one percent in market share, provided it remains at an average 50 percent market share.”) (Exhibit US-441).

flow can assist Airbus in offering greater pricing flexibility than it might otherwise have.¹⁰³

However, the EC claims that the subsidy benefits from Launch Aid and the other subsidies are too old and too small to impact current sales campaigns. The evidence shows that the EC's argument is mistaken.

157. Because the EC has chosen to designate its benefit calculation as BCI, we cannot discuss it in detail here. However, according to the non-BCI description that the EC provides of its methodology,¹⁰⁴ this calculation purports to be a countervailing duty (CVD) benefit calculation rather than an estimate of the effects of the subsidy, and even then it contains multiple significant flaws that we will discuss at a later time. In any event, the Appellate Body stated in the *Cotton* dispute that there is no obligation to quantify the amount of the subsidy benefit to resolve a claim of serious prejudice.¹⁰⁵ Given the nature of the subsidies at issue here, the United States does not believe that even an accurate CVD-type methodology would be particularly useful to the Panel in measuring the subsidies' effects.

158. However, to the extent that a rough calculation of the overall benefit is a useful way to determine the general magnitude of the subsidy, it seems that one should examine actual disbursements and repayments of Launch Aid and to determine the amount of the benefit using the loan benefit methodology set forth in Article 14(b) of the SCM Agreement. Using the

¹⁰³ EC Submission, paras. 2097, 2106 (asserting that Airbus had additional pricing flexibility in selling A340s previously ordered by Swissair to other customers after Swissair's bankruptcy).

¹⁰⁴ *Id.* paras. 1593-1635.

¹⁰⁵ *US – Cotton Subsidies (AB)*, para. 467.

benchmark interest rates calculated by the United States, and even assuming that 17 years after disbursement, any remaining unpaid balance is written off and no longer accrues additional interest, the resulting benefit from Launch Aid, over the life of Airbus, is well over \$100 billion.

159. To be clear, this figure represents the additional cost that Airbus would have incurred if it had obtained financing on the terms and conditions of Launch Aid at commercial interest rates for that type of financing. The magnitude of the benefit is more than sufficient to draw the conclusion that Airbus could not have done this. That is not to say that there never would have been an Airbus without Launch Aid. But it does show that, had Airbus been restricted to market-based financing for its aircraft projects, it would, at the very least, have proceeded on a different basis and with a different impact on the market. At the very least, the calculation shows beyond question that the EC is wrong when it alleges that the magnitude of the benefit of Launch Aid is small.

160. A more relevant measure of the impact of Launch Aid on Airbus's current financial position can be drawn from a January 2007 report by Deutsche Bank, which includes the chart included at page 8 of your materials.¹⁰⁶ The chart shows that over the 2001-2005 period, nearly half of the net "free cash flow" of EADS, the parent company of Airbus, is accounted for by changes in net Launch Aid – that is, new Launch Aid disbursements less repayments from deliveries of models currently in production. In 2001 and 2002, EADS' free cash flow would have been negative without Launch Aid. Yet it was precisely in this period, when the market

¹⁰⁶ Deutsche Bank, *EADS: Risks Mispriced – Downgrade to Sell*, Jan. 9, 2007, at 7 (Exhibit US-459).

was at its low, that Airbus intensified its effort to win sales and gain market share by aggressively underpricing Boeing and winning several major long-term sales. If during this period Airbus had been relying on its own resources to fund the ongoing development of the A340-500/600 and the A380 and preparing to fund the A350 – if it in fact could have done those things without government subsidies – its financial flexibility to pursue its pricing strategy would have been quite different.

B. There Is a Single Subsidized Product

161. Before moving on to address the particular U.S. serious prejudice claims, we would like to explain why these claims have been made with reference to all Airbus LCA.

162. The United States has demonstrated that both the general practice of Launch Aid and each specific instance of it provides benefits, and affects the market for, *all* of Airbus's LCA products. Airbus markets its LCA products as a whole and prominently features the commonality between its different LCA types as the heart of its product development. The Airbus advertisement at page 9 of your materials is just one illustration of this.¹⁰⁷ Although the various Airbus models in this advertisement are plainly of different sizes, Airbus stresses that they together form a family that provides “commonality and cost efficiency” that will save customers money.¹⁰⁸

¹⁰⁷ Exhibit US-390.

¹⁰⁸ *Id.*

163. The EC submission acknowledges the importance of the full LCA family when it states:

{T}he need to offer separate products whose commonality keep{s} operating costs down for customer airlines across the fleet but which can perform the various missions dictated by an airline's route structure has historically meant that no manufacturer of a single product or family of products, no matter how compelling, has survived in the LCA industry.¹⁰⁹

Thus, on the EC's own telling, an LCA producer cannot succeed by producing a single LCA model that competes independently in a particular segment of the LCA market. Rather, to succeed in *any* segment of the LCA market, a producer must offer a range of products to meet the diverse needs of customers.

164. The Airbus governments have therefore subsidized the full range of Airbus LCA so that each individual model could compete successfully.¹¹⁰ The EC submission says as much when it explains why Airbus needed equity infusions from the sponsoring governments:

With only the A300 and A310 programmes available for sale, Airbus could not compete effectively with Boeing's full line of passenger aircraft, which ranged from the single aisle 737 to the long haul 747. Airbus' relatively small market share during the years before the entry into service of the A320 in 1988 and the A330/A340 programme in 1993 demonstrate that the company either had to grow, or face a static future. Developing a full line of LCA was crucial to the company's growth¹¹¹

165. Rather than respond directly to the U.S. showing that Launch Aid and the other subsidies

¹⁰⁹ EC Submission, para. 30.

¹¹⁰ See U.S. Submission, paras. 718-724.

¹¹¹ EC Submission, para. 1133.

thus benefit all Airbus LCA as a whole, the EC contends that as a legal matter, all Airbus LCA can be a single “subsidized product” only if of the various subsidized Airbus LCA models are all “like products” to one another.¹¹² This has never been the test under the SCM Agreement or the comparable provisions of the Antidumping Agreement.

166. The terms “subsidized product” and “like product” are used repeatedly in Part III of the SCM Agreement. The Agreement does not define the term “subsidized product.” The term “like product” is defined in the SCM Agreement, and is defined in identical terms in the Antidumping Agreement, with respect to a “product under consideration,”¹¹³ although the term “product under consideration” is also not defined anywhere in these agreements. To the contrary, the panel in *US – Softwood Lumber Dumping* specifically concluded that a “product under consideration” under the Antidumping Agreement may consist of a range of specific goods, all of which are not necessarily “like” one another.¹¹⁴

167. This is also the EC’s own practice under these agreements. For example, in a recent antidumping investigation of bicycles from China and Vietnam, the EC concluded that all bicycles – specifically including mountain bicycles, children’s bicycles, and delivery tricycles – comprise a single “product under consideration,” notwithstanding the differences among these

¹¹² *Id.* paras. 1519-1521.

¹¹³ SCM Agreement footnote 46; Anti-Dumping Agreement Article 2.6.

¹¹⁴ *US – Softwood Lumber Dumping (Panel)*, para. 7.153.

products.¹¹⁵ Thus, under the EC’s own practice, the bicycle that Lance Armstrong would buy for himself, and the bicycle that one would buy for a seven-year-old child, can be – if imported from China or Vietnam – part of a single “product under consideration” or – if made in the EC – part of a single “like product,” even though the two bicycle models manifestly are not perfectly interchangeable with one another. The EC does not explain why bicycles of different sizes can be a single “product under consideration,” but LCA of different sizes cannot.

168. Indeed, the EC argued to the panel in *Korea – Commercial Vessels*: “As long as the complainant identifies markets or products that are reasonable and coherent, the Panel should accept that definition. The Panel should reject the complainant’s proposed definition only if it would make a market analysis impossible.”¹¹⁶ The EC does not contend that it is *impossible* to analyze the LCA market as a single market. After all, the Airbus document at page 5 of your materials examines market share in the single world LCA market as a whole.

169. In fact, it is the EC’s proposed division of the LCA market into five separate markets that is not “reasonable and coherent.” In the real world, competition among LCA frequently occurs across the artificial boundaries of the five “markets” that the EC proposes. In fact, British Airways just concluded one competition last month. According to press reports:

¹¹⁵ Council Regulation No. 1095/2005 (Bicycles from Vietnam and China), July 12, 2005, O.J. L 183/1, at 4 para. 22 (Exhibit US-460).

¹¹⁶ *Korea – Commercial Vessels*, Annex F-1, para. 33 (Oral Statement of the European Communities at the Second Panel Meeting).

“It was a close decision between the Boeing 777s and Airbus A330s,” said Robert Boyle, British Airways’ commercial director.¹¹⁷

Here, the customer was choosing between the A330, which according to the EC competes in “the 200-300 seat market” exclusively against the Boeing 767 and 787, and the Boeing 777, which according to the EC competes in “the 300-400 seat market” exclusively against the Airbus A340, not the A330.¹¹⁸ Nor does Airbus even describe the market as divided in the way insisted upon by the EC. Only last Wednesday, Airbus issued a press release that refers to the A330 and A340 together as “a unique family of five aircraft models in operation in the 250 to 375 seats category.”¹¹⁹ We will show later how the confidential information provided by the EC further demonstrates how the EC product division is at odds with how Airbus competes in the market.

C. Existence of Serious Prejudice

170. The previous discussion sets forth the analytic framework that the United States has used to demonstrate each type of serious prejudice it has alleged within the meaning of Article 5(c) and Article 6.3(a)-(c) of the *SCM Agreement*. The evidence of each major type of serious prejudice is, for the most part, not really in dispute; indeed much of it has been submitted by the EC itself. That each type of serious prejudice flows logically and directly from the market-

¹¹⁷ Associated Press, *British Airways Orders 4 Boeing 777s, Rejecting Airbus’s A330* (Feb. 22, 2007) (Exhibit US-461).

¹¹⁸ EC Submission, para. 1509.

¹¹⁹ Airbus Press Release, *Airbus Delivers the 800th A330/A340 Family Aircraft and Increases Further Production*, Mar. 14, 2007 (Exhibit US-462).

distorting impact of the subsidy is equally straightforward. In the interests of time, we will highlight just a few points here.

(1) *Displacement and Impedance*

171. That Airbus has dramatically improved its market share in recent years at the expense of Boeing – whether in the global LCA market, the U.S. market, the EC market, or in the markets of other countries – is not seriously in dispute. In 2006, Airbus maintained most, if not all, of its market share gains in recent years, as demonstrated in the graphs on page 10 of your materials. Airbus deliveries in 2006 broke the company record set in 2005, and in 2006 it built and delivered more LCA than Boeing for the fourth consecutive year.

172. The EC contends that the Panel should evaluate the U.S. displacement and impedance claims under Article 6.3(a) and Article 6.3(b) by examining the market share of *orders* rather than the market share for actual *deliveries*.¹²⁰ However, the text of Article 6.3(a) refers to situations in which “the effect of the subsidy is to displace or impede the *imports* of a like product of another Member into the market of the subsidizing Member,” while Article 6.3(b) refers to situations in which “the effect of the subsidy is to displace or impede the *exports* of a like product of another Member from a third country market.”¹²¹ The ordinary meaning of the terms “imports” and “exports” includes actual *articles* or *things* that cross international borders –

¹²⁰ E.g., EC Submission, paras. 1401-1414.

¹²¹ Emphasis added.

that is, deliveries.¹²² Orders are, at most, contracts for future imports and exports. As the EC acknowledges, orders may be, and frequently are, cancelled or deferred.¹²³

173. Therefore, the U.S. claims of displacement and impedance must be examined with reference to actual deliveries. The analysis of these forms of serious prejudice is distinct from the analysis of claims relating to pricing trends. Because the price of LCA is typically set at the time of order, with possible later adjustments, the analysis of claims of serious prejudice relating to pricing trends properly starts with orders, taking into account any later adjustments. But this is very different from applying an order-based analysis to claims under Article 6.3(a) or (b), which would be contrary to the text of those provisions.

174. Finally, we note that the EC claims that there are insufficient data points in most, if not all, third country markets to perform an analysis under Article 6.3(b).¹²⁴ Many third country LCA markets are, indeed, relatively small, and it is often difficult to establish clear trends over even a five-year period. The EC, of course, exacerbates the problem by artificially breaking up the LCA market into five segments and then treating orders for multiple LCA delivered over a period of years as a single data point; the data are generally more robust when analyzed correctly as deliveries of LCA as a whole.

¹²² See *New Shorter Oxford English Dictionary* at 889 (export defined as “an article that is exported”), 1323 (import defined as “something imported or brought in”).

¹²³ *E.g.*, EC Submission, paras. 1440-1441, 1446, 1451, 1453, 1460, 1495-1496, 1742, 1880, 1882, 1944.

¹²⁴ *E.g.*, *id.* para. 2029.

175. Nonetheless, even if the Panel were inclined to agree with the EC that there is insufficient data to examine any of the individual third country markets identified by the United States, the solution is not, as the EC suggests, to make no finding. Instead, given that both parties recognize that the LCA market is a world market, the United States would ask the Panel to examine whether the effect of the subsidy is to displace or impede the exports of Boeing LCA to the world market or to the markets of all third countries taken as a whole. The chapeau of Article 6.3 provides that serious prejudice “may arise in any case where” one or more of the specific enumerated market effects applies, but it does not prevent a finding of serious prejudice in other situations as well. And to be clear, we would make that argument only in the alternative, if the Panel accepted the EC’s argument.

(2) *Lost Sales, Price Undercutting, and Price Suppression and Depression*

176. With respect to the other forms of serious prejudice, the confidential nature of much of the evidence prevents a detailed discussion here. The public evidence, as set forth in our submission, demonstrates that Airbus has captured market share through a strategy of aggressive product launch and aggressive pricing at key, strategic campaigns. In many cases, Airbus has succeeded in capturing key customers from Boeing. Even where Boeing has been able to maintain customers, the increased competition from Airbus on the basis of price has resulted in depressed market prices and, accordingly, reduced revenues. The public evidence, which is largely confirmed by the confidential evidence provided by the EC, is that Airbus, not Boeing,

took the lead in driving prices downward in recent years. And, as I have already noted, subsidies give Airbus pricing flexibility that is essential for this pricing strategy.

177. The price effects of Launch Aid have significant adverse effects on Boeing. Recall for a moment the “base case” in Dr. Dorman’s model, on page 6 of your materials. The sensitivity of the value of the program to declines in LCA pricing means that even small deviations from expected prices have a large impact on the viability of aircraft programs. Thus, even if Airbus launches an aircraft that proves to be commercially unsuccessful, Boeing is still adversely affected if it is forced to reduce its prices in order to avoid losing sales. Dr. Wachtel’s assertion that if Airbus receives Launch Aid for an unsuccessful project, no one is harmed other than Airbus,¹²⁵ is simply incorrect.

D. Launch Aid, Alone and Together with All Challenged Subsidies, Causes Serious Prejudice to the Interests of the United States

178. In this statement, the United States has focused primarily on the effects of Launch Aid. Indeed, Launch Aid is the primary subsidy that the Airbus governments have used to finance the launch of each Airbus model and the full Airbus LCA family. In order to ensure effective rulings and recommendations by the DSB in this dispute, the United States respectfully asks the Panel to find specifically that Launch Aid is a measure and that Launch Aid alone has caused each of the forms of serious prejudice alleged by the United States.

¹²⁵ Wachtel, para. 15 (Exhibit EC-12).

179. However, the other subsidies that have been provided to Airbus are also significant. Their effects complement and exacerbate the effects of Launch Aid. By providing subsidies for infrastructure, research and technology, and EIB loans, the EC and the Airbus governments provide additional support for the development of Airbus LCA models and they complement Launch Aid in making the launch of those models possible. By providing equity infusions and debt forgiveness, the Airbus governments have provided additional financial flexibility to Airbus, allowing it to pursue its aggressive strategy of increasing market share through price undercutting, even at the cost of depressing and suppressing LCA prices in the market as a whole. Just as Moody's treats "government interference in the case of Airbus" as a single "helping hand in times of financial difficulties" without differentiating among the various types of subsidies,¹²⁶ the Panel properly may treat all of these subsidies together with Launch Aid to measure their effects under the *SCM Agreement*.

180. Therefore, the United States further respectfully asks the Panel to find that all of the challenged subsidies, taken together, have caused each of the forms of serious prejudice alleged by the United States.

E. Material Injury

181. With respect to the U.S. claims of material injury within the meaning of Article 5(a) of the SCM Agreement, the effects of the subsidies to Airbus are fundamentally similar in the U.S.

¹²⁶ Moody's at 1 (Exhibit US-450).

market as in other parts of the world LCA market. The specific details are set forth in our submission,¹²⁷ and we will not repeat them here. We would like to respond briefly, however, to the EC contention that the improvement in the market and financial position of Boeing in 2006 precludes a finding of present serious prejudice and, most especially, a finding that the U.S. LCA industry is experiencing present material injury.¹²⁸

182. The EC says that it accepts the well-established rule that only *measures* in existence at the time of panel establishment may be examined by a panel.¹²⁹ Likewise, despite what the EC says in its submission, the United States accepts the well-established rule that a panel may examine *evidence* that pre-dates or post-dates the establishment of a panel. However, the United States finds no support for the EC's view that the U.S. *claims* that the contested measures in this dispute have breached the EC's obligations under Article 5(a) and 5(c) of the SCM Agreement must be evaluated "at the time when a panel makes its decision"¹³⁰ rather than at the time of panel establishment.

183. To the contrary, the Panel's terms of reference require it to examine "the *matter* referred to the DSB by the United States" in its request for panel establishment.¹³¹ It is well established that the term "matter" as used in the DSU includes both the "measures" and the "claims"

¹²⁷ U.S. Submission, paras. 730-763.

¹²⁸ *E.g.*, EC Submission, para. 2159.

¹²⁹ *Id.* para. 1478.

¹³⁰ *Id.* para. 1477.

¹³¹ Document WT/DS316/4, para. 2 (Oct. 25, 2005) (emphasis added).

contained in the panel request.¹³² Accordingly, the *claims* referred to in a panel request, no less than the *measures* described there, are defined with reference to that panel request. As the Appellate Body has said, “generally speaking, the demands of due process are such that a complaining party should not have to adjust its pleadings throughout dispute settlement in order to deal with a disputed measure as a ‘moving target.’”¹³³ It would be equally improper if the claims raised by a complaining Member also became a “moving target” that could be evaluated only with respect to whether the measures breached a Member’s WTO obligations at some time after the establishment of the panel rather than when a panel was established for the purpose of examining the claim.

184. Therefore, the United States considers that the Panel’s terms of reference require it to examine the claim of the United States in 2005 that the subsidies were causing adverse effects, including material injury and various forms of serious prejudice, in 2005. Any assertion by the EC that material injury ceased to exist after the establishment of the Panel should therefore be left to the compliance stage of this proceeding.

185. Most important, as a matter of *evidence*, the improvement in Boeing’s performance in 2006 does not undermine the U.S. material injury claim. As the EC admits, “the LCA industry has an exaggerated business cycle which is particularly sensitive to external events.”¹³⁴ When demand is unusually strong, as it has been in 2005 and 2006, one would expect any company’s

¹³² *Guatemala – Cement I (AB)*, para. 72.

¹³³ *Chile – Price Bands (AB)*, para. 144.

¹³⁴ EC Submission, para. 29.

performance to improve. When demand is weak, Airbus has historically had its greatest gains in its share of orders; the orders won in market downturns (as in 2002 and 2003) then translate into an ever-greater share of deliveries in the up cycles. But the structural advantage of Launch Aid remains with Airbus throughout the business cycle.

186. Indeed, the 2006 improvement in Boeing's orders demonstrates how significantly relief from subsidized competition improves the fortunes of the U.S. LCA industry. The year 2006 was the first year in a decade or more in which Boeing did not have to counter an aggressive effort by Airbus to market a recently launched and heavily subsidized plane. In 2006, Airbus could not effectively market either its A380 (because of production problems) or its A350 (which had to be redesigned). What 2006 shows is how the absence of a subsidized and aggressively marketed new Airbus aircraft improves the fortunes of the U.S. LCA industry – and, by contrast, how significant the adverse effects of Launch Aid and the other Airbus subsidies have been.

187. The Panel should be under no illusions, however, that this temporary situation will continue if the EC is allowed to continue providing Launch Aid and other subsidies for future Airbus launches. Airbus will overcome the technical problems with A380 production, and the A350 with fully revised technical specifications will be back in the market in the very near future and, in fact, has already started to win new orders in recent weeks. If Launch Aid is permitted to continue, the adverse effects seen in recent years will continue as well.

188. Mr. Chairman, members of the Panel, on behalf of the United States, thank you for your attention through this rather lengthy statement and, again, for your willingness to serve in this dispute. We would be pleased to answer any questions you may have.
