

***EUROPEAN COMMUNITIES AND CERTAIN MEMBER STATES –
MEASURES AFFECTING TRADE IN LARGE CIVIL AIRCRAFT***

(WT/DS316)

**EXECUTIVE SUMMARY OF THE
SECOND WRITTEN SUBMISSION OF
THE UNITED STATES OF AMERICA**

June 4, 2007

1. **Introduction:** The EC looks at this dispute through the lens of the “specific characteristics” of the LCA industry, including its status as “one of the last mass-employment industries in economically developed countries, with a highly skilled workforce” and “an industry in which a lot of pride is invested, which is considered strategic and is closely interwoven with defence industries.” In the EC’s view, the massive subsidies provided to Airbus’s LCA development and production are justified by these “specific characteristics” of the LCA industry – though, of course, this view has no basis in the SCM Agreement. Perhaps realizing this weakness in its argument, the EC has offered up a number of other defenses, none of which are any more persuasive.

2. **Terms of Reference:** The EC continues to pursue the deeply flawed position that a subsidy is not covered by the SCM Agreement if the subsidy first came into existence prior to January 1, 1995. The EC ignores entirely that the relevant question under the SCM Agreement is not when a subsidy first came into existence, but whether the Member providing the subsidy is causing, through the use of the subsidy, adverse effects to the interests of other Members.

3. The EC also continues to pursue its position that the U.S. panel request does not identify the measures at issue with the specificity required by Article 6.2 of the DSU. The United States previously showed that not only is the U.S. panel request clear on its face, but the attendant circumstances leave no doubt as to the identity of the measures being challenged. The EC does not contest that the attendant circumstances made the identity of the challenged measures unmistakable. Instead, the EC contests the permissibility of relying on particular attendant circumstances. Yet, the EC fails to explain why certain attendant circumstances may be relied upon in some situations but not others. Finally, the EC has failed to show any prejudice from the deficiencies it alleges.

4. **Non-covered agreements not relevant:** Notwithstanding the text of the DSU and consistent panel and Appellate Body findings to the contrary, the EC continues to argue that non-covered agreements (*e.g.*, Tokyo Round Subsidies Code and 1992 U.S.-EU agreement) are relevant to this dispute. The EC ignores that the covered agreements listed in Appendix 1 to the DSU provide not only the basis for entering the dispute settlement system, but also the basis for resolving disputes under that system.

5. The EC argues that even though the 1992 agreement is a non-covered agreement it is relevant because it gives rise to “estoppel.” However, the WTO Members have not consented to provide for the application of what the EC refers to as “estoppel” in WTO dispute settlement. Not only do the panel and Appellate Body reports on which the EC relies not support its position, they actually undermine that position, inasmuch as they decline to recognize the applicability of “estoppel” to WTO dispute settlement. And, even by its own terms, the EC’s “estoppel” argument with respect to the 1992 agreement must fail. Among other facts demonstrating the absence of any basis for arguing “estoppel” is the fifth recital in the 1992 agreement, which expresses the parties’ “intention to act without prejudice to their rights and obligations under the GATT and under other multilateral agreements negotiated under the auspices of the GATT.”

6. **Footnote 16 of the SCM Agreement:** Mistakenly relying on footnote 16 of the SCM Agreement, the EC asserts that “the relevant test for determining whether a {Launch Aid} contract in the large civil aircraft sector constitutes a subsidy is the reasonableness of the

forecasts {of aircraft sales}.” However, whether forecasts are reasonable or not is irrelevant if the return the government demands is lower than what a market creditor would demand.

7. Further, while the EC acknowledges that “{f}ootnote 16 does not . . . discuss under which conditions royalty-based financing constitutes a subsidy,” it nevertheless insists that footnote 16 is relevant to that inquiry. In effect, the EC seeks to take footnote 16 out of context and elevate its status to that of a general rule applicable to all inquiries under the SCM Agreement, contrary to customary rules of interpretation of international law.

8. If anything, the existence of footnote 16 is persuasive evidence that Launch Aid does constitute a subsidy. The very fact that the drafters of the SCM Agreement saw a need to clarify that a particular circumstance involving the implementation of Launch Aid contracts “does not in itself” constitute deemed serious prejudice suggests that the drafters presumed that the provision of Launch Aid confers a benefit and thus constitutes a subsidy. Additionally, footnote 16 is evidence that the SCM Agreement applies to the Launch Aid that Airbus received prior to January 1, 1995. At the time the agreement was being negotiated, Airbus was “not fully repaying” the Launch Aid it had received for the A300 and the A310 programs.

9. **Launch Aid:** In its first submission, the EC asserted that the United States had not challenged Launch Aid “as a subsidy programme,” and therefore declined to engage on that U.S. claim at all. As the United States demonstrated in its statement at the first Panel meeting and in its responses to the Panel’s questions, that assertion is incorrect.

10. With respect to provisions of Launch Aid for the development of particular Airbus aircraft models, the EC attempted to show that in demonstrating that Launch Aid confers a benefit on Airbus the United States had overstated the relevant market benchmark and understated the expected return associated with Launch Aid. The EC is wrong on both counts.

11. The question in a benefit analysis under Article 1.1(b) of the SCM Agreement is “whether the recipient has received a ‘financial contribution’ on terms more favorable than those available to the recipient in the market.” In fact, the EC openly admits that for the A320 and A330/A340, Launch Aid was provided either interest-free (Germany and Spain), at the rate of inflation (France), or at the government’s cost of borrowing (UK). The panel in the *Canada - Aircraft* dispute treated a similar admission by Canada with respect to the Technology Partnerships Canada (TPC) program as dispositive with respect to the existence of a benefit and thus a subsidy. The EC also does not dispute that Launch Aid for the A300 and A310 was provided interest-free and thus confers a benefit.

12. This then leaves the A330-200, the A340-500/600, and the A380. For all of these models as well – whether one uses the benchmark rates calculated by the United States or those calculated by the EC – Launch Aid confers a benefit on Airbus. In fact, in responding the Panel’s questions, the EC acknowledged that Airbus sought Launch Aid for the A380 to “maximize{} the programme’s profitability.”

13. Moreover, the EC’s criticism of the market benchmark established in the Ellis Report (Exhibit US-80) is not well founded. First, the EC wrongly contends that Launch Aid should be

treated as pure debt, ignoring its equity-like qualities, including the governments' lack of entitlement to repayment with interest over a specified period of time and lack of recourse in the event of non-repayment. Second, the EC asserts that it is inappropriate to add what it calls "a project-specific risk premium derived from equity returns" to Airbus's cost of debt. It suggests that an equity risk premium should be added only to the corporate cost of equity. However, adding the risk premium that Ellis identified to Airbus's corporate cost of debt was done precisely to reflect the hybrid nature of Launch Aid. Third, the EC alleges that "use of an equity measure {for the risk premium} is at odds with the risk profile and terms of MSF loans." That statement ignores Launch Aid's equity-like qualities and assumes incorrectly that the risk premium identified by Ellis is "an equity measure" rather than a hybrid measure.

14. The benchmark established in the Ellis report is confirmed by several alternative cross-checks. The EC criticizes each of them but fails to discredit any of them. Its criticisms are flawed for reasons including their disregard of Launch Aid's equity-like qualities and their reliance on studies about risk that were unknown at the time that Launch Aid financing was provided and do not represent a consensus view.

15. Nor do the EC's own cross-checks undermine the Ellis benchmark. The first cross-check – a comparison to a contract between an Airbus company and a group of banks for financing development of an aircraft model – ignores important differences between that contract and government-provided Launch Aid, including *inter alia*, the relatively small amount pledged by the banks and the fact that the bank contract provided for full repayment over a relatively small number of sales. The second EC cross-check – a comparison between the Launch Aid risk premium established in the Ellis report and a supposed "equity ceiling" – wrongly assumes that the risk of a single project cannot exceed the risk of a company's equity; wrongly relies on a sample of companies whose sensitivity to economy-wide risk factors is likely to be lower than that of LCA projects; and is based largely on very recent research that does not represent a consensus approach to measuring equity risk.

16. The EC's alternative to the U.S. benchmark – based on project-specific returns for certain Airbus "risk-sharing suppliers" is inapposite, because the situation of risk-sharing suppliers is far different from that of an ordinary, market-based provider of Launch Aid-type financing to Airbus. Investment capital provided by banks and other financial entities is highly mobile, whereas a supplier's capital is relatively immobile in the short and intermediate terms. Further, the return that a risk-sharing supplier demands is likely to be influenced by a variety of factors that would have no relevance to an investor, including anticipated revenue from future business, sales of replacement parts, and servicing of goods supplied. And, a supplier may provide more than one component to Airbus and may adjust the rate it demands under one supply contract according to the rate it demands under a different supply contract. Finally, some suppliers may be shielded from risk by Airbus's commitment to purchase a minimum quantity of supplies regardless of actual aircraft deliveries.

17. In addition to erring in its criticism of the market benchmark in the Ellis report, the EC errs in criticizing the report's reference to the returns on Launch Aid actually identified in the Launch Aid contracts as the basis for comparison to the benchmarks. First, the EC's calculation of an "internal rate of return" for the governments is based on the governments eventually receiving royalties – a possibility Ellis considered so remote that it "would play a marginal role, at most, in a commercial lender's financing decision." Second, although the EC criticizes Ellis for not taking account of tax effects, it fails to provide any evidence to substantiate its assertion of tax effects, and, in any event, tax effects have no bearing on whether a financial contribution confers a benefit under the SCM Agreement. Market-based lenders set interest rates without regard to taxes that the recipients may subsequently pay and, indeed, neither the United States nor the EC allows a party to adjust for tax effects when calculating the amount of the benefit under its domestic countervailing duty regime.

18. Finally, even under the EC's own flawed analysis, Launch Aid confers a benefit, and the EC does not dispute this.

19. **Prohibited subsidies:** With respect to the U.S. claims that certain provisions of Launch Aid are prohibited export subsidies, the EC portrays the United States as arguing that the grant of Launch Aid is tied to anticipated exportation or export earnings merely because the Airbus governments expected that there would be exports of the LCA models developed as a result of Launch Aid. But the United States does not argue that the governments' expectations of exportation or export earnings alone make the provision of Launch Aid contingent upon export performance. Those expectations unquestionably are an important part of the picture. But an equally important part of the picture is the fact that the governments' decision to provide Launch Aid was made in reliance on and in return for a commitment by Airbus to undertake a course of action that necessarily involves exports. The governments' expectations – informed by Airbus's Business Cases, Global Market Forecasts, and Launch Aid applications and by the governments' own critical project appraisals – were an essential precondition to the governments' decisions to provide Launch Aid.

20. In responding to the U.S. showing that certain provisions of Launch Aid are prohibited export subsidies, the EC makes several critical errors. First, the EC adopts the mistaken view that the relationship between export performance and provision of a subsidy must be a condition-consequence or "if-then" relationship in order for the subsidy to be prohibited within the meaning of Article 3 of the SCM Agreement. However, not only is the term "consequence" not used in Article 3.1(a) or footnote 4 of the SCM Agreement, but the express reference to "anticipated exportation or export earnings" in footnote 4 means that a subsidy is contingent upon export performance even if it is granted prior to – rather than as a "consequence" of – "the future factual fulfilment" of exportation. This understanding is supported by the findings of the panels in *Canada - Aircraft* and *Australia - Leather*.

21. The EC compounds its error by making a series of arguments seeking to show the lack of a tie between the provision of Launch Aid and export performance. Its efforts ultimately fail, as they rely on a combination of mischaracterization of the U.S. argument (for example, falsely accusing the United States of confusing anticipation of export performance with a tie to export performance) and insistence on various irrelevant points (such as the possibility of Airbus

electing to prepay Launch Aid amounts and the consistency of the governments' forecasts of LCA sales with prudent business practices).

22. That the United States does not confuse anticipation of export performance with a tie to export performance is demonstrated by the wealth of evidence the United States has brought to bear establishing the existence of such a tie in each of the Launch Aid contracts at issue. The contracts consist of a commitment by the government to disburse Launch Aid according to a set schedule, which is undertaken in exchange for a commitment of performance by the company to repay the Launch Aid amounts on the basis of a specified levy per sale over an agreed-to number of sales. The number of sales over which Launch Aid is to be repaid is so large relative to demand in the EC for the LCA model at issue as to necessarily involve exportation in order to be achieved. The repayment provisions of the Launch Aid contracts establish that an essential condition for the provision of Launch Aid is a commitment to export. Other provisions of the Launch Aid contracts reenforce this point.

23. Related to the EC's mischaracterization of the U.S. export contingency argument is the EC's assertion of an inconsistency between the U.S. demonstration that Launch Aid confers a benefit on Airbus and the U.S. demonstration that the provision of Launch Aid is contingent upon export performance. However, the fact that the Airbus governments anticipate a return on Launch Aid does not contradict the demonstration that Launch Aid confers a benefit. And the fact that the governments are not guaranteed a return does not contradict the demonstration that the provision of Launch Aid is tied to anticipated exports.

24. Also related to the EC's mischaracterization of the U.S. export contingency argument is the assertion that following that argument "financial contributions that foresee a return (such as loans) are more susceptible to be found to contain a prohibited export contingent subsidy than financial contributions in the form of outright grants." However, it is not the foreseeing of a return that makes Launch Aid export contingent but the conditioning of the provision of Launch Aid on a commitment by Airbus to repay Launch Aid over levels of sales that necessarily involve exportation. An actual refutation of the EC's argument is the panel report in *Australia - Leather*, finding a grant contract to be export contingent, but not a loan contract to the same recipient.

25. An additional aspect of the EC's futile attempt to show the absence of a tie between the provision of Launch Aid and anticipated exportation is its reference to Airbus's option to prepay Launch Aid amounts. This point is irrelevant because, *inter alia*, unlike repayment over the number of deliveries specified in the Launch Aid contract, prepayment is not an obligation. Likewise, the EC's reference to the "guarantee" provided by entities related to the company in certain Launch Aid contracts does not help the EC's argument, because these guarantees are not guarantees of repayment of Launch Aid. They merely provide that in the event the company fails to make timely payment to the government following delivery of an aircraft, the government may turn to the company's parent for payment.

26. Finally, the EC offers certain "countervailing explanations" for the Airbus governments' decision to condition the provision of Launch Aid on Airbus's commitment to repay Launch Aid over levels of sales that necessarily involve exports. However, these explanations do not address

the existence of a contractual tie between Launch Aid and export performance but, rather, governments' motivations for establishing a tie.

27. Also, in an effort to show that the United States has somehow confused “export performance” with mere “performance,” the EC misconstrues the evidence. The EC repeatedly asserts that the repayment terms of the Launch Aid contracts are “origin neutral” and that the evidence does not show that these terms “vary at all by reference to the European Communities and the rest of the world.” But these observations are beside the point. Indeed, they suggest a test that has absolutely no basis in the SCM Agreement. The SCM Agreement does not provide that a subsidy is contingent upon export performance, and thus prohibited, only if the instrument tying the subsidy to actual or anticipated exportation or export earnings makes an express demarcation between domestic sales and export sales. Further, the Launch Aid contract repayment terms are “origin-neutral” only if considered in a vacuum, without any reference to the realities of the market in which the LCA models at issue are sold.

28. The EC's argument also is tainted by its misreading of the panel report in *Australia - Leather*. Contrary to the EC's characterization, the fact that the recipient of the subsidy at issue there was the sole exporter of automotive leather was relevant but not dispositive (as was the recipient's status as a participant in a prior program); and, in any event, Airbus is the only EC exporter of LCA. The EC also ignores key facts, including that one of the grant disbursements at issue in *Leather* was made before any of the anticipated exportation had occurred. The EC ignores the sale-based repayment obligations in the Launch Aid contracts, which make them distinguishable from the loan contract in *Leather*. And it ignores that the guarantee of repayment referred to by the *Leather* panel is entirely unlike the “guarantees” provided in certain Launch Aid contracts.

29. Finally, the EC's recourse to portions of the preparatory work for the SCM Agreement is misplaced. The EC's assertion that the U.S. approach to Article 3.1(a) would lead to manifestly absurd or unreasonable results is based on arguments the United States has not made.

30. **European Investment Bank (“EIB”) loans:** With respect to the U.S. claims regarding EIB loans to Airbus, the EC responded principally by contesting that the EIB loans are specific and that they confer a benefit. Among other flaws, the EC's argument relies heavily on an approach to disproportionality for purposes of determining whether a subsidy is *de facto* specific that would measure each loan provided by the EIB against the totality of EIB lending over its entire five-decade-long history – an approach that effectively would excuse massive, long-established subsidy programs such as the EIB from the disciplines of the SCM Agreement. Also, the EC is wrong to suggest that EIB loans do not confer a benefit on Airbus because of supposed (but completely unsubstantiated) “obligations imposed by the EIB” that, according to the EC, a commercial lender does not impose on its borrowers.

31. The United States has presented evidence showing that the EIB's very purpose is to provide financing on terms more favorable than those available in the market. The EC misleadingly attempts to downplay the unmistakable import of statements about the EIB's mission. For example, the EC asserts that the requirements that EIB interest rates “be set at a level enabling EIB ‘to meet its obligations, to cover its expenses and to build up a reserve fund’”

and that the EIB “not grant any reduction in interest rates” mean that “the bank’s Statute expressly prohibits the bank from subsidising any borrower.” But that is not what these provisions mean. All banks – regardless of whether they are for-profit or (as the EIB) not-for-profit – are required “to meet . . . obligations, to cover . . . expenses and to build up a reserve fund.” What distinguishes a market lender from the EIB is that a market lender, in addition to meeting obligations, covering expenses, and building up a reserve fund, seeks a profit.

32. Further, the EC openly admits that the interest on EIB loans provided to Airbus from 1988 to 1993 did not include a risk premium, making them preferential to those available in the market by definition. Even with respect to the 2002 EIB loan to EADS for A380 development, the EC is less than clear as to whether the interest rate actually included a risk premium. That EIB loans confer a benefit on the recipient is further confirmed by a comparison between the EIB loans to Airbus and market benchmarks established on the basis of the only two EIB loans for which the EC identified the precise terms and conditions.

33. In addition to lower-than-market interest rates, EIB loans confer a benefit by excluding a commitment fee. The EC’s assertion that uncertainty about date of disbursement and the final interest rate on an EIB loan explain the absence of a commitment fee ignores the purpose of a commitment fee as compensating for providing a borrower the valuable option of drawing on funding at a later date.

34. The EC’s proposed market benchmark for measuring the benefit conferred by EIB loans is flawed for several reasons, including, *inter alia*, its reliance on bonds issued in the United States, notwithstanding known yield differences between such bonds and dollar-denominated bonds issued by persons outside the United States.

35. With respect to specificity, despite repeated assertions that eligibility for EIB lending is “objective” and “automatic” (and therefore, in the EC’s view, non-specific as a matter of law), the EC’s position is belied by its own explanation. In particular, the EC describes multiple layers of review that must be completed in order for the EIB to approve a loan application, showing that obtaining an EIB loan is anything but “automatic.” Also, the factors considered during that process show that the criteria or conditions governing eligibility – such as “improvement of the efficiency and/or quality of the infrastructure” and “alleviation of social problems or exclusion” – are subjective rather than objective. While the EC calls the EIB Eligibility Guidelines “a very good example of criteria which are economic in nature and horizontal in application, and which are not favouring enterprises of any sector (or even any size),” it provides absolutely no demonstration of why this characterization is accurate. And, indeed, it is not.

36. Additionally, with almost no discussion, the EC asserts that “{t}he challenged EIB loans . . . cannot be specific under Article 2.1(a) *SCM Agreement*,” apparently based on the absence of explicit limitations on eligibility for EIB loans. However, if the unique terms and conditions of a given subsidy contract are sufficiently different from the terms and conditions of other contracts granted under the same subsidy program, this can cause the subsidy at issue to fall outside the parameters of the broader program of which it is a part. In that case, the subsidy ought to be considered separately from the larger program for purposes of a *de jure* specificity analysis

under Article 2.1(a) of the SCM Agreement. In this regard, the EC has refused to provide the information that the Panel would need to evaluate the unique terms and conditions of most of the EIB loans at issue. Moreover, the EC refused to provide information about other EIB lending that might allow for an analysis of the manner in which the EIB exercised its discretion in providing loans to Airbus as compared with other borrowers.

37. **Infrastructure:** The EC’s argument concerning U.S. claims relating to provisions of infrastructure rests largely on the position that much of what the United States has challenged constitutes “general infrastructure” within the meaning of Article 1.1(a)(1)(iii) of the SCM Agreement and, therefore, is excluded from the definition of “subsidy.” To make that argument, the EC asserts a broad definition of “general infrastructure” that finds no support in the SCM Agreement or, indeed, in the EC’s own practice under its state aids regime.

38. Based on its ordinary meaning, the term “general infrastructure” must include, involve, or affect all or nearly all the parts of a whole territory or community; must be completely or nearly universal, as opposed to partial, particular, or local. The EC has proffered a very different definition that focuses on the fulfillment of broad public policy goals, such as “*enabl{ing}*” members of the public at large, thereby fulfilling a public policy objective.” Governments routinely act with the intention of “fulfilling a public policy objective.” If any grant of infrastructure that met that test were deemed to be general infrastructure then virtually every grant of infrastructure would be excluded from the SCM Agreement’s definition of “subsidy.” But that result would deprive the word “general” in the phrase “general infrastructure” of any meaning. Nor do the *travaux préparatoires* for the SCM Agreement help the EC’s position. And, indeed, that position is contradicted by the EC’s own practice under its state aids regime.

39. **Infrastructure (Airbus site at Mühlenberger Loch):** There is no dispute between the EC and the United States that the City of Hamburg created the artificial land at the Mühlenberger Loch free of charge and free of risk for Airbus – and thereby allowed Airbus to expand its existing facilities to accommodate A380 production. The EC’s approach to addressing the undisputed facts is to treat the creation of the site, the building of flood protection measures, and the building of special-purpose facilities on the site as three separate transactions, each distinct from one another, as well as being distinct from and unconnected to the lease of the newly created land and special purpose facilities to Airbus. The EC argues that the creation of the site, in and of itself, did not constitute a financial contribution to Airbus but, rather, the provision of general infrastructure. The EC then treats the lease to Airbus no differently from an ordinary commercial lease in which it was not necessary to first create the artificial land. This approach ignores the reality that the City of Hamburg invested Euro 750 million into creating a site to the specifications of Airbus, an amount that Airbus otherwise would have had to spend itself on the expansion of its existing site.

40. The EC's assertion that creation of the Airbus site at the Mühlenberger Loch amounted to the provision of general infrastructure is wrong for several reasons. First, the EC's theory that land for industrial and residential use in Hamburg is limited because Hamburg is "surrounded by water" is factually incorrect. Hamburg is located on the river Elbe, but it is certainly not surrounded by water, and Hamburg's own Minister for the Economy has touted the "abundant supply of office space and commercial real estate" in Hamburg.

41. Second, the EC's assertion that the creation of the new, artificial land in the Mühlenberger Loch was motivated by the need for additional land for the harbor and thus undertaken to fulfil a public task – the development of the harbor – is both legally irrelevant and factually wrong. It is legally irrelevant because the test for whether infrastructure is general is not whether it serves some "public policy objective." As for the facts, a closer examination shows that the creation of the site for Airbus does not serve the development of the Port of Hamburg, but was undertaken exclusively for Airbus. As the EC grudgingly admitted in responding to the Panel's questions, the entire site created from wetland and river areas in the Mühlenberger Loch and Rüschkanal is located outside the Harbor Area as defined by Hamburg's Port Development Act. The EC also errs in describing plans for expansion of the Harbor Area.

42. Third, the EC ignores that the Mühlenberger Loch and the Rüschkanal were transformed into artificial land exclusively for Airbus. This fact is confirmed by contemporaneous statements by the European Commission, the Hamburg government, and the Hamburg Court of Appeals.

43. Equally erroneous is the EC's theory that the Airbus site amounts to general infrastructure due to the remote possibility that one day the site might be used by another user, as long as the City of Hamburg retains formal ownership of the site. It would be very easy to circumvent the SCM Agreement if the provision of infrastructure by a WTO Member to specific companies or industries – even on a decades-long basis – were excluded from the agreement by virtue of being "general infrastructure" simply due to the Member's retaining title to the infrastructure. Moreover, the EC's portrayal of the relevant facts is incorrect. German planning law prohibits any use of the site other than for aircraft manufacturing and aviation purposes. And with respect to the dyke lane that surrounds the site, the EC ultimately must admit that during the period of Airbus's lease, it is open to use only by "Airbus employees and officials of Hamburg with a responsibility for dyke maintenance and security." Even assuming hypothetically that the restrictions under German planning law did not exist and that Airbus terminated its use of the newly created land, the site still would not be suitable for users other than Airbus given the land's physical and geographical situation.

44. As for the dykes around the Airbus site – built at a cost of Euro 29.3 million (about four percent of the total cost of creating the artificial land) – these are not general infrastructure, because it would not have been necessary to build them absent the creation of that land for Airbus in the first place.

45. Given that the site created for Airbus at the Mühlenberger Loch is not general infrastructure, its lease to Airbus on terms that do not include the investment in creating the site confers a benefit on Airbus. And, in addition to ignoring the cost of creating the site, Hamburg

assumed the entire risk that the artificial land may subside, conferring an additional benefit on Airbus in the form of a reduced lease price until 2019.

46. The EC argues that the cost of turning the wetland and water areas in the Mühlenberger Loch and the Rüschanal into a site for Airbus are irrelevant as a benchmark. In the EC's view, these costs do not reflect the benefit to Airbus, but the cost to Hamburg. However, the EC ignores that Hamburg's actions represent a substantial cost savings to Airbus. Had it not been for the government's creation of the land, Airbus would have had to make that investment itself.

47. Even assuming, for the sake of argument, that the value of pre-existing land is the right basis for determining a market price for Airbus's lease, the actual lease price still falls below a market benchmark. The opinion to the contrary by the Hamburg Committee of Experts for Property Values is flawed in part because it accepts the proposition that the risk that the land will settle should be accounted for through a rent reduction, and in part because it uses the wrong basis under German law for calculating a market interest rate. Finally, even assuming that the land leased by the City of Hamburg had already existed (and that a market-based lease price would not, therefore, have reflected the cost of creating the land in the first place), a private landowner certainly would have demanded a premium from Airbus over the lease price it would have charged any other lessee, given that this site is adjacent to Airbus's existing facilities and is the only site that Airbus could use to locate its A380 production in Germany.

48. **Infrastructure (grants in Germany and Spain):** With respect to grants for the construction of Airbus and EADS manufacturing and assembly facilities provided by a regional government in Germany and by national, regional, and local governments in Spain, supported in some cases by the European Regional Development Fund, the EC's principal defense is to argue that the grants are not specific within the meaning of Article 2 of the SCM Agreement. This argument rests on two mistaken propositions: (1) that for a subsidy to meet the regional specificity test under Article 2.2, it must be limited to a subset of enterprises within a designated geographical region, and (2) that even if a subsidy meets this mistaken standard, it nevertheless may be found non-specific by virtue of Article 2.1(b).

49. The EC's reading of Article 2.2 would reduce Articles 2.1(a) and 8.2(b) of the SCM Agreement to redundancy or inutility. Article 2.1(a) provides that a subsidy "shall be specific" if access is "explicitly limited" to "certain enterprises." Yet, the EC would read Article 2.2 to provide the same thing. Article 8.2(b) made subsidies in the form of assistance to disadvantaged regions non-actionable during the period when the article was in force, as long as the subsidies met certain criteria. One of those criteria was that the subsidies be "non-specific (within the meaning of Article 2) within eligible regions." Yet, under the EC's reading of Article 2.2, if a subsidy provided to a particular region is non-specific within that region, then it is not specific under Article 2.2 in the first place. Following that logic, it would have been unnecessary to provide that a regional subsidy is non-actionable if, *inter alia*, it is non-specific within the region. Similarly, under the EC's reading of Article 2.2, Article 8.1(b) would make no sense.

50. The EC professes to find support for its reading of Article 2.2 in the SCM Agreement negotiating history. However, its discussion of the history is inaccurate and ultimately does not support the EC's conclusion. In particular, the EC ignores that the focus of the debate on

regional specificity was on whether the fact that a subsidy was limited to a “designated geographical region” would automatically make it specific or whether, instead, regional specificity would depend on the scope of the granting authority’s jurisdiction. Finally, the EC’s proposed construction of the regional specificity provision in Article 2.2 is contrary to its own practice in countervailing duty proceedings.

51. Additionally, the SCM Agreement does not support the EC’s theory of a hierarchical relationship between Articles 2.1(b) and 2.2, whereby a finding of non-specificity under the former will prevail over a finding of specificity under the latter. When the drafters of the SCM Agreement wanted to make one provision subject to another then knew how to do so, but did not do so with respect to these two articles.

52. **Infrastructure (Aéroconstellation site):** With respect to the U.S. claim regarding the Aéroconstellation site in Toulouse, France, the EC’s principal response is to argue that the goods the French authorities provided to Airbus constitute general infrastructure and therefore are excluded from the definition of “subsidy.” This is another example of the EC’s flawed understanding of what constitutes “general infrastructure.” Moreover, as with the Hamburg site, the EC’s contention that the United States has taken a cost-to-the-government approach to showing the existence of a subsidy ignores the fact that by transforming agricultural land into an industrial site and then providing it to Airbus at a below-market price, the French authorities have conferred a benefit on Airbus in the form of a cost savings.

53. Also, Airbus does not pay a lease price reflecting market conditions for the so-called EIG facilities (taxiways, parking, etc.) at the Toulouse site. The average annual lease price of Euro 3.1 million demanded by Grand Toulouse for Airbus’s use of the EIG facilities is substantially below a market price of between Euro 9.9 million and Euro 12.1 million for the facilities and the land. Other non-commercial aspects of the lease include the fact that Grand Toulouse allows for a deferral of the lease payments.

54. **Infrastructure (Bremen airport runway extension):** With respect to the U.S. claim regarding Airbus’s exclusive use of the runway extension at the Bremen airport, the EC argues that Airbus does not receive a benefit “because it is landing heavier aircraft, and is in turn paying a higher user fee.” However, the EC misunderstands the fee regulation adopted by the City of Bremen. Under that regulation, fees are based on maximum take-off weight, not actual take-off weight. And in any event, regardless of the maximum take-off weight, users other than Airbus are not allowed to use the extended runway. Absent an arrangement that ensures that the City of Bremen is compensated for the runway infrastructure created specifically for Airbus and open for use only by Airbus, Airbus receives a benefit from having been provided with this infrastructure.

55. **Infrastructure (EADS-CASA’s Sevilla/La Rinconada facility):** With respect to the U.S. claim concerning an October 2004 grant of Euro 61.9 million from the regional government of Andalusia to EADS-CASA for an investment project in the municipalities of Sevilla and La Rinconada, the EC asserts that the grant is not being used for large civil aircraft activities. However, the evidence it provides fails to substantiate this assertion.

56. **Infrastructure (Broughton facility):** With respect to the U.S. claim concerning a £19.5 million grant the Welsh Assembly provided to BAE Systems in September 2000, the EC argues that the grant is not specific within the meaning of Article 2 of the SCM Agreement. However, the EC fails to address the circumstances under which the grants were provided. In particular, it ignores entirely BAE Systems’s application for a grant under the Welsh government’s RSA scheme and the reaction provoked by the rejection of that application, leading to the grant actually provided. Examining the circumstances surrounding the Welsh grant in their totality reveals that the grant indeed is specific within the meaning of Article 2 of the SCM Agreement.

57. **German government’s settlement of DM 9.4 billion debt for DM 1.7 billion:** In 1998, Deutsche Airbus owed the German government approximately DM 9,400,000,000 in LCA-related debt. In that same year, Deutsche Airbus and the German government reached an agreement whereby the company made a one-time, lump sum payment of DM 1,735,000,000, in consideration for which the government extinguished the remainder of the debt. The EC does not dispute these facts. Nevertheless, it would have the Panel believe that the elimination of DM 7,700,000,000 in debt did not confer a benefit on the company. Its theory is that the 1998 transaction was a fair-value payment for the net present value of the outstanding debt.

58. While the United States does not accept the EC’s characterization of the 1998 transaction, the characterization does not change the fact that the transaction conferred a benefit. Under either characterization, the German government effectively turned potential benefits that Deutsche Airbus might have enjoyed in the future from savings on debt provided interest-free by the German government into an actual cash grant of DM 7.7 billion provided in 1998.

59. The EC wrongly accuses the United States of responding to the EC’s characterization of the 1998 transaction by asserting a new claim. In fact, the United States simply has responded to the EC on its own terms, demonstrating that even if, *arguendo*, the EC’s characterization of the 1998 transaction were accurate, the transaction still conferred a benefit. The EC’s theory that the United States really is challenging the German government’s 1989 aid package to Deutsche Airbus rather than the 1998 debt settlement, and that the aid package is outside the Panel’s terms of reference because it was not identified in the U.S. panel request is mistaken. First, the U.S. panel request refers, in relevant part, not only to the German government’s “forgiveness” of debt owed by Deutsche Airbus but also to its earlier “assumption . . . of . . . debt accumulated by Deutsche Airbus.”

60. Second, the EC mistakes the relevance of the 1989 aid package to the U.S. claim. The United States is not challenging the aid package in and of itself. It is challenging the 1998 debt settlement transaction. That transaction appears to be a forgiveness of the approximately DM 7,700,000,000 difference between the face amount of the debt and the amount the company actually paid the government. In light of the EC’s response, the United States reexamined the transaction from the point of view of the EC’s characterization. That necessarily entailed consideration of the elements that determined the fair value of the debt, notably its highly preferential repayment terms. This showed that following the EC’s characterization leads economically to the same result as originally observed by the United States.

61. **German and French government equity infusions:** The United States has shown that Airbus benefits from equity infusions provided by the German and French governments at moments when a market-oriented investor would not have made such investments due to the dire financial condition of the French and German Airbus companies, respectively. The EC responded that the governments' actions were consistent with the usual practice of private investors. To make its case with respect to the German infusion, the EC relies on a false benchmark that it holds up as a market benchmark. It asserts that "at the same time" that the government made its investment a private investor, "Daimler (through MBB)," also made an investment in Deutsche Airbus – omitting the fact that Daimler's willingness to make its investment depended heavily on the government first providing a substantial aid package which included the government's own investment.

62. In addition, the EC errs in its attempt to discredit the evidence relied upon by the United States. The EC incorrectly suggests that the United States based its assessment of Deutsche Airbus's equity-worthiness solely on an assessment of the financial condition of the company's parent (MBB). While noting the dire state MBB was in when Daimler invested in MBB, the United States pointed in particular to the financial distress that Deutsche Airbus was in at the time and was expected to be in for the foreseeable future.

63. To make its case with respect to the French infusions, the EC relies on evidence such as statements by management (rather than potential private investors) and *ex post* information about returns supposedly realized on those investments. The EC does not provide any evidence of contemporaneous studies or analyses by the French government on the investment prospects of Aérospatiale. It also looks selectively at indicators of financial performance, ignoring Aérospatiale's abysmal balance sheet, its troublesome financial ratios, and the poor prospects it would have faced if it had not received very significant additional government financing.

64. With respect to the French government's December 1998 transfer to Aérospatiale of its 45.76 percent equity stake in Dassault Aviation, the EC argues, first, that "nothing of economic significance occurred," because the French government effectively did nothing more than transfer its Dassault shares to itself. Second, the EC argues that when Aérospatiale was later combined with Matra Hautes Technologies to form ASM, the value of its "45.76 percent stake in Dassault was fully captured in the price charged for ASM shares in the public offering that took place in 1999." Neither argument is correct. The problem with the EC's first argument is that it assumes that the relevant point of view is that of the government rather than that of Aérospatiale. Moreover, the EC's assertion that "nothing of economic significance occurred" is belied by the fact that in order to persuade the private owners of Dassault to consent to what amounted to a tie-up with Aérospatiale, the French government had to give up the valuable double voting rights associated with its shares in Dassault.

65. As for the EC's second argument, the EC ignores that the French government received no compensation for giving up voting control in Dassault. Also, the price charged for ASM shares in the 1999 public offering was based not on independent "fairness opinions," but on valuations by investment banks (post-dating the actual Dassault transaction) that sought to ratify a previously identified outcome.

66. **Research and development funding:** The EC admits that Airbus has received Euro 648.9 million in R&D subsidies. However, that number understates the amount actually received, as it reflects an arbitrary determination that certain recipients of LCA-related R&D subsidies are “relevant companies” and others are not. Adding back in the amounts the EC arbitrarily excludes, the total R&D subsidies Airbus actually has received under both the EC Framework Programs (FPs) and national and regional programs likely exceeds Euro 3 billion.

67. Further, the EC responds to the U.S. showing that FP grants are specific by arguing that “{t}he Second, Third, Fourth and Fifth Framework Programmes do not have sub-budgets specific to the aeronautics industry.” The EC does not dispute the existence of such a sub-budget in the Sixth Framework Programme. With respect to the Second through Fifth Framework Programs, the EC seems to be arguing semantics. Although it does not acknowledge the existence of formal “sub-budgets,” it does seem to acknowledge that the programs “allocate . . . portions of their budget to research activities such as ‘aeronautics and space’ or ‘aeronautics.’”

68. In addition to making a semantic argument, the EC argues that specificity should be analyzed not at the level of the sub-budget but at the level of the entire Framework Program. Accepting that argument, however, would lead to absurd results. A Member could make virtually any subsidy to “certain enterprises” non-specific simply by formally joining it under one roof with other subsidies to other certain enterprises and calling the combined subsidies a “program.” The SCM Agreement does not support such a formalistic approach. Finally, with respect to the *de facto* specificity of aeronautics R&D grants under the Framework Programs, the relevant numbers show predominant use by Airbus (as well as showing Airbus’s receipt of disproportionately large amounts of FP aeronautics funding).

69. With respect to R&D subsidies provided by member State governments, the EC admits certain grant amounts but asserts that other amounts are “not relevant.” As it gives no explanation for its assertion of what is relevant and what is not, its argument should be rejected.

70. In the case of grants under Germany’s LuFo program, the EC contends that certain amounts are not relevant because they were only committed but not yet received by July 1, 2005. However, a subsidy within the meaning of Article 1 of the SCM Agreement includes “potential direct transfers of funds” as well as an actual direct transfer of funds. Thus, even if the EC were correct in its characterization of the grants at issue, that would not be a basis for excluding those amounts from the Panel’s consideration.

71. The EC argues that the United States has not shown that loans provided to Airbus by the Spanish government under the PTA program confer a benefit on Airbus because the United States has not performed a comparison to a market benchmark. However, in view of the terms of the loans as demonstrated by the United States, they are, by definition, preferential to terms available in the market. The EC also errs in arguing that loans provided by Spanish authorities under the PROFIT program are outside the Panel’s terms of reference, as such loans plainly were covered by the U.S. panel request. The EC’s argument that PROFIT loans are not specific is equally erroneous. As with the EC Framework Programs, the EC mistakenly argues that for

specificity purposes, PROFIT should be analyzed at the level of the broad “umbrella” under which it is implemented, rather than at the individual program level.

72. With regard to the UK’s Technology Programme, the EC itself has acknowledged that the program is sub-divided into 43 “research themes” targeting a limited set of industries. Each of the research themes has its own budget and tends to be highly industry-specific. The R&D funding provided to Airbus and the aeronautics industry under the Technology Programme is therefore specific within the meaning of Article 2.1 of the SCM Agreement.

73. **Subsidies have not been “extinguished” or “extracted”:** The EC’s theory of how subsidies to Airbus were either “extinguished” or “extracted” is deeply flawed. The EC sought to rely on panel and Appellate Body reports from disputes in the countervailing duty (“CVD”) context concerning the effects of a full privatization on pre-privatization subsidies. Those reports stand for the proposition that, in the CVD context, a full privatization may result in the extinction of pre-privatization subsidies where the privatization involves the sale of all or substantially all of the subsidized entity, at arm’s length and for fair market value, and where the seller relinquishes control of the entity. Since the transactions cited by the EC do not meet these criteria, the reports do not help the EC’s argument.

74. The EC’s “extinction” argument is based on four sets of transactions: (i) the 1999 corporate tie-up between Aerospatiale and Matra Hautes Technologies (“Matra”); (ii) the 2000 creation of EADS; (iii) the exercise by BAE of its put option in 2006; and (iv) the offerings of small portions of EADS shares between 2000 and 2007. By the EC Commission’s own admission, the transactions resulting in the creation of EADS and Airbus SAS did not “affect the quality or nature of control of Airbus.” They represented nothing more than “a restructuring and rationalisation of the existing legal partnership between the parties {that previously had coordinated their Airbus activities through Airbus GIE}.” Moreover, it is telling that when asked how it responds to the U.S. statement that “{n}one of {the pertinent} transactions involved a transfer of ‘all or substantially all’ of the subsidized entity to private interests,” the EC simply ignored the phrase “all or substantially all.”

75. Turning to the particular transactions at issue, first, several of the transactions occurred well after the establishment of this Panel and, therefore, have no bearing on the resolution of this dispute. Second, several of the transactions are not even actual sales of shares. Third, all of the post-panel-establishment transactions and all but one of the remaining transactions that the EC argues “extinguished” parts of the subsidies to Airbus concern between 1% and at most 9.95% of the shares in the entities concerned. In other words, they involved significantly less than “all or substantially all” of the shares of those entities. Fourth, none of the transactions cited by the EC resulted in the seller “no longer {having} any controlling interest” in the company at issue. Finally, the EC has in no way demonstrated that the transactions it cites occurred at arm’s length and for fair market value.

76. As for the EC’s “extraction” theory, first, while the EC makes vague references to “{t}he WTO treatment of change of ownership,” “the test for cash extraction,” and “the established WTO rules,” it never states where in the SCM Agreement this “treatment,” “test,” or “rules” can be found. It does not do so because it cannot do so. Second, the EC asserts that “the test for

cash extraction is a ‘but for’ test,” even though the agreement contains no such test, and elsewhere the EC has insisted on interpreting and applying the language actually used in the agreement. Third, as there is no treaty text to support its argument, the EC refers instead to what it calls “economic common sense,” but provides no citation to a textbook or any other support for this “economic common sense.” In effect, the EC invents a special accounting rule whereby, when a subsidized entity transfers cash to the account of its owner, the transferred money is first attributed to any subsidies provided to the entity and is attributed to non-subsidized investment only after the amount transferred equals the amount of pre-transfer subsidies.

77. More fundamentally, the EC’s “extraction” theory relies on a supposed separation between a company and its shareholders – the very separation that the EC successfully opposed in *US -Countervailing Measures*. If it is the case that money taken out of an owner’s pocket amounts to money taken out of the company, potentially eliminating subsidies that reside in the company, then the converse must also be true: Money that is simply moved from the company to the owner’s pocket has not really left the company-shareholder unit. Indeed, following the EC’s logic, it would seem that a company “extracts” subsidies every time it buys back stock or pays dividends to its shareholders – both types of transactions that involve a transfer of cash from the company to its owners. Yet, if this were so, then opportunities to circumvent the SCM Agreement would abound.

78. Finally, the EC seems to argue that the transfers of cash from CASA to the government of Spain and from DASA to DaimlerChrysler were analogous to repayments of subsidies and thus constituted withdrawals of subsidies within the meaning of Article 4.7 and 7.8 of the SCM Agreement. However, the EC ignores an important distinction between these transactions and actual repayments of subsidy. When withdrawal of a subsidy is effectuated by repayment, the government that provided the subsidy in the first place receives cash from the subsidized entity and gives up nothing in return. That is not what happened in the CASA and DASA transactions. Both the government of Spain and Daimler gave something up in the sense that they received smaller stakes in EADS than they would have received if the cash transfers had not occurred.

79. **Launch Aid profoundly distorts competition in LCA markets:** With respect to launch decisions, the EC’s attempt to rebut the economic model of Dr. Gary Dorman fails, and in any event, the EC has chosen not to contest that Launch Aid was decisive in most of Airbus’s key launch decisions. The economist selected by the EC to review Dr. Dorman’s model, Dr. Wachtel does not consider the particular importance that economies of scale play in the LCA industry. As a 1995 study for the British government states, “scale economies are so important in this technology that, if a producer enters a market at all, it will always do so at a scale of production that makes a significant difference to its competitors’ sales.”

80. The EC claim in this dispute that Launch Aid was not necessary for the launch of the A380 is contradicted by the evidence. For example, the stated policy of the UK government is to provide Launch Aid only if the recipient demonstrates, *inter alia*, “that Government investment is essential for the project to proceed on the scale and in the time-scale specified in the application.” For the French government, the problem was “above all” the crushing financial impact of private financing for the A380, even assuming it could be found, on the balance sheet of Airbus.

81. The EC response to the U.S. demonstration of the distorting effects of Launch Aid is *not* to contend that Launch Aid has had no impact on Airbus's launch decisions. Rather, the EC contends that the United States, by arguing that subsidies created the existing supply, in fact argues that Boeing should have a monopoly in the LCA market; it then rebuts this straw man by arguing that even without the subsidized Airbus entry, there would have been another competitor with exactly the same product line as Airbus. The EC argument is pure speculation devoid of evidentiary support.

82. The effect of Launch Aid on prices of aircraft after they are launched is a second and *independent* economic distortion of the LCA market caused by Launch Aid. Because the subsidies have been instrumental in creating Airbus's LCA product family, they necessarily create supply-side pressure on market prices. Further, the impact of Launch Aid on the overall financial performance of Airbus allows Airbus to keep to an aggressive launch schedule, while simultaneously following its publicly stated policy of pursuing market share, even at the cost of short-term profitability.

83. The EC further complains that the United States has not demonstrated that the subsidies have caused adverse effects because it fails to quantify with precision the benefit that Launch Aid provides to Airbus and asserts that the magnitude of the benefit of Launch Aid and certain other subsidies is too small to produce significant adverse effects. The EC's contention is incorrect for several reasons. First, the United States is under no obligation to provide a detailed quantification and allocation of the subsidy benefit. Second, the EC's attempt to show a small current benefit from Launch Aid is riddled with significant errors. Finally, any reasonable calculation of the magnitude of the subsidy demonstrates that it is – contrary to the EC's claims – very large.

84. The EC also asserts that many LCA sales do not involve "competition" between Airbus and Boeing, and that where sales are not "competitive" there is no possibility for subsidies to cause adverse effects. The EC definition of a "competitive" sale, however, excludes many sales in which price competition between Airbus and Boeing is highly relevant. A customer may not conduct a formal bidding process, but only if it believes that it is getting a market price. If a customer thinks that holding a competition will drive down the price, it will do so.

85. Subsidies other than Launch Aid, when provided in combination with Launch Aid, have the effect of amplifying and reinforcing to the market-distorting impact of Launch Aid. To the extent that these subsidies to Airbus have effects that are complementary to Launch Aid, their effects should be considered together with Launch Aid.

86. **There is one subsidized product (Airbus LCA) and one like product (Boeing LCA):** Launch Aid benefits the Airbus family as a whole in at least six ways: (1) it enables Airbus to be present in all segments of the LCA market, as the EC agrees any competitive LCA producer must; (2) technologies or production facilities developed as part of the launch of one Airbus LCA model are used for other models; (3) Airbus uses "commonality," or common elements among different LCA models that reduce the cost of operating multiple Airbus LCA models, as a central feature in selling the entire Airbus LCA fleet to customers; (4) Airbus uses one Airbus

LCA model to sell other LCA models in “package” deals, either simultaneously or consecutively; (5) Launch Aid reduces the debt burden on Airbus of building each individual LCA model, which in turn allows Airbus to move on to launch the next model much more easily and quickly; and (6) Launch Aid provides Airbus with additional cash flow that allows it to reduce prices of any LCA model whenever it concludes that a price reduction is necessary to capture orders that would otherwise have gone to Boeing. Thus, each provision of Launch Aid benefits the entire Airbus LCA family and has adverse effects on the entire like Boeing family. Accordingly, the “subsidized product” for each of the subsidies, and for all of the subsidies taken together, is Airbus LCA.

87. The EC argues that not every Airbus LCA model is “like” every other Airbus LCA model or every Boeing LCA model. The EC confuses the identification of the “like product” with the identification of the “subsidized product.” This confusion is particularly evident in the EC’s discussion of the panel report in *Indonesia – Autos*, where the identity of subsidized product was undisputed. Indeed, the reasoning of the *Indonesia – Autos* panel, which defines the “like product” narrowly with respect to the “subsidized product,” would support a *broader* approach to the definition of the “subsidized product.”

88. Even if it were useful or reasonable to divide the LCA market into a number of submarkets, the EC proposed division is not supported by the evidence. And even if the Panel were to find any merit whatsoever in the EC market segmentation, the EC contention that no Airbus models compete with the Boeing 747 is manifestly erroneous.

89. **The reference period should include data prior to 2004:** The EC contends that the appropriate starting point for the Panel’s adverse effects analysis is 2004, not 2001. The 2001-2003 period was not aberrational, as the EC claims; if anything, it is the increase in LCA demand in 2005 and 2006 that is historically anomalous. Moreover, if the EC were correct in its contention that changes in market share from 2001 to 2003 were due to temporary phenomena unrelated to subsidization, one would expect the relative market shares of Boeing and Airbus to return to their “normal” levels after the market recovered in 2004. Yet this has not occurred.

90. Indeed, the LCA market and industry operate under unusually long time horizons. It takes several years to develop a new aircraft and bring it to market. Similarly, LCA sales typically are for deliveries over several years with options to purchase additional aircraft over a time frame that is longer still. The subsidies at issue are long-term loans intended to fund the launch of LCA that are produced and sold over a period of decades; any measurement of their effects must therefore take into account their long-term nature.

91. **The EC’s focus on market developments after Panel establishment is legally and factually misplaced:** The United States has demonstrated the validity of its claim, set forth in its request for the establishment of this Panel, that the challenged subsidies have caused adverse effects to the interests of the United States. The EC has chosen not to rebut this showing. Instead, the EC contends that the only question for the Panel is whether the adverse effects referred to in the U.S. panel request have ceased to exist. Most of the trends that demonstrate the adverse effects to the interests of the United States over the 2001-2005 period have continued

unabated through 2006 and, to the extent data are available, into 2007. Where the trends show small improvements in 2006 when compared to 2005, these are largely due to temporary factors such as the 2006 delays in A380 production and A350 design rather than any elimination of the effects of the subsidies. In any event, the EC's exclusive focus on data for 2006 shows that it cannot contest that adverse effects had existed in the period through 2005; the EC certainly makes no effort to do so.

92. However, the EC argument is also legally incorrect. In *EC – Biotech*, the EC asked the panel to decline to rule on a disputed measure on the basis that the measure had allegedly ceased to exist after the establishment of the panel. The panel refused, finding that (1) it had the authority to make findings on the WTO-consistency of the measure even if it had ceased to exist subsequent to the establishment of the panel, (2) that such findings would help “secure a positive solution” to the dispute, and (3) that it did not need to make findings on whether the measure was still in existence in order to make the recommendation required by Article 19.1 of the DSU. The reasoning of the *Biotech* panel applies equally in the present dispute.

93. **The EC focus on orders rather than deliveries is erroneous:** The EC agrees that the ordinary meaning of the terms “imports” in Article 6.3(a) and “exports” in Article 6.3(b) carries “the notion of movement of goods.” As contracts for the future “movement of goods,” orders are certainly relevant to an analysis of likely *future* trends in the LCA market, but the “movement of goods” that has actually occurred and is now occurring is captured by data on actual deliveries. Moreover, an exclusive analytical focus on *order* data leads to factually inaccurate conclusions, particularly in third-country markets where there are a relatively small number of transactions. This can be seen, for example, in an examination of the LCA market in Mexico.

94. **Existence of serious prejudice: Displacement and impedance in the EC market:** Airbus increased its market share in the EC LCA market by 9 percentage points from 2001 to 2005, when measured by total volume of LCA delivered and maintained all of its increased market share in 2006. The EC fails to respond to the U.S. argument; instead it segments and breaks up the data in a way that magnifies random fluctuations and obscures trends. The data speak for themselves – significantly fewer Boeing LCA are being imported into the EC than was the case just a few years ago.

95. **Existence of serious prejudice: Displacement and impedance in third-country markets:** Airbus increased its market share in third-country markets, taken as a whole, by 20 percentage points from 2001 to 2005, when measured by total volume of LCA delivered. Boeing regained only five percentage points of its share of these markets in 2006 and remains well below its share in 2001 and 2002. These markets other than the EC and the United States have grown substantially over the 2001-2005 period and have continued to grow in 2006. Total deliveries by Boeing and Airbus have increased in each year (except for a very small drop from 2003 to 2004). Thus, the shift in market share in third-country markets largely results from Airbus gaining more of the increased demand than Boeing. With respect to particular third-country markets identified in the U.S. first written submission, Boeing's loss of market share to Airbus continued in 2006 in most markets.

96. **Existence of serious prejudice: Lost sales and price undercutting:** From the late 1990s through at least 2005, Airbus won a series of campaigns at major low-cost carriers in the United States, Europe, and Asia. Public and confidential evidence shows that aggressive Airbus pricing was the key factor in Airbus's winning, and Boeing's losing, these key campaigns. Airlines that ordered the A380 would otherwise have expanded their fleets with Boeing LCA. With respect to A340-500/600 sales, the EC argues that Airbus had the right plane at the right time, while Boeing did not. Once again, however, this concedes the causal link; in the absence of Launch Aid, Airbus would not have been in a position to offer what it claims was the right plane at the right time. The evidence therefore confirms that the significant lost sales identified by the United States were lost primarily because of subsidies.

97. **Existence of serious prejudice: Price suppression and depression:** Prices for Boeing LCA in the world market fell, or failed to rise in keeping with cost inflation, in the period from 2001-2005. Despite two years of unprecedented high demand for LCA, prices for the Boeing 737, 747, and 767 continued to be seriously depressed in 2006. Aggressive Airbus pricing has altered price expectations of customers in the market and continues to prevent prices from rising. Price trends for the 777 were somewhat different both in 2001-2005 and in 2006. That the price suppression and depression is the effect of the subsidy is confirmed by the fact that the effect of price suppression and depression recedes first – and, so far, only – where Airbus's product offering has proven the weakest and at the time when Airbus's ability to leverage its subsidies to lower price to offset the difference is most strained.

98. **Existence of material injury:** Airbus increased its market share in the United States by 18 percentage points from 2001 to 2005. Boeing regained only five percentage points in 2006. Both Airbus and Boeing have been affected by the decline in overall LCA demand in the U.S. market. Indexed pricing data shows that 737 prices in the U.S. market remained depressed in 2006. The EC discusses at length the improvement in Boeing's financial condition in 2006 (while neglecting to mention that Airbus, too, had record deliveries and performance in the same year) and argues that, whatever may have been the case in the past, Boeing cannot be said to be experiencing material injury at the present time. However, the relevant question for an adverse effects claim under the DSU and the SCM Agreement is whether the EC was in breach of its obligation under Article 5(a) when the Panel was established. Moreover, the improvement in the financial condition of Boeing must be placed in the context of unusually high demand in 2005 and 2006 in this cyclical industry. Indeed, the events of 2006 demonstrate how significantly relief from subsidized competition improves the fortunes of the U.S. LCA industry.
