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

(WT/DS316)

**ANSWERS OF THE UNITED STATES OF AMERICA
TO THE PANEL'S QUESTIONS IN CONNECTION WITH
THE SECOND SUBSTANTIVE MEETING**

November 16, 2007

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<i>US – Countervailing Measures (Panel)</i>	Panel Report, <i>United States – Countervailing Measures Concerning Certain Products from the European Communities</i> , WT/DS212/R, adopted 8 January 2003, as modified by the Appellate Body Report, WT/DS212/AB/R
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<i>US – Lead Bars (Panel)</i>	Panel Report, <i>United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom</i> , WT/DS138/R, adopted 7 June 2000, as modified by the Appellate Body Report, WT/DS138/AB/R
<i>US – Lead Bars (AB)</i>	Appellate Body Report, <i>United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom</i> , WT/DS138/AB/R, adopted 7 June 2000
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<i>US – Softwood Lumber CVD Final (AB)</i>	Appellate Body Report, <i>United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada</i> , WT/DS257/AB/R, adopted 17 February 2004
<i>US – Wheat Gluten (AB)</i>	Appellate Body Report, <i>United States – Definitive Safeguard Measures on Imports of Wheat Gluten from the European Communities</i> , WT/DS166/AB/R, adopted 19 January 2001
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*European Communities and Certain Member States –
Measures Affecting Trade in Large Civil Aircraft (DS316)*

**Answers of the United States to the Panel’s Questions in Connection
with the Second Substantive Meeting**

November 16, 2007

I. QUESTIONS TO THE UNITED STATES¹

A. LAUNCH AID / MEMBER STATE FINANCING (“LA/MSF”)

136. Is the Panel correct in understanding, from paragraph 39 of the United States second non-confidential oral statement (“SNCOS”), that the United States considers that it is not necessary to show the precise content of the alleged launch aid programme nor to show that it is a measure of general and prospective application in order to establish that the measure exists?

Response

1. Showing the precise content of the Launch Aid Program and showing that the Launch Aid Program has general and prospective application are relevant factors that could help establish that the Launch Aid Program is a measure. However, it is not the case that the test for establishing that the Launch Aid Program is a measure is as it has been alleged by the European Communities (“EC”).

2. At paragraph 39 of its second non-confidential oral statement, the United States assumes for the sake of argument that the test for showing that the Launch Aid Program is a measure distinct from individual grants of Launch Aid is as alleged by the EC. According to the EC, to establish that the Launch Aid Program is a measure, the United States must show the Program’s precise content and that it has general and prospective application.² The EC derives this test from the report of the Appellate Body in *US - Zeroing (EC)*.³

¹ General note regarding citations: In the following responses to the Panel’s questions, all references to oral statements are to the “as delivered” versions of those statements. Additionally, references to the EC’s responses to questions from the Panel following the first substantive meeting with the parties (“EC Responses to First Panel Questions”) are to the revised version of those responses filed on July 6, 2007. The United States clarifies this point, because there is a discrepancy in paragraph numbering between the originally filed (April 30, 2007) version of the EC Responses to First Panel Questions and the revised (July 6, 2007) version of that document. Beginning with paragraph 60, the EC removed certain text which it placed in an HSBI appendix. The result is a five-paragraph numbering discrepancy, beginning with paragraph 60.

² See EC First Written Submission (“FWS”), para. 343; EC First Confidential Oral Statement (“FCOS”), para. 2; EC Second Written Submission (“SWS”), para. 107.

³ See, e.g., EC SWS, para. 107 (quoting *US - Zeroing (EC) (AB)*, para. 198).

3. At paragraphs 39 to 52 of its second non-confidential oral statement, the United States explained that even assuming that the EC has correctly identified the test for establishing that the Launch Aid Program is a measure, the United States has met that test: It has shown the precise content of the Launch Aid Program, and it has shown that the Launch Aid Program has general and prospective application. As a threshold matter, however, the United States disagrees with the EC's asserted test for demonstrating that the Launch Aid Program is a measure. Rather, establishing that the Program is a measure should be based on the ordinary meaning of the term "measure" in context and in light of the object and purpose of the WTO Agreement.⁴ In applying that standard, the Panel should consider the relevant evidence and draw logical conclusions from that evidence.

4. In its report in *US - Zeroing (EC)*, the Appellate Body discussed factors that should be established in bringing an "as such" challenge "against a 'rule or norm' that is *not* expressed in the form of a written document."⁵ As the United States explained at paragraphs 33 to 37 of its second non-confidential oral statement, its challenge against the Launch Aid Program is not what is commonly referred to in WTO dispute settlement as an "as such" challenge; that is, it is not a challenge that something about the Launch Aid Program mandates or necessarily results in the breach of a covered agreement obligation each time the Program will be applied in the future. The U.S. challenge is that the Launch Aid Program is a measure that currently is breaching EC obligations under the *Agreement on Subsidies and Countervailing Measures* ("SCM Agreement") by causing adverse effects to the interests of the United States. Because the U.S. challenge is not an "as such" challenge, the Appellate Body's identification of "the criteria for bringing an 'as such' challenge"⁶ does not provide the relevant test.

5. Indeed, in other disputes, panels have found unwritten measures to exist without applying the test the EC alleges to be applicable here. For example, in *EC - Biotech*, the panel found the EC's *de facto* moratorium on the approval of biotech products during the period October 1998 to August 2003 to be a challengeable measure.⁷ To reach that finding, the panel did not apply the test the EC now identifies. Instead, it examined all of the evidence, drew logical conclusions from that evidence, and found the moratorium to be a measure, based on the ordinary meaning of the term "measure" in context and in light of the object and purpose of the covered agreement.⁸

⁴ See *Vienna Convention on the Law of Treaties*, Art. 31(1).

⁵ *US - Zeroing (EC)* (AB), paras. 197-198.

⁶ *US - Zeroing (EC)* (AB), para. 203.

⁷ *EC - Biotech*, paras. 7.456, 7.1271-7.1285, 7.1292-7.1295.

⁸ See, e.g., *EC - Biotech*, paras. 7.1271-7.1272.

While it discussed the moratorium's general applicability, it did not discuss prospective applicability, contradicting the EC's assertion that the latter factor is part of the relevant test.⁹

6. In *Japan - Semi-Conductors* (the GATT panel report cited in the *EC - Biotech* report), the panel took a similar approach to establishing the existence of an export restriction in breach of Article XI:1 of the GATT 1947.¹⁰

7. This Panel should take a similar approach to determining that the Launch Aid Program is a measure in its own right, distinct from individual grants of Launch Aid. In taking that approach, the Panel logically should consider the measure's content, which the United States has demonstrated to consist of the consistent provision, for each major new Airbus large civil aircraft ("LCA") model, of long-term, unsecured financing at zero or below-market rates of interest, with back-loaded repayment schedules that allow Airbus to repay, if at all, through levies on deliveries of the financed aircraft.¹¹ The Panel also could consider the measure's general and prospective application, which the United States also has demonstrated.¹² This additional factor would support the conclusion that the Launch Aid Program is a measure in its own right. However, the Panel is not required to consider this factor.

8. In sum, the point the United States emphasized in its second non-confidential oral statement was that the standard for determining whether the Launch Aid Program is a measure is not the EC's asserted test, but a standard based on the ordinary meaning of the term "measure" in context and in light of the object and purpose of the WTO Agreement, which standard must be applied based on the facts. Following this standard, even if the Panel disagreed with the United States that the Launch Aid Program has general and prospective application, it still should find that the Program constitutes a challengeable measure, based on the totality of the evidence.

137. Assuming the Panel concludes it is necessary to determine whether the alleged "launch aid programme" is prospective in nature, could the United States explain on what basis it argues that this criterion is satisfied?

Response

⁹ See *EC - Biotech*, para. 7.1272. Indeed, the panel referred to evidence indicating a lack of prospective applicability, inasmuch as there had been a departure from the moratorium after August 2003, while the panel proceedings were underway. See *id.*, para. 7.1271(c).

¹⁰ GATT Panel Report, *Japan - Trade in Semi-Conductors*, paras. 109-117, L/6309 - 35S/116 (adopted May 4, 1988).

¹¹ See U.S. FWS, paras. 91-164; U.S. First Non-Confidential Opening Statement ("FNCOS"), paras. 19-26.

¹² See U.S. Responses to First Panel Questions, paras. 25-41; U.S. SNCOS, paras. 39-52; U.S. Second Confidential Opening Statement ("SCOS"), paras. 8-11.

9. As discussed in response to Question 136, it is not necessary for the Panel to determine that the Launch Aid Program is prospective in nature in order to find that the Program constitutes a measure. However, if the Panel were to find that such a showing is necessary or helpful to its analysis, ample evidence demonstrates that the Program is prospective. That evidence consists of the institutional apparatus established to administer the Launch Aid Program, statements by Airbus government officials, statements by Airbus itself, and statements by market actors showing their expectation of the Launch Aid Program's continuity as a fixture in the financial landscape in which Airbus operates.

10. A measure has prospective application if it is intended to apply to situations occurring after the measure comes into existence.¹³ Also relevant to assessing prospective application is whether the measure "creates expectations among the public and among private actors."¹⁴ The Launch Aid Program exhibits both of these qualities.

11. Clear evidence demonstrating that the Launch Aid Program has prospective application includes the series of inter-governmental agreements, beginning with the Program's origins in the 1969 agreement between France and Germany regarding the launch of Airbus's A300-B, in which the governments affirm their commitment to "reinforce European cooperation in the field of aeronautics."¹⁵ That commitment expressly looks beyond support for a single model. Indeed, subsequent commitments of support – up to and including the governments' most recent, legally binding commitments to provide Launch Aid for the A350¹⁶ – build upon the original 1969 commitment and show the Program to be one of prospective application.

12. Further demonstrating the prospective application of the Launch Aid Program is the complex national and international institutional apparatus established to support the Program.¹⁷ The very existence of this bureaucracy shows the Airbus governments' intent to use Launch Aid consistently to support Airbus. In its opening statement at the second substantive meeting of the Panel, the United States illustrated this point by quoting from the stated mission of the French

¹³ See *US - OCTG from Argentina* (AB), para. 187 (explaining that U.S. Department of Commerce Sunset Policy Bulletin is "intended to have prospective application, as it is intended to apply to sunset reviews taking place after its issuance").

¹⁴ *US - OCTG from Argentina* (AB), para. 187.

¹⁵ U.S. FWS, para. 93 (quoting 1969 agreement, preamble (Exhibit US-11)); see also U.S. SNCOS, para. 43.

¹⁶ See U.S. FWS, para. 94 and footnote 85.

¹⁷ See U.S. FWS, paras. 95-101; U.S. SNCOS, paras. 43-45.

government's special unit on "transport aircraft of more than 100 seats."¹⁸ A fuller quote from that mission statement further reinforces the prospective application of the Launch Aid Program:

It deals with requests for reimbursable advances . . . and it prepares the decisions and the draft financial agreements that accompany them. . . .

It follows technical progress, and industrial and commercial progress of the {aircraft} programs and manages the protocols, particularly with respect to the provision of advances from the State and their reimbursement. . . .

It prepares, negotiates and applies the intergovernmental agreements that set the conditions according to which the programs . . . are financed and managed, to the extent that they are managed in the context of international cooperation. It participates in the work of the intergovernmental bodies put in place to this end.¹⁹

13. Moreover, statements by the European Commission and the Airbus governments bolster the conclusion that the Launch Aid Program is a measure of prospective application. As the European Commission explained in defending the governments' commitment of Launch Aid for the A350, Launch Aid is "part of the commercial landscape of aircraft development in Europe."²⁰ That view has been echoed repeatedly by heads of State and government who, like former French Prime Minister de Villepin, have made clear that "the State will fully play its part"²¹ in the long-term success of EADS and Airbus.²²

14. Indeed, Airbus has come to rely on each government "fully play{ing} its part." This was summed up when Airbus's CEO stated recently, "We are not putting away refundable launch investment."²³ Or, as another Airbus spokesman put it, "Launch aid is the only available system

¹⁸ See U.S. SNCOS, para. 44.

¹⁹ Arrêté du 3 mars 2005 "portant organisation des mission et sous-directions de la direction des programmes aéronautiques et de la coopération de la direction générale de l'aviation civile," JO April 10, 2005, 489a, 496 (Exhibit US-50).

²⁰ U.S. FWS, para. 103 (quoting *EU backs new Airbus aid request, despite US opposition*, Agence France Presse (May 19, 2005) (Exhibit US-60)).

²¹ Gil Bousquet and Jean-Pierre Bédéï, *Interview: de Villepin: "I will remain vigilant"*, La Dépêche du Midi (Nov. 14, 2006) (Exhibit US-638) (quoted at U.S. SNCOS, para. 48).

²² See U.S. FWS, para. 102 (discussing statements by heads of state and government and cabinet officials consistently expressing commitment to support Airbus through Launch Aid).

²³ U.S. FNCOS, para. 23 (quoting AFP, *Airbus weighing up state-backed loans for A350: Gallois* (Mar. 9, 2007) (Exhibit US-449)).

right now.”²⁴

15. Finally, in addition to creating expectations for Airbus, the Launch Aid Program has created expectations among disinterested market actors. It is precisely because of the Program’s prospective application – giving rise to an “expectation for continuing government support, which is primarily in the form of refundable advances for up to 1/3 of the development cost of each new aircraft program at the Airbus level” – that the Moody’s commercial rating service maintained an A3 debt rating for Airbus’s parent company, EADS, in 2003.²⁵ Subsequent reviews by Moody’s and other market actors have confirmed expectations based on the Program’s prospective application.²⁶

16. All of the foregoing evidence demonstrates that the Launch Aid Program has prospective application. Individual provisions of Launch Aid are not merely *ad hoc* measures; they are part of a larger Launch Aid Program, which itself is a measure with an established existence giving rise to expectations separate from each individual grant. While finding prospective application is not necessary to conclude that the Launch Aid Program is a distinct measure, the evidence supports such a finding in the event the Panel believes that finding to be necessary or helpful to its analysis.

138. Could the United States explain the adverse effects it claims are caused by the alleged “launch aid programme”, as distinct from the adverse effects it claims are caused by the individual grants of LA / MSF?

Response:

17. The United States has challenged the Launch Aid Program, as well as the individual disbursements of Launch Aid, primarily because the Launch Aid Program *is* the measure through which each particular Launch Aid disbursement has been made and through which the individual disbursements of Launch Aid have collectively distorted the LCA market and caused adverse effects. Given that the Airbus governments have in fact provided Launch Aid as part of a coordinated program, the United States believes that findings with respect to the Launch Aid Program, as well as individual grants of Launch Aid, would facilitate the resolution of this

²⁴ U.S. FNCOS, para. 23 (quoting Katrin Bennhold, *Airbus looks likely to seek state assistance*, International Herald Tribune (June 19, 2006) (Exhibit US-62)).

²⁵ U.S. FWS, para. 104 (quoting Press Release, *Moody’s Assigns A3 Rating to New Euro Mtn Program of European Aeronautic Defence and Space Company EADS N.V.*, Moody’s Investor Service (Feb. 6, 2003) (Exhibit US-56)).

²⁶ See U.S. FNCOS, para. 24 and footnote 17 (citing evidence); U.S. Responses to First Panel Questions, para. 30.

dispute.

18. As the United States has already explained, there is a distinct benefit to Airbus – and therefore a distinct market effect – that results from the consistent provision of Launch Aid and the perception of an overarching commitment by the Airbus governments to provide Launch Aid as necessary to “give Airbus the means to win the battle against Boeing.”²⁷ Thus, for example, in explaining its high credit ratings for EADS, Moody’s references the consistent provision of Launch Aid rather than any particular instance of it:

Moody’s is comforted by continuing government support in the form of refundable advances of up to 1/3 of the required development expenses for Airbus’ commercial aircraft²⁸

19. Additionally, the knowledge that the Airbus governments will make Launch Aid available to Airbus provides “comfort” to Airbus itself in its internal planning and strategic decisionmaking. As a factual matter, the HSBI and other evidence already discussed by the United States demonstrates that Airbus has, in its launch and other strategic decisions, taken into account the certain availability of Launch Aid well before the formal provision of Launch Aid by the Airbus governments.²⁹

20. As the United States explains in response to Question 139, the incremental benefit of this continuous quality of Launch Aid – particularly the advantageous credit rating resulting in access to private capital on better terms than would otherwise be the case – is properly attributed to the Launch Aid Program. This incremental benefit also contributes to the relief from the full financial consequences of Airbus’s aggressive product development and pricing strategies that, as the United States has already demonstrated, is the effect of Launch Aid and that, in turn, has been the cause of the adverse effects shown to have occurred during the reference period and beyond. In this way, the benefit attributed to the Launch Aid Program makes a distinct contribution to the adverse effects of Launch Aid. Moreover, the Launch Aid Program’s contribution to Airbus’s strategic planning and financial flexibility endures beyond the last grant of Launch Aid, as the market has confidence that future instances of Launch Aid will be forthcoming.

21. Moreover, even if there were no “Launch Aid Program” to which this benefit and effect

²⁷ *Jospin pledges to aid Airbus in fight against Boeing*, Reuters (Mar. 8, 2000) (Exhibit US-1) (quoting then-French Prime Minister Lionel Jospin in speech to Parliament).

²⁸ Moody’s Investor Service Press Release (Feb. 6, 2003) (Exhibit US-56).

²⁹ *See, e.g.*, U.S. SCOS, paras. 51-53; U.S. FWS, HSBI App. Section X; U.S. Response to EC Request for Preliminary Rulings (Nov. 15, 2006), paras. 32-35.

could be attributed, they would have to be attributed instead to the cumulative impact of the individual instances of Launch Aid. However, the systemic and continuous commitment of support by the EC and the Airbus governments is most accurately described as a distinct measure in its own right, and this benefit and effect should be attributed to that measure, the Launch Aid Program.

139. Does the United States consider that the alleged “launch aid programme” comprises a financial benefit separate from any amounts disbursed pursuant to individual LA /MSF contracts? If so, could the United States indicate how much financial contribution it considers is at issue?

Response:

22. The Launch Aid Program is a “financial contribution” within the meaning of Article 1 of the SCM Agreement (distinct from the financial contributions provided pursuant to individual Launch Aid contracts) that confers a benefit on Airbus distinct from the benefits conferred by disbursements pursuant to individual Launch Aid contracts. The Launch Aid Program is “a government practice {that} involves a direct transfer of funds . . . {or} potential direct transfers of funds.” Accordingly, it constitutes a “financial contribution” within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement.³⁰

23. As noted in response to Question 138, the benefit conferred by the Launch Aid Program that is different from the benefit conferred by individual grants of Launch Aid consists primarily of the reduced capital costs that result from the value the financial markets attribute to the Program.³¹ As noted in response to Questions 137 and 138, Moody’s rating service explained its A3 long-term debt rating for Airbus’s parent company, EADS, in 2003 as derived in part from “the expectation for continuing government support, which is primarily in the form of refundable advances for up to 1/3 of the development cost of each new aircraft program at the Airbus level.”³² Moody’s confirmed this explanation in maintaining an A1 rating for EADS’s long-term debt earlier this year.³³ This suggests that absent “the expectation for continuing government

³⁰ See U.S. FWS, para. 109; U.S. SNCOS, para. 36.

³¹ See, e.g., U.S. FWS, para. 146; U.S. SNCOS, para. 36.

³² Press Release, *Moody’s Assigns A3 Rating to New Euro Mtn Program of European Aeronautic Defence and Space Company EADS N.V.*, Moody’s Investor Service (Feb. 6, 2003) (Exhibit US-56).

³³ See Moody’s Investor Service, *Moody’s confirmation of EADS highlights government’s role as odd rescuers* (Mar. 12, 2007) (Exhibit US-450) (discussed at U.S. FNCOS, para. 24). In issuing an “upgrade rating” for EADS in June 2006, Credit Suisse also took account of the Launch Aid Program as part of the financial landscape in which Airbus operates. Thus, Credit Suisse observed, “Supported by a European government launch aid, Airbus has developed an extremely competitive product range, competing with Boeing in all segments following the launch of

support” EADS’s debt rating would not have been as high, which would have made the company’s cost of capital more expensive.

24. Having shown that the Launch Aid Program is a “financial contribution” and identified the benefit thereby conferred, the United States has shown that the Launch Aid Program is a subsidy within the meaning of Article 1 of the SCM Agreement. There is no need to precisely quantify the subsidy. As the Appellate Body explained in *US - Cotton Subsidies*, in an analysis under Part III of the SCM Agreement, “{a} precise, definitive quantification of the subsidy is not required.”³⁴

25. If the Panel, nevertheless, considers it relevant to estimate the amount of financial contribution at issue in the Launch Aid Program as distinct from particular disbursements of Launch Aid under individual contracts, it is possible to show conceptually how this would be done. Given the value attached to “the expectation for continuing government support” in rating EADS’s long-term debt, one could determine a debt rating in the absence of that expectation. The difference between the higher cost of capital associated with a debt rating that excludes “the expectation for continuing government support” (*i.e.*, a less favorable debt rating) and the actual cost of capital associated with the company’s actual debt rating (which includes that expectation) is the amount of financial contribution at issue.

140. At para. 167 of its SWS, the EC states that “to enable an ‘apples-to-apples’ comparison between a MSF loan and a commercial loan, the effective price paid under the MSF loan must reflect the additional obligations for the recipient that would not be present in a commercial loan”. To what extent does the United States consider that any such “additional obligations” should be taken into account by the Panel in its assessment of whether the LA / MSF measures conferred a benefit to the relevant recipients?

Response:

26. As discussed at paragraph 60 of the U.S. second non-confidential oral statement, the EC’s discussion of hypothetical “additional obligations for the recipient” under Launch Aid contracts as compared with commercial loans is extremely vague and not supported by any evidence. The EC alleges that Launch Aid “may impose costs on the recipient that market

the A380 super jumbo, including the B747.” CreditSuisse, *Value versus Risk*, EADS upgrade rating, at 14 (June 15, 2006) (Exhibit US-465).

³⁴ *US - Cotton Subsidies* (AB), para. 467; *see also US - Cotton Subsidies* (Panel), para. 7.1173 (rejecting notion of quantifying subsidy for purposes of serious prejudice analysis because “{b}roader considerations are at play in a serious prejudice analysis than those involved in a countervailing duty sense”).

instruments do not.”³⁵ It later alludes to the possibility that [

]³⁶ However, the EC does not even assert that the Launch Aid contracts do contain such additional obligations, let alone substantiate such an assertion by reference to particular provisions in particular Launch Aid contracts and to corresponding provisions in instruments the EC alleges to be “commercial.”

27. It is well established in WTO dispute settlement that “the burden of proof rests upon the party, whether complaining or defending, who asserts the affirmative of a particular claim or defence.”³⁷ In this dispute, at a very late stage, the EC has asserted as a new defense that Launch Aid “may impose costs on the recipient that market instruments do not.”³⁸ However, it has made no attempt to prove that assertion.

28. Even if the EC had provided evidence to support its allegation that “additional obligations” exist that somewhat offset the benefit conferred by Launch Aid as compared with market-based financing, it would not be appropriate to take these “additional obligations” into account in the Panel’s benefit analysis. Doing so would make a benefit analysis a virtually impossible task. How, for example, would one compare the allegedly [

³⁹

] contained in commercial financing instruments? Or, to take another example, how would one compare the burden associated with applying for Launch Aid with the burden (including the efforts of lawyers, bankers, and others) associated with obtaining financing from the market? Engaging in the exercise the EC proposes would be entirely speculative.

141. At para. 128 of its SWS, the United States asserts that “[m]arket lenders set interest rates without regard to taxes that the recipients may subsequently pay to their governments. Therefore, it would be inappropriate to adjust the actual rates in Launch Aid contracts upward to account for the effects of taxes.” However, as we understand it, the EC argues that taxation returns must be taken into account in respect of government debt because they effectively amount to a return on money loaned in the same way as interest payments (see, e.g., para. 542 of the EC FWS). How does the United States respond to this argument?

³⁵ EC SWS, para. 159 (emphasis added).

³⁶ EC SWS, para. 166 (emphasis added).

³⁷ *US - Wool Shirts (AB)*, p. 14;

³⁸ EC SWS, para. 159.

³⁹ EC SWS, para. 166.

Response:

29. The EC's argument regarding the relevance of alleged tax effects to determining the benefit conferred by Launch Aid is flawed for at least three reasons. First, the argument reflects a cost-to-government approach to analyzing a subsidy benefit, and for this reason alone should be rejected. As the Appellate Body found in *Canada - Aircraft*, the relevant inquiry in an analysis of "benefit" within the meaning of Article 1.1(b) of the SCM Agreement is "whether the recipient has received a 'financial contribution' on terms more favourable than those available to the recipient in the market."⁴⁰ The relevant inquiry is not the cost of the financial contribution to the government. From the point of view of the benefit to Airbus, it is irrelevant that the subsidy provider and the tax collector happen to be one and the same.

30. Second, as the EC itself states, "{T}he level of anticipated return needs to be analysed when the government concludes the MSF contract."⁴¹ However, when the government concludes the contract, it is unlikely to know what Airbus's tax liability (if any) will be. As the EU Council and Commission themselves explained in one countervailing duty determination, a company's tax liability "will depend on many factors, most of which are influenced by commercial decisions made by the company itself."⁴² When the Airbus governments provide Launch Aid, they do not know, for example, what offsets to taxation Airbus will be able to take for factors such as depreciation and the carrying forward of losses from prior years. Therefore, even if taxation were relevant in theory, it could not be taken into account as a practical matter, due to the inability to know Airbus's tax liability at the moment when the government's "level of anticipated return needs to be analysed" – *i.e.*, when the Launch Aid contract is concluded.

31. Third and finally, the EC has provided no evidence to substantiate its taxation argument. As the United States discussed in its second written submission, the EC simply avoided the Panel's Question 71 on this point.⁴³ The EC asserted that Airbus "paid all corporate taxes that were due."⁴⁴ However, it provided no tax returns or other evidence to show the amount of taxes paid and thereby to support its theory that such taxes should be taken into account in analyzing the benefit Launch Aid conferred on Airbus. Thus, even if there were a legal basis for taking

⁴⁰ *Canada - Aircraft (AB)*, para. 157.

⁴¹ EC FWS, para. 461.

⁴² Council Regulation (EC) No. 74/2004 of 13 January 2004 imposing a definitive countervailing duty on imports of cotton-type bedlinen originating in India, OJ L12/1, 17.1.2004, p. 6 (recital 50) (Exhibit US-538) (quoted in U.S. SWS, para. 129). As discussed in the U.S. second written submission, the EC (like the United States) does not take tax consequences into account for purposes of its countervailing duty law. See U.S. SWS, para. 128.

⁴³ See U.S. SWS, paras. 125-126.

⁴⁴ EC Responses to First Panel Questions, para. 107.

taxation into account – which, as noted above, there is not – the EC has not given the Panel an evidentiary basis for doing so.

142. In its SWS, the United States argues that because of the “very substantial uncertainty” attached to any royalty payments “they would play a marginal role, at most, in a commercial lender’s financing decisions” (United States, SWS, para. 122). Thus, the United States submits that the cost of the expected royalty payments in respect of the relevant LA / MSF measures is [], between []. Please explain whether the [] values cited in its SWS refer to any particular LA / MSF measure(s) or whether these values are relevant to each of the challenged measures that contain royalty provisions?

Response:

32. The [] range referred to in paragraph 122 of the U.S. second written submission is the range of royalties per plane provided for in those Launch Aid contracts that provide for royalties after the end of levy-based payments. The only such contracts at issue in this dispute are: []

- The French A330-200 Launch Aid contract provides for a [] royalty to be paid on that portion of the value of each delivered plane after the [] that is attributable to Airbus France.⁴⁵
- The French A340-500/600 Launch Aid contract provides for a [] royalty to be paid on that portion of the value of each delivered plane after the [] that is attributable to Airbus France.⁴⁶
- The French A380 Launch Aid contract provides for a [] royalty to be paid on that portion of the value of each delivered plane after the [] that is attributable to Airbus France.⁴⁷
- The German A380 Launch Aid contract provides for a [] royalty to be paid

⁴⁵ French A330-200 Launch Aid Agreement, Protocole, Art. 6.2, DS316-EC-BCI-0000316, -0000323 (Exhibit US-78 (BCI)).

⁴⁶ French A340-500/600 Launch Aid Agreement, Protocole, Art. 7, DS316-EC-BCI-0000276, -0000304 (Exhibit US-36 (BCI)).

⁴⁷ French A380 Launch Aid Agreement, Protocole, Arts. 7.1-7.3, DS316-EC-BCI-0000249, -0000253 (Exhibit US-75 (BCI)).

on that portion of the value of each delivered plane after the [] that is attributable to Airbus Deutschland.⁴⁸

- The UK A380 Launch Aid contract provides for a [] royalty to be paid on that portion the value of each delivered plane after the [] that is attributable to Airbus UK.⁴⁹

33. In fact, the foregoing nominal royalty percentages overstate the impact that potential royalties would have on an investor's decision to provide financing on terms comparable to those in the Launch Aid contracts. As summarized above, royalties become due only after a substantial number of planes has been delivered, and indeed, after the principal and the below-market interest rates on which the Launch Aid contracts are principally based have been fully repaid. In the case of the UK A380 Launch Aid contract, for example, this means that the royalty provision is [] as Airbus's own A380 Business Case forecasts delivery of a total of 751 A380s over the life of the program.⁵⁰

34. Even for the other Launch Aid contracts at issue, royalties become due only after a number of deliveries that, according to Airbus's and the governments' own forecasts, at best will be achieved only by the very end of the 17-year period described in the EC's ITR report as the life of a plane.⁵¹ A market investor considering financing an LCA launch likely would not take into account the prospect of returns it might receive beyond the anticipated life of the financed model. Indeed, most investors probably would look to recover their investment and make a commercial return over a much shorter period of time.

35. Furthermore, certain of the contracts that provide for the possible payment of royalties in the distant future also expressly limit Airbus's obligation to pay royalties. For example, under both the German and French A380 contracts, []

⁴⁸ German A380 Launch Aid Agreement, Sec. 10.1, DS316-EC-BCI-0000345, -0000361 (Exhibit US-72 (BCI)).

⁴⁹ UK A380 Launch Aid Agreement, Schedule 3, Para. 5, DS316-EC-BCI-0000556, -0000586 (Exhibit US-79 (BCI)).

⁵⁰ See Andreas Sperl, *Status of the A380 programme and way forward*, EADS, Global Investor Forum 2006, at 9 (reporting that the Airbus Business Case forecasts 751 A380 deliveries) (Exhibit US-74); see also U.S. FWS, HSBI App., paras. 12-16.

⁵¹ See U.S. FWS, HSBI App., paras. 12-15, 18, 24; International Trade Resources, *Calculating Magnitude of the Subsidies Provided to the Recipient Entities*, para. 28 (Feb. 5, 2007) (Exhibit EC-13 (HSBI)).

].⁵²

143. As the Panel understands it, the interest rate benchmark proposed by the United States appears to equate the risk that is accepted by the government lenders of LA / MSF with the risk that would normally accepted by venture capitalists. Would the United States agree that returns from venture capital financing are typically obtained through the profits associated with the funded project? If so, how relevant would the use of an interest rate benchmark based on venture capital financing be in the case of LA / MSF contracts which require repayment irrespective of project profitability?

Response:

36. First, the United States wishes to underscore an important point noted in its second non-confidential oral statement: “{T}he U.S. benchmark does not rely on returns to individual venture capital projects. Rather, it relies on the much lower returns – on average, about 16.7 percent – to well-diversified portfolios that contain venture capital investments.”⁵³ This point bears emphasis, given the EC’s caricature of the U.S. benchmark and the confusion created by the EC’s reference to the high average return of almost 700 percent to individual venture capital projects that culminate in public offerings.⁵⁴ The U.S. benchmark bears no resemblance to financing with such returns.

37. Second, while the United States does not dispute that the returns from venture capital financing are typically obtained through profits, that proposition by itself gives an incomplete picture of the risks associated with venture capital financing. In particular, the fact that venture capital returns typically come from profits does not mean that venture capital financing typically takes the form of simple equity (*i.e.*, common stock). It does not. Only 1.9 percent of securities issued in venture capital financing are wholly in the form of common stock.⁵⁵ Most venture

⁵² German A380 Launch Aid Agreement, Sec. 10.1, DS316-EC-BCI-0000345, -0000361 (Exhibit US-72 (BCI)); French A380 Launch Aid Agreement, Protocole, Art. 7.3, DS316-EC-BCI-0000249, -0000253 (Exhibit US-75 (BCI)).

⁵³ U.S. SNCOS, para. 59 (discussing NERA Response to Whitelaw Report, p. 7 (explaining reliance on “the risk premium for a well-diversified investor in both venture capital projects and other, less risky, equity investments represented by a stock market index”).

⁵⁴ See Whitelaw Rebuttal Report, para. 19 (Exhibit EC-656 (HSBI)).

⁵⁵ See NERA Response to Whitelaw Report, p. 10 (Exhibit US-534 (HSBI)); Steven N. Kaplan and Per Stromberg, “Financial Contracting Theory Meets the Real World: An Empirical Analysis of Venture Capital Contracts,” 70 *Review of Economic Studies*, 281, 284 (2003) (Exhibit US-653). The 1.9 percent figure is the sum of the categories “Multiple classes of common stock” (1.4 percent) and “Common stock” (0.5 percent) in Table 1 at page 284.

capital securities (79.8 percent) take the form of convertible preferred stock. Other forms of venture capital financing include combinations of common stock and convertible preferred stock, straight preferred stock, and convertible debt.⁵⁶

38. These other forms of venture capital financing would have priority over common stock in the event of a company's insolvency and thus bear less risk than common stock. These securities also typically have redemption rights, which allow the venture capitalists to demand that the firm redeem the investments at their liquidation value after a certain period of time.⁵⁷ In sum, while returns on venture capital may typically be obtained from profits, a more complete understanding of the risks associated with venture capital financing must take account of these additional features, which tend to lessen risk.

39. Third, and more fundamentally, the proposition that returns from venture capital financing are typically obtained through profits is largely besides the point. In analyzing the benefit conferred on Airbus by Launch Aid, the key question is how the terms of Launch Aid compare with the terms of market-based financing of comparable risk. The risk associated with a type of financing depends only in part on the source of returns. Financing for a group of projects that provides for returns to be paid from profits is not inherently more risky than financing for a single project that provides for returns to be paid through levies on individual sales that may result from the project. Put more bluntly, equity financing is not necessarily more risky than debt financing.⁵⁸

40. Fourth, because it is comparability of risk that ensures an apples-to-apples comparison between Launch Aid and an appropriate market-based benchmark, the use of a benchmark based on well-diversified portfolios that contain venture capital investments is highly relevant. As NERA has explained in its expert reports, the risk profile of an LCA project is quite similar to that of venture capital investments. Put succinctly, "the project-specific, delivery-contingent and non-recourse nature of launch aid gives it equity-like risk exposure to a success or failure of only one aircraft model."⁵⁹

41. Launching a new aircraft model requires huge up-front investments (billions of dollars) to be made early in a project's life cycle, when uncertainty about key variables is high, and with

⁵⁶ See NERA Response to Whitelaw Report, p. 10 (Exhibit US-534 (HSBI)).

⁵⁷ Steven N. Kaplan and Per Stromberg, "Financial Contracting Theory Meets the Real World: An Empirical Analysis of Venture Capital Contracts," 70 *Review of Economic Studies* 281, 291 (2003) (Exhibit US-653).

⁵⁸ See, e.g., U.S. SWS, paras. 109-112; U.S. SCOS, para. 44; NERA Response to Whitelaw Report, pp. 19-21 (Exhibit US-534 (HSBI)).

⁵⁹ NERA Response to Whitelaw Report, p. 19 (Exhibit US-534 (HSBI)).

the prospect of those investments being lost if the project fails.⁶⁰ Launching a typical project financed by venture capital requires similar commitments to be made in an environment characterized by similar uncertainty.⁶¹

42. A government provider of Launch Aid financing assumes a substantial part of the project's risk. Airbus is required to repay the government only upon making a delivery. If it fails to make the forecast number of deliveries, or if there are delays in making deliveries, the government's return will be less than it had anticipated. In these scenarios, the government does not have the option to declare Airbus to be in default. These elements of risk are comparable to the risks faced by an investor that expects its returns to come from the profits generated by a financed project.⁶²

43. Moreover, unlike a provider of venture capital financing, a provider of Launch Aid does not have the prospect of substantial gains in the event the financed project is a success. Even taking into account the possibility that a government provider of Launch Aid may receive royalty payments at some point in the distant future, the potential increase in the government's absolute return is very small.⁶³ While a provider of Launch Aid assumes the risks of a financier whose returns depend on profits, it has no prospect of sharing the rewards.

44. In sum, the proposition that venture capital returns typically come from the financed project's profits does not affect the relevance of well-diversified portfolios that contain venture capital investments as the basis for a benchmark in analyzing the benefit conferred by Launch Aid. What is important in identifying a market benchmark is that the risk associated with the benchmark be comparable to the risk associated with Launch Aid financing. Given the similarities between risks associated with projects typically financed by venture capital and risks associated with the LCA launches financed by Launch Aid, a market benchmark in excess of the 16.7 percent average return identified by the United States would have been justified. The use of a benchmark based on well-diversified portfolios that contain venture capital investments is, in fact, quite conservative.⁶⁴

⁶⁰ See U.S. FWS, paras. 112-115.

⁶¹ See NERA, *Economic Assessment of the Benefits of Launch Aid*, pp. 3-4, 19-20 (Nov. 10, 2006) ("Ellis Report") (Exhibit US-80 (BCI)).

⁶² See U.S. FWS, paras. 116-124; U.S. SWS, paras. 82-88; Ellis Report, pp. 3-4, 19-20 (Exhibit US-80 (BCI)).

⁶³ See U.S. Response to Question 142, *supra*.

⁶⁴ It also should be noted that the validity of the U.S. benchmark is confirmed by various cross-checks, which the United States has discussed at length in prior submissions and statements. See, e.g., U.S. FWS, paras. 158-168 and HSBI App., paras. 4-7; U.S. FCOS, paras. 28-36; U.S. SWS, HSBI App., paras. 2-7; U.S. SCOS, paras.

B. PROHIBITED EXPORT SUBSIDIES

144. Does the United States rely on the same evidence it uses to substantiate the existence of “anticipated exportation or export earnings” to also show that the granting of the alleged subsidy measures was in fact contingent upon export performance?

Response:

45. There is some overlap between evidence demonstrating the existence of anticipated exportation or export earnings and evidence demonstrating that the provision of Launch Aid for the A380, A340-500/600, and A330-200 is tied to such anticipated exportation or export earnings. Evidence demonstrating the “tied to” relationship also tends to demonstrate the existence of anticipated exportation or export earnings.

46. Evidence of the “tied to” element in a demonstration of export contingency is evidence of a relationship between two things – the provision of a subsidy and actual or anticipated exportation or export earnings. It is not surprising that evidence of the relationship will often also be evidence of one or both of the things that are related. This is illustrated, for example, by the panel report in *Australia - Leather*. In that report, the panel considered evidence that “the Australian market for automotive leather is too small to absorb Howe’s production” as relevant both to its finding that the Australian government “anticipated continued and possibly increased exports by Howe” and to its finding that “Howe’s anticipated export performance was one of the conditions for the grant of the subsidies.”⁶⁵ Similarly, in *Canada - Aircraft*, the panel looked at the same evidence to support both its finding of the existence of anticipated exportation or export earnings and its finding of a tie between the provision of subsidies and anticipated exportation or export earnings.⁶⁶

47. In the present dispute, Launch Aid contracts for the A380, A340-500/600, and A330-200 evidence the “tied to” relationship between the provision of Launch Aid and anticipated exportation, and they also evidence the existence of anticipated exportation. Airbus’s commitment to repay Launch Aid on a per-sale basis over a specified number of aircraft sales, when understood in light of information in Airbus’s Global Market Forecasts and the governments’ project appraisals regarding the domestic and worldwide markets for the aircraft,

13-26.

⁶⁵ *Australia - Leather*, para. 9.67; see also *id.*, para. 9.66 (analyzing evidence of Howe’s export orientation to support finding that “continued exports, that is, anticipated exportation, was an important condition in the provision of {financial} assistance”).

⁶⁶ See *Canada - Aircraft (Panel)*, paras. 9.340 - 9.341.

demonstrates the existence of anticipated exportation. The fact that Airbus's commitment is set out in a contract in which it is undertaken in exchange for a commitment by a government to provide Launch Aid demonstrates the existence of a "tied to" relationship between the provision of Launch Aid and the anticipated exportation manifest in Airbus's commitment.⁶⁷ By its very nature, a contract is a reciprocal exchange of obligations in which one party's performance is conditional or dependent on the other party's performance, and the Launch Aid contracts are no exception.⁶⁸ Other provisions in the Launch Aid contracts – such as representations and warranties by Airbus to the government relating to Airbus's ability to fulfill its contractual obligation – reinforce the existence of the conditional or dependent relationship.⁶⁹

48. Likewise, critical project appraisals undertaken by the Airbus governments in connection with the decision to provide Launch Aid for each of the subject models are evidence of both anticipated exportation and of the tie between the provision of Launch Aid and anticipated exportation. The appraisals demonstrate that the governments are aware that the levels of sales over which Airbus is to repay Launch Aid according to the terms of the Launch Aid contracts cannot be attained without exportation; thus they demonstrate the existence of anticipated exportation. At the same time, as the appraisals play a central role in the governments' decisions to provide Launch Aid, they demonstrate the conditional (*i.e.*, "tied to") relationship between the provision of Launch Aid and anticipated exportation.⁷⁰

49. Similar observations can be made about other evidence consisting of information Airbus provided to the governments to facilitate their decisions to provide Launch Aid. This includes Airbus's Global Market Forecasts, its Launch Aid application for the A380 provided to the government of Germany, and its Business Case for the A380. Each of these documents corroborates the existence of anticipated exportation. Equally, in highlighting anticipated exportation as a key part of the case for providing Launch Aid, this evidence reinforces the tie between the provision of Launch Aid and anticipated exportation.⁷¹

50. Likewise, the announcement of the UK government's commitment of Launch Aid for the A380 evidences both anticipated exportation and the tie between the provision of Launch Aid and anticipated exportation. The announcement highlights that Airbus "contributes £1 billion to

⁶⁷ See, e.g., U.S. FWS, paras. 347, 353-357 (A380); paras. 364-365, 373 (A340-500/600); and paras. 378-384 (A330-200).

⁶⁸ See *Canada - Aircraft (AB)*, para. 171 (stating that "tied to" element in footnote 4 of the SCM Agreement "emphasizes that a relationship of conditionality or dependence must be demonstrated").

⁶⁹ See U.S. SWS, paras. 163-209 (citing Launch Aid contract provisions).

⁷⁰ See U.S. FWS, HSBI App., paras. 26-60.

⁷¹ See U.S. FWS, paras. 346, 349-350, 354-357, 366, 380, and HSBI App., paras. 31-32, footnote 34.

the UK's trade balance.”⁷² That statement plainly shows anticipated exportation. The very fact of making the statement in connection with an announcement of a provision of Launch Aid shows the tie between the provision of Launch Aid and anticipated exportation.⁷³

51. As noted above, the United States relies on other evidence primarily to demonstrate the existence of anticipated exportation. Such evidence is not as central as other evidence to the demonstration of a tie, but neither is it irrelevant to that demonstration. Evidence of the export orientation of Airbus is a good example. This evidence adds to the wealth of other evidence demonstrating that the Airbus governments anticipated exportation when they provided Launch Aid for the A380, A340-500/600 and A330-200.⁷⁴ By itself, the export orientation of Airbus would not substantiate a tie between the provision of Launch Aid and anticipated exportation, in view of the second sentence of footnote 4 of the SCM Agreement. However, in conjunction with other evidence, the evidence of Airbus's export orientation helps to substantiate that tie.⁷⁵

145. How does the United States respond to the comment made by Canada, at para. 8 of its third party oral statement, that the contractual terms of repayment (i.e., the contractual performance commitments) in the LA / MSF measures, at most, only show an expectation of export sales.

Response:

52. Canada's comment is incorrect. While Airbus's contractual performance commitments under the Launch Aid contracts do show an expectation of export sales (*i.e.*, anticipated exportation or export earnings), they also show that the provision of Launch Aid is tied to anticipated exportation or export earnings within the meaning of footnote 4 of the SCM Agreement. As discussed in the U.S. second written submission, they show that anticipated

⁷² Press Release, *Byers Announces £530 Million Government Investment in Airbus*, Department of Trade and Industry (Mar. 13, 2000) (Exhibit US-360); *see also Blair Says Airbus A380 will Repay 530 Mln Stg UK Govt Investment*, AFX.com (Jan. 18, 2005) (Exhibit US-361) (quoting British Prime Minister stating that “{t}he export gains {from the A380} will run into the billions of pounds”).

⁷³ *Cf. Canada - Aircraft (Panel)*, para. 9.340 (6th bullet point) (citing as evidence in support of its finding of export contingency a press release by Industry Canada announcing a \$100 million contribution to Pratt & Whitney, in which the Industry Minister cites “generating economic growth and export dollars” among the justifications for the subsidy).

⁷⁴ *See* U.S. FWS, paras. 350, 369-370, 378.

⁷⁵ *See Canada - Aircraft (AB)*, para. 173 (“the export orientation of a recipient may be taken into account as a relevant fact, provided that it is one of several facts which are considered and is not the only fact supporting a finding”) (emphasis in original); *see also Australia - Leather*, para. 9.66 (“While the fact of exportation cannot be the sole determinative fact in the evaluation, in our view, it is clearly a relevant factor in this case, as is the level of exports.”).

exportation or export earnings is an essential precondition to the Airbus governments' provision of Launch Aid for the A380, A340-500/600, and A330-200.⁷⁶

53. In asserting that the contractual link between the provision of Launch Aid and anticipated exportation does not constitute the “tied to” relationship provided for in footnote 4 of the SCM Agreement, Canada is repeating arguments that it made and that the panel and Appellate Body rejected in the *Canada - Aircraft* dispute. For example, it states that “if Airbus failed to make a single export sale of the relevant planes, the Airbus governments would have no recourse against Airbus under these contracts.”⁷⁷ Canada made precisely the same argument in *Canada - Aircraft*.⁷⁸ In rejecting it, the panel explained:

While this argument may be relevant in determining whether a subsidy would not have been granted but for actual exportation or export earnings, we find this argument insufficient to rebut a *prima facie* case that a subsidy would not have been granted but for anticipated exportation or export earnings.⁷⁹

54. The Panel in this dispute should reach the same conclusion. The Launch Aid contracts for the A380, A340-500/600, and A330-200 establish a “tied to” relationship between the provision of Launch Aid and anticipated exportation or export earnings. Accordingly, the provisions of Launch Aid under these contracts are export contingent subsidies prohibited under Article 3 of the SCM Agreement.

55. In ignoring or belittling the relationship between Airbus's performance commitments set forth in the Launch Aid contracts and the governments' provisions of Launch Aid set forth in the same contracts, Canada makes the same critical mistake that the EC makes. Canada's error is especially evident when the comment in paragraph 8 of its oral statement is considered in light of a statement two paragraphs earlier. There, Canada states, without explanation: “{T}he simple fact that the repayment schedules are incorporated into the financial contribution agreements does not make the granting of the alleged subsidies contingent upon export performance.”⁸⁰

⁷⁶ See, e.g., U.S. SWS, paras. 134-143, 163-209; see also U.S. SNCOS, paras. 9-11, 20-22, 28.

⁷⁷ Canada Third Party Oral Statement, para. 7.

⁷⁸ See *Canada - Aircraft (Panel)*, para. 6.251.

⁷⁹ *Canada - Aircraft (Panel)*, para. 9.343. Canada's confusion of a tie to actual exportation or export earnings and a tie to anticipated exportation and export earnings is repeated in other assertions in its oral statement, including its discussion of the *Australia - Leather* panel report and of the concept of “neutrality” as between export sales and domestic sales. See Canada Third Party Oral Statement, para. 6. In this regard, Canada repeats the EC's analytical errors. The United States has discussed these errors in prior submissions and statements. See, e.g., U.S. SWS, paras. 148-160, 236-250; U.S. SNCOS, paras. 13-19.

⁸⁰ Canada Third Party Oral Statement, para. 6.

Thus, Canada, like the EC, sees no relevance in the linking through contract of a government's provision of Launch Aid, on the one hand, to Airbus's commitment to performance that requires exportation, on the other.⁸¹

56. However, this contractual link is a quintessential "tie" between the provision of a subsidy and anticipated exportation or export earnings within the meaning of footnote 4 of the SCM Agreement. As the Appellate Body explained in *Canada - Aircraft*, the "tied to" element in footnote 4 "emphasizes that a relationship of conditionality or dependence must be demonstrated."⁸² That is precisely the relationship established in the Launch Aid contracts. The anticipated exportation reflected in Airbus's performance commitments does not exist independently of the provision of Launch Aid, as Canada's comments seem to suggest. Rather, the provision of Launch Aid (the government's contractual obligation) is conditional or dependent upon Airbus's undertaking of a commitment that it can fulfill only if it exports (Airbus's contractual obligation). As previously noted, this is the essence of the contractual relationship.⁸³

57. The EC admits that "the A330-200, A330-500/600 {sic} and A380 contracts were concluded in the expectation of a significant return to the granting governments."⁸⁴ Thus, there is a relationship of conditionality or dependence – a "tied to" relationship – between the governments' concluding of the contracts in which they provide Launch Aid for these models and their "expectation of a significant return." Airbus's performance obligations under the contracts are a manifestation of that "expectation of a significant return." Due to the levy-based nature of Airbus's repayment obligations, the number of aircraft deliveries that must be made in order to attain a "significant return," and the relative demand for the covered aircraft in the EC and outside the EC, that expectation cannot be fulfilled without Airbus making substantial exports. Accordingly, the conditional/dependent/"tied to" relationship between the provision of Launch Aid and "the expectation of a significant return to the granting governments" is a conditional/dependent/"tied to" relationship between the provision of Launch Aid and anticipated exportation or export earnings.⁸⁵

58. That relationship is reinforced by other provisions of the Launch Aid contracts. For

⁸¹ See generally U.S. SWS, paras. 211-214 (discussing EC's mischaracterization of U.S. argument as an argument that contingency upon export performance results from mere expectation of exports).

⁸² *Canada - Aircraft (AB)*, para. 171.

⁸³ See, e.g., U.S. SWS, paras. 133-143; U.S. SNCOS, paras. 9-11.

⁸⁴ EC FWS, para. 448. The EC mistakenly refers to the "A330-500/600" when it evidently meant the A340-500/600. See also EC Responses to First Panel Questions, para. 48.

⁸⁵ See U.S. SWS, paras. 133-143, 163-167.

example, [

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]

59. [

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60. Examples of other Launch Aid contract provisions substantiating the relationship of conditionality or dependence – that is, a “tied to” relationship – between the provision of Launch Aid and anticipated exportation are detailed in the U.S. second written submission.⁸⁹

146. How does the United States respond to the EC comment (at para. 136 of its SNCOS) that “the United States relies on evidence other than the text of the measure” in advancing its *de jure* export contingency claims?

Response:

61. The EC’s comment at paragraph 136 of its second non-confidential oral statement⁹⁰ rests on the flawed premise that it is impermissible to look beyond the text of the measure at issue to establish that a subsidy is contingent in law upon export performance within the meaning of Article 3.1(a) of the SCM Agreement. That flawed premise rests in turn on a misreading of the

⁸⁶ UK A380 Launch Aid Contract, Art. 3.1.4, DS316-EC-BCI-0000556 (Exhibit US-79 (BCI)); *see also* U.S. SWS, para. 169.

⁸⁷ German A380 Launch Aid Contract, Sec. 1, clause 5), DS316-EC-BCI-0000345 (Exhibit US-72 (BCI)); *see also* U.S. SWS, para. 176.

⁸⁸ German A380 Launch Aid Contract, Sec. 12, clause 3)b), DS316-EC-BCI-0000345 (Exhibit US-72 (BCI)).

⁸⁹ *See* U.S. SWS, paras. 163-209.

⁹⁰ Paragraph 136 of the “check against delivery” version of the EC’s second non-confidential oral statement appears to correspond to paragraph 137 of the “as delivered” version of that statement.

Appellate Body report in *Canada - Autos*. As the Appellate Body explained in *Canada - Autos*, to establish *de jure* export contingency, it is appropriate to consider not only the text of the measure, but also how the measure “actually work{s}.”⁹¹ The EC neglects this point in the incomplete and misleading summary of the *Canada - Autos* report set forth in its second written submission.⁹²

62. *Canada - Autos* concerned a legal regime for the exemption of duty on certain imports of motor vehicles into Canada. As relevant here, the EC and Japan complained about two aspects of that regime. The first concerned a limitation on imports eligible for the duty exemption that was set according to the ratio between a manufacturer’s vehicle production in Canada and its sales in Canada. The effect of the production-to-sales ratio limitation was that the more vehicles a manufacturer exported from Canada, the more vehicles it could import duty-free. The EC and Japan challenged this aspect of the regime as a *de jure* export contingent subsidy inconsistent with Article 3.1(a) of the SCM Agreement.⁹³

63. Additionally, the Canadian duty exemption regime required each manufacturer to meet certain Canadian value added (“CVA”) requirements. The CVA requirements varied from company to company and could be met by aggregating factors including cost of parts produced in Canada and of Canadian origin materials incorporated in motor vehicles, direct labor costs incurred in Canada, manufacturing overhead incurred in Canada, general and administrative expenses incurred in Canada and attributable to the production of motor vehicles, depreciation of machinery and equipment in Canada attributable to vehicle production, and capital cost allowance for land and buildings in Canada used in vehicle production.⁹⁴ The EC and Japan challenged this aspect of the regime as subsidies that were both *de jure* and *de facto* contingent upon the use of domestic over imported goods and therefore inconsistent with Article 3.1(b) of the SCM Agreement.⁹⁵

64. The *Canada - Autos* panel agreed with the EC and Japan that, by virtue of the ratio requirements, the duty exemption was *de jure* export contingent.⁹⁶ The Appellate Body upheld

⁹¹ *Canada - Autos (AB)*, para. 128 (quoted in U.S. SNCOS, para. 27); see also U.S. Responses to First Panel Questions, para. 66 and footnote 66, paras. 70-71.

⁹² See EC SWS, paras. 261-264.

⁹³ See *Canada - Autos (Panel)*, paras. 2.15-2.35, 3.1, 3.3.

⁹⁴ See *Canada - Autos (Panel)*, para. 10.204; *Canada - Autos (AB)*, para. 124.

⁹⁵ The EC and Japan also challenged the duty-exemption regime as a prohibited export subsidy in view of the CVA requirements. However, the panel overlooked that claim. See *Canada - Autos (AB)*, para. 111.

⁹⁶ *Canada - Autos (Panel)*, paras. 10.192, 10.201.

that finding.⁹⁷ However, with respect to the CVA requirement, the panel “examine{d} the legal instruments in question”⁹⁸ and found that “depending upon the factual circumstances, a manufacturer might well be willing and able to satisfy a CVA requirement without using any domestic goods whatsoever.”⁹⁹ Accordingly, the panel concluded that the CVA aspect of the duty exemption regime was not *de jure* inconsistent with Article 3.1(b) of the SCM Agreement.¹⁰⁰

65. The Appellate Body reversed the panel’s findings with respect to the CVA aspect of Canada’s duty exemption regime. In doing so, the Appellate Body faulted the panel for “not conduct{ing} an analysis of how the CVA requirements under the {applicable legal instruments} actually work.”¹⁰¹ It explained:

{W}hether or not a particular manufacturer is able to satisfy its specific CVA requirements without using any Canadian parts and materials in its production depends very much on the *level* of the applicable CVA requirements. For example, if the level of the CVA requirements is very high, we can see that the use of domestic goods may well be a necessity and thus be, in practice, required as a *condition* for eligibility for the import duty exemption.¹⁰²

66. The Appellate Body went on to state:

{T}he Panel did not make findings as to what the actual CVA requirements are and how they operate for individual manufacturers. Without this vital information, we do not believe the Panel knew enough about the measure to determine whether the CVA requirements were contingent ‘in law’ upon the use of domestic over imported goods.¹⁰³

⁹⁷ *Canada - Autos (AB)*, para. 109.

⁹⁸ *Canada - Autos (Panel)*, para. 10.212.

⁹⁹ *Canada - Autos (Panel)*, para. 10.216.

¹⁰⁰ *Canada - Autos (Panel)*, paras. 10.216, 10.222. The panel also found that Article 3.1(b) does not reach subsidies that are contingent in fact upon use of domestic over imported goods, only subsidies that are contingent in law upon such use. *Id.*, para. 10.221.

¹⁰¹ *Canada - Autos (AB)*, para. 128 (emphasis added); *see also id.*, para. 129 (noting that panel did not “scrutinize the actual CVA requirements for {covered} manufacturers to see whether they could indeed be satisfied without using domestic goods”).

¹⁰² *Canada - Autos (AB)*, para. 130 (emphasis indicated by underscoring added; emphases indicated by italics in the original).

¹⁰³ *Canada - Autos (AB)*, para. 131 (emphasis added).

67. The Appellate Body then concluded that

{t}he Panel’s failure to examine fully the legal instruments at issue here and their implications for individual manufacturers vitiates its conclusion that the CVA requirements do not make the import duty exemption contingent ‘in law’ upon the use of domestic over imported goods. In the absence of an examination of the operation of the applicable CVA requirements for individual manufacturers, the Panel simply did not have a sufficient basis for its finding on the issue of ‘in law’ contingency.¹⁰⁴

68. In its response to the Panel’s Question 10, the United States called attention to the foregoing discussion in the Appellate Body’s *Canada - Autos* report to demonstrate that in examining a claim of *de jure* export contingency it is appropriate to consider not only the words of the particular legal instruments at issue (as the EC suggests) but also how those instruments “operate” “in practice.”¹⁰⁵ In the present dispute, evidence from Airbus’s Global Market Forecasts and from project appraisals undertaken by governments in connection with granting Launch Aid show how the Launch Aid contracts operate in practice. In particular, this evidence shows anticipated demand for the subject aircraft models in the EC and in the rest of the world and thus provides important context for understanding the performance Airbus undertakes in the Launch Aid contracts covering those models. The evidence shows that Airbus cannot fulfill its contractual obligation to repay Launch Aid over the number of sales specified in those contracts unless it exports. In light of this evidence of how the Launch Aid contracts operate in practice, the terms of the contracts necessarily imply that the provision of Launch Aid is contingent upon export performance. In short, the provision of Launch Aid is *de jure* contingent upon export performance within the meaning of Article 3.1(a) of the SCM Agreement.

69. Tellingly, in arguing that an analysis of a claim of *de jure* export contingency must be confined to “the text of the measure,”¹⁰⁶ the EC discusses only those parts of the *Canada - Autos* reports pertaining to the production-to-sales ratio aspect of the Canadian duty exemption regime.¹⁰⁷ The EC entirely neglects the panel and Appellate Body discussions of the CVA aspect of the Canadian regime. That aspect gets mentioned only in passing when the EC asserts without explanation that “the absence of findings by the panel as to what the CVA requirements were was sufficient to conclude that the panel had erred in conducting its ‘in law’ contingency analysis.”¹⁰⁸ However, that assertion is demonstrably incorrect.

¹⁰⁴ *Canada - Autos (AB)*, para. 132 (emphases added).

¹⁰⁵ See U.S. Responses to First Panel Questions, paras. 70-71.

¹⁰⁶ EC SNCOS, para. 137 (as delivered version).

¹⁰⁷ See EC SWS, paras. 260-264, 272.

¹⁰⁸ EC SWS, para. 275.

70. In its *Canada - Autos* report, the Appellate Body noted one instance in which the panel “did make a finding as to the level of the CVA requirements for one company, CAMI.” It found that level to be “60 percent of the cost of sales of vehicles sold in Canada.”¹⁰⁹ If the EC’s understanding of the Appellate Body report were correct, then, at least with respect to the CAMI company, the *Autos* panel would not have erred. However, the Appellate Body found that even with respect to CAMI the panel had erred, inasmuch as “the Panel did *not* examine how the CVA requirements would actually operate at a level of 60 per cent.”¹¹⁰

71. In sum, the Appellate Body was quite clear in its *Canada - Autos* report: In analyzing a claim of *de jure* breach of Article 3.1 of the SCM Agreement a panel should consider not only the text of the measures at issue but also how those measures “operate” “in practice.”¹¹¹ In considering how a measure operates in practice it may well be necessary to look to evidence that sheds light on the necessary implications of the text of the measure. That is the case with respect to the U.S. claims of *de jure* export contingency in this dispute. For the reasons explained above and in the U.S. response to the Panel’s Question 10, Airbus’s Global Market Forecasts and the governments’ project appraisals show that the terms of Airbus’s commitments under the Launch Aid contracts necessarily imply that the provision of Launch Aid for the A380, A340-500/600, and A330-200 is contingent in law upon export performance.

147. At para. 133 of its SNCOS, the EC submits that the United States “makes no attempt to establish anything about the existence of any supposed subsidy programme, of which the seven measures at issue are supposed to be applications”. Could the United States please respond to the EC’s submission?

Response:

72. The EC’s statement at paragraph 133 of its second non-confidential oral statement¹¹² appears to confuse the U.S. export contingency claims, which arise under Part II of the SCM Agreement, with a different claim the United States makes concerning the EC’s breach of obligations under Part III of the SCM Agreement by causing adverse effects to the interests of the United States through the use of subsidies.

¹⁰⁹ *Canada - Autos (AB)*, para. 131.

¹¹⁰ *Canada - Autos (AB)*, para. 131 (emphasis in original).

¹¹¹ *Canada - Autos (AB)*, paras. 130-131.

¹¹² This paragraph from the check-against-delivery version of the EC’s second non-confidential oral statement corresponds to paragraph 134 of the as-delivered version.

73. The U.S. export contingency claims concern the provision of Launch Aid for the A380 by the French, German, UK, and Spanish governments; the provision of Launch Aid for the A340-500/600 by the French and Spanish governments; and the provision of Launch Aid for the A330-200 by the French government.¹¹³ Separately, and not in the context of its export contingency claims, the United States has shown that the Launch Aid Program is a measure distinct from individual provisions of Launch Aid and that the EC is causing adverse effects to the interests of the United States through its use of the Launch Aid Program, in breach of Article 5 of the SCM Agreement.¹¹⁴

74. For reasons that are not at all clear to the United States, the EC attaches significance to the fact that the United States has not made arguments about the Launch Aid Program “{i}n the context of its claims regarding the seven alleged subsidies contingent upon export performance.”¹¹⁵ The EC seems to believe that this observation about the U.S. argument somehow undermines the U.S. demonstration that the Launch Aid Program is a measure in its own right.¹¹⁶ However, there is no reason that this should be the case, and the EC offers none. Instead, it simply repeats assertions it has made elsewhere in a failed attempt to show that the Launch Aid Program is not a measure.¹¹⁷

75. In sum, the absence of a U.S. claim that the Launch Aid Program is export contingent is irrelevant to the claim that the Launch Aid Program is itself a subsidy through which the EC is causing adverse effects to the interests of the United States in breach of Article 5 of the SCM Agreement.

C. EIB LOANS

148. To what extent does the United States consider that the fact that a lender operates on a not-for-profit basis necessarily implies that each and every loan provided by that lender to a recipient must be found to be on terms and conditions that are more favourable than comparable loans available to the same recipient on the market?

¹¹³ See, e.g., U.S. FWS, paras. 321-386; U.S. SWS, paras. 163-209.

¹¹⁴ See, e.g., U.S. SNCOS, paras. 31-52; U.S. FNCOS, paras. 19-26; U.S. FWS, paras. 91-106.

¹¹⁵ EC SNCOS, para. 134.

¹¹⁶ See, e.g., EC SWS, para. 218 (“In other words, the United States has neither asserted nor demonstrated the existence and precise content of a general ‘Launch aid’ measure ‘as such.’”).

¹¹⁷ See EC SNCOS, paras. 134-135.

Response:

76. If a lender, such as the EIB, operates on a not-for-profit basis, then by definition it does not seek an element of return on its loans that market-based lenders do seek. Whereas the return sought by both for-profit and not-for-profit lenders must be sufficiently high to meet obligations, cover expenses, and build up a reserve fund, only the return sought by a for-profit lender will incorporate the additional element of profit.¹¹⁸ To the extent that the element of profit is absent from the return on loans provided by a non-profit lender, the terms and conditions of such loans are likely to be more favorable than comparable loans available to the same recipient on the market. This is especially likely when the lender's not-for-profit status is coupled with an express mission to pass along to borrowers the benefit of the "fine rates" associated with "the highest possible credit rating."¹¹⁹

77. This does not mean, however, that a lender's not-for-profit status, by itself, translates into more favorable terms and conditions to a borrower for each and every loan. It is conceivable, for example, that the administrative costs a given not-for-profit lender seeks to recoup will be so high as to eliminate any benefit to the borrower that would otherwise result from the lender's non-pursuit of profit. In that case, however, it would be illogical for the lender to announce to the public that it is in the business of investing in projects "that would otherwise not get the money – or would have to borrow it more expensively."¹²⁰ Nor would a lender in this position promote its business by stating that "{i}nterest rates are based on {its} borrowing cost and a small margin to cover administrative expenses and other costs."¹²¹

78. In short, in the case of the EIB, what is relevant is not merely that the Bank operates on a not-for-profit basis. Rather, it combines its not-for-profit status with a low cost of funds, resulting from its superior, "AAA" credit rating, and a mission to "pass {} on the benefits to its clients in the form of loans at fine rates."¹²² It is these features in combination that result in EIB loans – in particular, the loans to Airbus – with terms that confer a benefit within the meaning

¹¹⁸ See U.S. SWS, paras. 262-263.

¹¹⁹ EIB, FAQs, Projects & Loans at 1-2, <http://www.eib.org/faq/faq.asp?faq=65> (Exhibit US-160); EIB, What Does the Bank Do? [Http://europa.eu.int/institutions/eib/index_en.htm](http://europa.eu.int/institutions/eib/index_en.htm) (Exhibit US-153); see also U.S. FWS, paras. 398-402; U.S. SWS, paras. 260-268; U.S. SNCOS, paras. 120-122.

¹²⁰ The European Investment Bank, *What Does the Bank Do?*, http://europa.eu.int/institutions/eib/index_en.htm (Exhibit US-153) (quoted in U.S. FWS, para. 398).

¹²¹ EIB, FAQs, Projects & Loans at 1-2, <http://www.eib.org/faq/faq.asp?faq=65> (Exhibit US-160) (quoted in U.S. FWS, para. 399).

¹²² EIB, FAQs, Projects & Loans at 1-2, <http://www.eib.org/faq/faq.asp?faq=65> (Exhibit US-160) (quoted in U.S. FWS, para. 399).

of Article 1.1(b) of the SCM Agreement.

149. How does the United States respond to the EC’s assertion at para. 507 of its SWS that “when considering benchmarks, one should not forget that there is no single absolute rate that is supposed to constitute a market benchmark” and that, therefore, “{a} benefit could exist only if the EIB rate were convincingly outside” a “spread of rates” of “20 to 50 basis points above or below the single benchmark rate” it has proposed?

Response:

79. The EC essentially is arguing for what it apparently believes to be a *de minimis* exception to Article 1.1(b) of the SCM Agreement. Under this alleged exception, it seems that if the benefit conferred by a financial contribution is not “convincingly outside” a supposed “spread of rates,” then a subsidy does not exist. However, the SCM Agreement contains no such exception. The EC cites no authority for its supposed “20 to 50 basis points” rule and, indeed, none exists. In fact, the context of Article 1 contradicts the EC’s position.

80. As the Appellate Body found in *Canada - Aircraft*, “Article 14 . . . constitutes relevant context for the interpretation of ‘benefit’ in Article 1.1(b).”¹²³ With respect to loans, Article 14 provides the following guideline:

{A} loan by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the loan pays on the government loan and the amount the firm would pay on a comparable commercial loan which the firm could actually obtain on the market. In this case the benefit shall be the difference between these two amounts.¹²⁴

81. In other words, Article 14 contemplates a market benchmark consisting of an “amount,” not a spread of amounts.

82. Moreover, in arguing for a *de minimis* exception to Article 1.1(b) for benefits that fall within a supposed spread of rates, the EC essentially is taking the position that Canada took and the panel rejected in *Canada - Aircraft*. In that dispute, the panel explained:

In order to rebut the *prima facie* case of ‘benefit’, we consider that Canada must do more than simply demonstrate that the amounts of specific ‘benefit’ estimated by Brazil may be incorrect, or that TPC’s rate of return covers Canada’s cost of funds. Rather, Canada

¹²³ *Canada - Aircraft (AB)*, para. 155. The EC accepts the proposition that Article 14 is context for interpreting the term “benefit” in Article 1.1(b). See, e.g., EC FWS, para. 1215.

¹²⁴ SCM Agreement, Art. 14(b) (emphasis added).

must demonstrate that no ‘benefit’ is conferred, in the sense that the terms of the contribution provide for a commercial rate of return.¹²⁵

83. In this dispute, the United States has adduced evidence demonstrating that the EIB loans to Airbus do not provide for a commercial rate of return and thus confer a benefit within the meaning of Article 1.1(b).¹²⁶ It made a *prima facie* case of benefit, causing the burden to shift to the EC to demonstrate that no benefit is conferred by the EIB loans. Instead of meeting that burden, the EC (like Canada in *Canada - Aircraft*) has made an argument about the amount of benefit conferred. Like the panel in *Canada - Aircraft*, this Panel should reject that argument.

150. In its answer to Panel Question 117 and at para. 294 of its SWS, the United States argues that “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 for purposes of a *de jure* specificity ...”.

- (a) Is the Panel correct to understand this statement as an allegation that each of the challenged EIB loans are *de jure* specific because they allegedly possess “sufficiently different” terms and conditions?**
- (b) How does the United States respond to the arguments and information presented by the EC at paras. 416-426 of its SWS?**

Response:

84. The U.S. argument that the subsidies conferred by the EIB loans to Airbus are *de jure* specific within the meaning of Article 2.1(a) of the SCM Agreement has been shaped in part by the very limited information the EC has provided to the Panel and the United States, despite repeated requests for more complete information. As the United States discussed in response to the Panel’s Question 117, as of the U.S. submission of that response on April 30, 2007, the EC had provided information on only two of the 12 EIB loans at issue. Further, the EC had not provided any 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.¹²⁷

85. The EC refused to provide this information despite express requests during the Annex V

¹²⁵ *Canada - Aircraft (Panel)*, para. 9.312 (emphasis added).

¹²⁶ See U.S. FWS, paras. 397-404, 410-416.

¹²⁷ U.S. Responses to First Panel Questions, para. 352.

process.¹²⁸ It was only at a very late stage in this dispute, with its second written submission, that the EC finally provided the contracts for the EIB loans at issue.¹²⁹ Even then, however, the EC refused to provide evidence that could meaningfully serve as a basis against which to compare those loans, instead providing only a standard form EIB contract and the most general information about how the EIB operates.¹³⁰

86. Based on the limited information the EC provided, together with publicly available information, it was still possible to discern certain basic facts. In particular, each EIB subsidy is conveyed in a loan agreement that is negotiated with and limited to an individual borrower. Further, in the EIB's words, each loan it provides is "tailored to each individual project."¹³¹ Based on these facts, the subsidy conferred by each EIB loan is "specific" within the meaning of Article 2.1(a).¹³²

87. Following the first substantive meeting with the parties, the Panel posed Question 117, in which it asked for the parties' views on "the extent to which a subsidy granted, through a contract including one or more unique terms and conditions, to an individual enterprise pursuant to a subsidy programme that does not explicitly limit access to subsidies to certain enterprises, may be specific within the meaning of Article 2.1(a) of the SCM Agreement." The United States provided a response that included the proposition referred to in the present question. The United States also noted that the EC had refused to provide information regarding both the EIB loans to Airbus and EIB loans to other borrowers that the Panel would need in order to undertake the comparative analysis described in the U.S. response.¹³³

88. In view of the reasoning set out in the U.S. first written submission,¹³⁴ the Panel should not need to undertake the comparative analysis described in the U.S. response to Question 117.

¹²⁸ See *Replies to Questions by the Facilitator under Annex V of the SCM Agreement by the European Communities* (Nov. 18, 2005), Q80 and Q82 (Exhibit US-5 (BCI)); see also U.S. FWS, para. 410; U.S. SWS, paras. 294-297.

¹²⁹ See EC SWS, para. 420.

¹³⁰ See U.S. SNCOS, para. 125 (discussing EC refusal to provide information on EIB loans).

¹³¹ EIB, *The Project Cycle at the European Investment Bank*, at 4-5 (July 12, 2001) (Exhibit US-166) (discussed in U.S. FWS, para. 406).

¹³² See U.S. FWS, paras. 406, 418-419.

¹³³ See U.S. Responses to First Panel Questions, para. 352.

¹³⁴ See U.S. FWS, paras. 406, 418-419.

89. In an attempt to counter the U.S. argument regarding specificity, the EC refers to the recently circulated report of the panel in *Japan - Countervailing Duties on Dynamic Random Access Memories from Korea*.¹³⁵ However, the EC's discussion of that report is extremely misleading. In fact, the panel in *Japan - DRAMs* (following the reasoning of the panel in *EC - DRAMs*), rejected an argument by Korea remarkably similar to the EC's argument in this dispute, and found a subsidy to be specific where it was "tailored to the needs of the recipient company," even though it was granted pursuant to a broad "framework programme."¹³⁶

90. At issue in *Japan - DRAMs* were certain restructurings involving the Hynix company. Like the EC in this dispute, Korea contended that a specificity analysis of the Hynix restructurings should involve a comparison to a broader set of activities. Thus, it argued that "the same basic rules that governed Hynix's restructurings – as embodied in the Workout Agreement and later in the Corporate Restructuring Promotion Act {CRPA} – were the same rules that governed the restructuring of other Korean companies."¹³⁷ This is much like the EC's assertion, based on the facts of this dispute, that the "unique terms and conditions" in the EIB's loans to Airbus "do not depart from the standard criteria and methodology applied to all other projects."¹³⁸

91. The *Japan - DRAMs* panel rejected Korea's argument. It upheld a finding by Japan's investigating authorities ("JIA") in the countervailing duty investigation underlying that dispute that "the CRPA merely provided the procedural framework within which the October 2001 and December 2002 restructurings took place, rather than actually determining the terms of those restructurings."¹³⁹ The panel noted evidence in the JIA's record showing that within the CRPA "procedural framework" "the substantive terms of restructurings were the prerogative of the Councils for Creditor Financial Institutions, which were set up for each restructured company separately."¹⁴⁰ The panel went on to observe that a subsidy given "on pre-determined terms (that are therefore not tailored to the recipient company)" would not be specific simply by virtue of

¹³⁵ See EC SNCOS, paras. 173-178 (discussing Panel Report, *Japan - Countervailing Duties on Dynamic Random Access Memories from Korea*, WT/DS336/R, paras. 7.372-7.374 (notice of appeal filed Aug. 30, 2007) ("*Japan - DRAMs*").

¹³⁶ *Japan - DRAMs*, para. 7.374.

¹³⁷ *Japan - DRAMs*, para. 7.364 (summarizing Korea's argument).

¹³⁸ EC SWS, para. 423.

¹³⁹ *Japan - DRAMs*, para. 7.372.

¹⁴⁰ *Japan - DRAMs*, para. 7.372.

being given to a specific company, but that these were not the facts before it.¹⁴¹

92. Likewise, the facts of the present dispute show that the EIB subsidies to Airbus were not given “on pre-determined terms (that are therefore not tailored to the recipient company).” Quite the contrary, as noted above, the EIB’s loans are “tailored to each individual project.”¹⁴² Like the restructurings in *Japan - DRAMs*, the subsidies to Airbus were given pursuant to a “procedural framework” set forth in documents such as the EIB Statute and eligibility guidelines. This procedural framework does not set “pre-determined terms,” but identifies steps the EIB follows in exercising its discretion to provide loans.¹⁴³ In sum, contrary to the EC’s argument, the panel report in *Japan - DRAMs* reinforces the point that, given the facts at issue in this dispute, the Panel should analyze the specificity of the EIB’s loans to Airbus on a loan-by-loan basis, rather than on the basis of a comparison to the “procedural framework” represented by the EIB institution as a whole.

93. If the Panel, nevertheless, were to view the entire lending activity of the EIB as “a subsidy programme that does not explicitly limit access to subsidies to certain enterprises” and individual EIB loans as subsidies granted pursuant to that program, then a comparative analysis of the type described in the U.S. response to Question 117 would be warranted. However, the EC has made such an analysis impossible by withholding critical information. Although it has belatedly provided the contracts for the EIB loans to Airbus, it has not provided information requested in the Annex V Facilitator’s Question 80 or other information, such as a representative sample of other EIB loan contracts, that would make a comparative analysis possible.

94. In its second written submission, the EC asserts that its financing contract template together with general background information about the EIB (such as the EIB statute and eligibility guidelines) and summary information about EIB lending activity should enable such an analysis.¹⁴⁴ But, they do not. In fact, even the EC, in its response to the Panel’s Question 85, expressed doubt about the relevance of a standard form contract to a specificity analysis.¹⁴⁵ The

¹⁴¹ *Japan - DRAMs*, para. 7.374.

¹⁴² EIB, *The Project Cycle at the European Investment Bank*, at 4-5 (July 12, 2001) (Exhibit US-166).

¹⁴³ See U.S. SWS, paras. 285-293. The EC asserts that the interest rates on EIB loans are set “in an automatic manner and with no space for discretion.” EC SNCOS, para. 183. However, it fails to substantiate this assertion. Elsewhere, the EC states that the EIB undertook a significant change in its approach to setting interest rates in 1999 – *i.e.*, after all but one of the loans to Airbus came into existence. The EC states that prior to 1999, the EIB had not included a risk premium in its loans, and after 1999, did so only for “projects where normal risk-mitigation measures could not be applied.” EC FWS, para. 1070.

¹⁴⁴ See EC SWS, paras. 422-423.

¹⁴⁵ See EC Responses to First Panel Questions, para. 186.

United States shares that doubt.

95. The EC’s contract template reveals nothing about how core terms may differ between loans to Airbus and loans to other enterprises. Indeed, what that document shows is that it is precisely these core terms – the terms that may cause a loan to confer a benefit and thus constitute a subsidy – that vary from contract to contract. Under the template, important elements, such as [

] ¹⁴⁶ Without information from actual contracts, it is impossible to know the extent to which the variables highlighted by the template differ as between the Airbus loans and loans to other enterprises.

96. The EC asserts that “it is apparent that the unique terms and conditions present in EIB loans, including the challenged loans, that matter for the finding of existence of subsidy, such as interest rate, maturity, repayment profile, etc., do not depart from the standard criteria and methodology applied to all other projects.”¹⁴⁷ However, the EC provides absolutely no evidence to substantiate that assertion. In fact, as the United States discussed in its second written submission, the eligibility guidelines on which the EC relies so heavily in arguing for non-specificity reflect a high degree of subjectivity and require significant exercises of discretion in the loan provision process.¹⁴⁸

97. The EC asserts that what is relevant in a specificity analysis is not “the existence of discretion as such” but “the ‘manner in which discretion has been exercised.’”¹⁴⁹ However, the contract template and other general information the EC has provided about EIB lending reveal nothing about the “manner in which discretion has been exercised.” In short, the EC has made a meaningful comparison between the EIB loans to Airbus and other EIB lending impossible.

98. In light of the EC’s refusal to provide information that would allow the Panel to make such a comparison, the reasonable inference to be drawn is that such information would confirm that the unique terms and conditions of the EIB’s loans to Airbus are sufficiently different from the terms and conditions of other EIB loans as to cause the Airbus loans to be *de jure* specific subsidies. If the Panel were to conclude that a comparison between the loans to Airbus and EIB loans to other borrowers is necessary for purposes of a specificity analysis under Article 2.1(a),

¹⁴⁶ EIB, Financing Contract Template, Arts. 1.01, 1.03., 1.04, 4.01, 3.01, 4.03 (Exhibit EC-609 (BCI)).

¹⁴⁷ EC SWS, para. 423.

¹⁴⁸ See U.S. SWS, paras. 287-293.

¹⁴⁹ EC SNCOS, para. 185 (quoting SCM Agreement, Art. 2.1(c)).

the United States respectfully requests the Panel to draw such an inference.¹⁵⁰

151. The United States reveals, in response to Panel Question 14, that it focused its “disproportionality” analysis of the 2002 loan to EADS on the “research and development” heading of the EIB’s “i2i” lending. Does the United States consider that the funds provided under the “research and development” heading evidence the existence of a particular “research and development” “subsidy programme”?

- (a) **If so, please explain what it is about the funds provided under the “research and development” heading that renders it a “programme” for purposes of Article 2.1(c).**
- (b) **If not, please explain, in the light of the assessment that is envisaged under Article 2.1(c), why it is appropriate to focus the relevant “disproportionality” analysis on a subset of funds granted under the EIB’s “i2i” lending.**

Response:

99. As discussed in response to Question 218, below, Article 2.1(c) of the SCM Agreement does not require that a subsidy be granted pursuant to a subsidy program in order to be *de facto* specific. It is the EC that suggests that specificity must be evaluated relative to a subsidy program. However, it offers no standard for determining what constitutes a subsidy program. It simply asserts without explanation that all lending by the EIB over its entire 50-year history constitutes a subsidy program, and that it is within this frame of reference that the 2002 loan to EADS (as well as other EIB loans to Airbus) must be analyzed for purposes of Article 2 of the SCM Agreement.¹⁵¹

100. For reasons discussed in response to the Panel’s Questions 13, 14, and 119, in applying the specificity factors set out in Article 2.1(c), it is not appropriate to compare the EADS loan to all lending by the EIB over its entire history.¹⁵² Rather, the Panel should adopt a more meaningful frame of reference. This approach is supported by the context of the last sentence of Article 2.1(c), which states that “account shall be taken . . . of the length of time during which

¹⁵⁰ Paragraph 7 of Annex V of the SCM Agreement states that the Panel should draw adverse inferences from instances of non-cooperation by any party involved in the information-gathering process. The EC’s refusal to provide relevant information regarding EIB lending is an instance of such non-cooperation.

¹⁵¹ See, e.g., EC FWS, para. 1039; EC Responses to First Panel Questions, para. 367; EC SWS, paras. 434-436, 478; EC SNCOS, para. 184; see also EC SWS, para. 629 (asserting, in the context of argument regarding research and development grants, that “specificity within the meaning of Article 2 of the *SCM Agreement* must be assessed at the programme level”).

¹⁵² See U.S. Responses to First Panel Questions, paras. 81-91, 92-102, 365-370.

the subsidy programme has been in operation.” Even if (contrary to the reasoning set out in the U.S. response to Question 218) the Panel were to treat all lending by the EIB over 50 years as a single “subsidy programme,” taking account of “the length of time during which the subsidy programme has been in operation” would require identifying a subset of the EIB’s activity as a reasonable basis against which to compare the loan to EADS.¹⁵³

101. In identifying such a subset, it is appropriate to consider the way in which the EIB itself analyzes its lending activity. The loan to EADS was granted under the auspices of what the EIB itself referred to as the i2i program. The EIB divided that program into five discrete objectives. It was pursuant to one of these – the research and development objective – that the EIB made the Euro 700,000,000 loan to EADS. The EIB itself focused on lending under each objective in describing its own activity. Thus, its 2002 report states that “{i}n 2002, the EIB ploughed {Euro} 2.1 billion into 15 R&D projects spanning 6 EU countries, with one pan-European international cooperation project partly located in Switzerland. . . .”¹⁵⁴

102. In short, the United States does not contend that the research and development objective within the i2i program is itself a “subsidy program.” Rather, it is because the EIB itself classified its lending under the i2i program on an objective-by-objective basis that it is appropriate to analyze the 2002 loan to EADS in comparison to the i2i objective under which it was granted.¹⁵⁵ As already noted, Article 2 of the SCM Agreement does not require that the Panel analyze specificity on the basis of a subsidy program, as opposed to another appropriate frame of reference. However, even if the Panel were to disagree – that is, if the Panel were to find that the EADS loan should be analyzed in comparison to a particular subsidy program – there still would be no basis for identifying all lending activity of the EIB over a 50-year period as that program, as the EC suggests. In that case, the relevant program would be the i2i program.

103. In response to Question 218, below, the United States discusses factors relevant to identifying a series of subsidies as a subsidy program and shows that these factors are evident in what the EIB itself calls the i2i program, but not in the broad universe of EIB lending activity over the bank’s entire history. The United States also shows that even if the Panel were to consider all lending activity of the EIB as a single subsidy program, that would not deprive the i2i program of its status as a subsidy program. Given the existence of a program within a program, the requirement under Article 2.1(c) to take account of “the length of time during which the subsidy programme has been in operation” indicates that the Panel should look to the i2i program rather than all EIB lending ever, as noted above.

¹⁵³ See, e.g., U.S. Responses to First Panel Questions, para. 92.

¹⁵⁴ The EIB Group, Activity Report 2002, at 14 (Exhibit US-165).

¹⁵⁵ See U.S. Responses to First Panel Questions, para. 100.

104. If the Panel were to use the i2i program as a whole, rather than the research and development objective of the i2i program, as its frame of reference, it still should find that the 2002 loan to EADS is specific within the meaning of Article 2. As previously discussed, the loan to EADS was the single largest loan to any one company under the i2i program as a whole.¹⁵⁶ Thus, from inception of the i2i program in 2000 through the EIB's announcement that it "had fully achieved its i2i objectives" by the end of 2002, EADS was the predominant user of the program.¹⁵⁷

D. INFRASTRUCTURE

152. Please explain what the United States means when it states, in its response to Panel Question 20 (at para. 137), that in order to be excluded from Article 1.1(a)(1)(iii) of the SCM Agreement, 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. Does the United States suggest that, in addition to a requirement that the infrastructure be completely or nearly universal, the infrastructure must also include, involve or affect all or nearly all the parts of a whole territory or community, or is that latter requirement intended to be an example of the requirement of complete or near universality?

Response:

105. The U.S. response to the Panel's Question 20 set out the ordinary meaning of the word "general" and then analyzed the term "general infrastructure" as used in Article 1.1(a)(1)(iii) in light of that meaning. The dictionary definition of "general," on which the United States relied for the word's ordinary meaning, contains two phrases separated by a semicolon, each of which conveys the same essential concept in a slightly different way. In applying the definition of "general" to the phrase "general infrastructure," the United States applied each of the relevant phrases, in the interest of providing a complete and accurate understanding of the term. In doing so, the United States did not mean to suggest that the two alternative phrases used to define the word "general" correspond to two distinct requirements, each of which must be separately

¹⁵⁶ See U.S. Responses to First Panel Questions, para. 101; Overview of i2i loans (Exhibit US-474). Even treating the Innovation 2000 Initiative and its successor, the Innovation 2010 Initiative, as a single program (as the EC asserts, incorrectly, they should be treated (*see* U.S. Responses to First Panel Questions, para. 98)), EADS stands out as the predominant user. The EC's exhibit EC-164 lists all loans signed under both the Innovation 2000 Initiative and the Innovation 2010 Initiative, through the end of 2006. The 2002 loan to EADS is one of only three on that list in an amount of Euro 700,000,000 or more, and the only such loan under the R&D objective (the other two pertaining to telecommunications projects under the Information and Communications Technology objective).

¹⁵⁷ Other measures also confirm a finding of specificity. For example, the EADS loan represented 18% of the Euro 3.8 billion in EIB financing for R&D from 2000 through the EIB's finding that it "had fully achieved its i2i objectives" by the end of 2002. *See* U.S. Responses to First Panel Questions, para. 101.

fulfilled in order for infrastructure to be general infrastructure. Rather, as the Panel correctly indicates, the United States understands that if infrastructure includes, involves, or affects all or nearly all the parts of a whole territory or community it is likely, therefore, to be completely or nearly universal, as opposed to partial, particular or local.¹⁵⁸ Thus, as the United States explained in its oral statement at the first Panel meeting, “{V}iewed 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.”¹⁵⁹

153. At paragraph 95 of its SNCOS, the United States argues that the improvements to the DR902 and RD963 are not general infrastructure because they were undertaken expressly to provide access to the AéroConstellation site for Airbus and its suppliers. To what extent is the objective or motive of the government in creating infrastructure determinative of its status as general infrastructure or otherwise?

Response:

106. The United States has not argued that improvements by French authorities to the RD 902 and RD 963 constitute non-general infrastructure because they serve to implement a certain government objective or motive. Rather, the United States has argued that the improvements made to allow Airbus to access the AéroConstellation site from the RD 902 and the RD 963 are, in fact, open for use only by Airbus and its suppliers. That is what makes them non-general infrastructure.¹⁶⁰

107. At paragraph 95 of its second non-confidential oral statement, the United States addressed a misrepresentation of the U.S. argument in the EC’s second written submission. The EC misleadingly portrayed the United States as contending that the improvements to the RD 902 and RD 963 are non-general because they are “used more often by the companies located in the

¹⁵⁸ In its third party oral statement, Canada suggested, incorrectly, that the reference to “all or nearly all the parts of a whole territory or community” in the U.S. explanation of “general infrastructure” is a reference to a WTO Member’s entire territory. *See* Canada Third Party Oral Statement, para. 14. It is not. A territory or community need not be co-extensive with the entirety of a Member’s territory. As is clear from the U.S. explanation, the territory or community referred to is the territory or community affected by the infrastructure at issue.

¹⁵⁹ U.S. FNCOS, para. 79 (emphasis in original). As discussed in the U.S. second written submission, the U.S. understanding of the term “general infrastructure” is entirely consistent with the approach taken by the EC under its state aids regime. Thus, in one recent decision, the European Commission described general infrastructure as infrastructure that is “open to all potential users on equal and non-discriminatory terms.” European Commission, Decision of 21 December 2005, Aid No N 503/2005, UK Great Yarmouth Outer Harbour, pp. 4-5 (Exhibit US-546) (quoted at U.S. SWS, para. 309).

¹⁶⁰ *See* U.S. Responses to First Panel Questions, para. 150; *see also* U.S. FWS, para. 482 (quoting statement from the website of the government of Grand Toulouse that refers to “the access roads for the site”).

ZAC than others.”¹⁶¹ The point the United States made in reply is that it is not merely predominant use by Airbus that makes the improvements other than general infrastructure. Rather, it is the fact that the improvements are for use only by Airbus and its suppliers that leads to this conclusion.

108. Using documents published by the government of Grand Toulouse and by Air France, as well as satellite photographs and maps of the AéroConstellation site, the United States has shown that Air France, STTS, and SIDMI access the site from the South, via the RD 901, while the improvements created at the site’s northern perimeter (at the RD 963) and at its eastern perimeter (at the RD 902, including, in particular, the “Diffuseur de Pinot”) are open for use exclusively by Airbus and its suppliers as access infrastructure for Airbus’s facilities.¹⁶² It was to this evidence that the United States was alluding when it stated that the improvements at issue “were undertaken expressly to provide access to the AéroConstellation site for Airbus and its suppliers.”

109. Finally, a basic point that bears emphasis is that the status of infrastructure as “general” or otherwise does not depend on the motive or objective of the government creating the infrastructure. There is no basis for the EC’s contrary view that infrastructure is “general” merely because it “benefits society as a whole and reflects legitimate economic development policies.”¹⁶³ As previously discussed, that description would fit virtually any government-sponsored infrastructure (not to mention, virtually any subsidy). The EC’s approach would render the term “general” redundant with the term “infrastructure” in Article 1 of the SCM Agreement, contrary to customary rules of interpretation of public international law.¹⁶⁴

154. How does the United States suggest that the benefit to a recipient be determined when, under prevailing market conditions, costs associated with infrastructure in the form of reclamation of land cannot be recovered in the market price for the provision of that infrastructure? Does it make any difference if that reclaimed land is provided together with additional infrastructure in the form of the developed reclaimed land?

Response:

¹⁶¹ EC SWS, para. 373.

¹⁶² See U.S. Responses to First Panel Questions, para. 150 and footnote 165 (citing Exhibits US-208, US-217, and US-481).

¹⁶³ EC FWS, para. 909; *see also id.*, para. 923.

¹⁶⁴ See U.S. FNCOS, para. 79; U.S. Responses to First Panel Questions, paras. 138-140; U.S. SWS, paras. 305-307.

110. The United States understands this question to relate to the City of Hamburg's provision to Airbus of an industrial site (adjacent to an existing Airbus site), which was created by reclaiming wetlands in the Mühlenberger Loch, and for which the lease terms did not return to the government its investment in creating the site. Before responding to the hypothetical scenario posed by this question, it is important to make clear that the facts at issue in this dispute differ substantially from those suggested by the hypothetical. What the City of Hamburg provided to Airbus was not simply reclaimed land. It was an entire industrial site for final assembly of the A380, adjacent to Airbus's existing site, custom-made to Airbus's specifications, and uniquely valuable to Airbus. Providing that site necessitated the reclamation of land. But, it would be incorrect to view the reclamation of land as separate from the rest of the transaction.¹⁶⁵

111. As the United States will discuss later in its response to this question and in its response to Question 155, because the industrial site that Hamburg created for and provided to Airbus is uniquely valuable to Airbus, it is not appropriate to refer to a price that a buyer or lessee in the market might pay for the infrastructure. In this circumstance, a different market benchmark must be identified. As will be discussed below, the appropriate benchmark is the government's investment into creating the infrastructure.

112. Turning to the hypothetical scenario described in this question, the United States first recalls that the starting point for determining the benefit that a financial contribution confers on a recipient is a comparison to the marketplace. As the Appellate Body explained in *Canada - Aircraft*, the question is "whether the recipient has received a 'financial contribution' on terms more favourable than those available to the recipient in the market."¹⁶⁶ The Appellate Body also found it appropriate to refer to Article 14 of the SCM Agreement as "relevant context in interpreting Article 1.1(b)."¹⁶⁷ Subparagraph (d) of Article 14 states that "the provision of goods or services . . . by a government shall not be considered as conferring a benefit unless the provision is made for less than adequate remuneration." It goes on to state that "{t}he adequacy of remuneration shall be determined in relation to prevailing market conditions for the good or service in question in the country of provision . . . (including price, quality, availability, marketability, transportation and other conditions of purchase or sale)."

113. The terms available in the market for a good or service usually will include the cost incurred to produce the good or service plus a reasonable rate of return.¹⁶⁸ Specifically, with

¹⁶⁵ See, e.g., U.S. FWS, paras. 423-429; U.S. SWS, paras. 332-348.

¹⁶⁶ *Canada - Aircraft (AB)*, para. 157.

¹⁶⁷ *Canada - Aircraft (AB)*, para. 158.

¹⁶⁸ See U.S. FWS, paras. 434-436.

respect to infrastructure in the form of reclamation of land (recalling, again, that at issue in this dispute is not simply the reclamation of land, but the provision of an entire industrial site), a profit-maximizing developer would not undertake to create the infrastructure unless it had reason to believe that it could obtain a return that would enable it to recover its costs plus a reasonable profit. It is conceivable, however, as the question suggests, that prevailing market conditions will make it impossible for the developer to recover its costs. A macroeconomic event, such as the onset of a recession, may occur after the developer has undertaken to create the infrastructure. In such a situation, the developer still would seek to maximize its return, perhaps by putting the infrastructure up for auction and selling or leasing it to the highest bidder. The price offered by the highest bidder presumably will reflect “prevailing market conditions for the good or service in question in the country of provision” and thus is likely to represent adequate remuneration.

114. If, in the foregoing scenario, the developer were the government rather than a private investor and the government provided the infrastructure to the highest bidder, the provision likely would not be considered to confer a benefit within the meaning of the SCM Agreement, even if the price paid by the highest bidder did not enable the government to recover its costs. If the government provided the infrastructure at a price lower than that offered by the highest bidder, then the provision probably would confer a benefit to the extent of the difference.

115. The inclusion of infrastructure in addition to the bare, reclaimed land complicates the analysis. Depending on how specialized it is, the additional infrastructure may be of value to only a select group of potential buyers or lessees – or, perhaps, only one potential buyer or lessee – while to others, the additional infrastructure constitutes an unnecessary encumbrance (*i.e.*, it has negative value). The additional infrastructure may cause this latter group not to bid for the reclaimed land at all, or to offer lower bids than they would have offered for the bare land, due to the costs this group associates with tolerating or removing the additional infrastructure that they do not value. The result may be that the highest price offered for the reclaimed land plus the additional infrastructure does not accurately reflect – in fact, understates – the market value of the unencumbered reclaimed land itself.

116. Unlike either of the two hypothetical scenarios just described, the facts relevant to the U.S. claims regarding government provision to Airbus of reclaimed land do not include any attempt by the government to recover its costs or otherwise obtain a market price for the infrastructure. The German authorities that created the industrial site for Airbus by filling wetlands adjacent to the company’s existing site in Hamburg did not reclaim the land and then offer it to the highest bidder. From the outset, the authorities undertook this project for Airbus and provided the infrastructure to Airbus without taking into account the authorities’ investment into creating the infrastructure – something that a market provider of infrastructure would not

have done.¹⁶⁹ Indeed, the authorities had no expectation of recovering their costs. As Hamburg's former minister for economic affairs explained:

The investment would in fact be unprofitable based on the rent alone. The whole thing must be viewed in terms of the public economy.¹⁷⁰

117. As the United States summarized the evidence in its second non-confidential oral statement: “Under EC and German law, the reclamation of the protected wetlands would not have been permitted but for Airbus’s specific need; Airbus has a 30-year exclusive right to use of the land; the ‘land construction plan’ adopted by the City of Hamburg designates the land exclusively for an aircraft factory and air traffic; and inadequate access would make it impractical to use the land other than as an extension of Airbus’s existing site.”¹⁷¹ In short, the facts regarding the German authorities’ provision of infrastructure to Airbus bear no resemblance whatsoever to the hypothetical scenario described above, in which a government obtains a market price for infrastructure but, due to prevailing market conditions, the market price does not enable it to recover its costs. Here, the government undertook to provide specialized infrastructure to a particular company at a location uniquely valuable to that company with no intention of seeking to recover the Euro 751,000,000 invested into creating the site. Under these circumstances, the recipient of the infrastructure – Airbus – unquestionably received a benefit within the meaning of Article 1.1(b) of the SCM Agreement. It received an industrial site meeting its requirement of “immediate proximity to the existing aircraft production facility in Hamburg-Finkenwerder”¹⁷² at a price that did not include the Euro 751,000,000 it would have had to invest to create the site itself.

118. A similar analysis applies to the French authorities’ provision to Airbus of an industrial site in Toulouse. In that case, the government invested more than Euro 200,000,000 into converting agricultural land adjacent to Airbus’s headquarters into an industrial site described as a “tailor-made solution for the A380”¹⁷³ and making road improvements necessitated by the site.

¹⁶⁹ See U.S. FWS, paras. 423-442; U.S. FNCOS, paras. 82-83; U.S. FCOS, paras. 38-45; U.S. SWS, paras. 311-315, 332-338, 352-361; U.S. SNCOS, paras. 86-87; U.S. SCOS, para. 48.

¹⁷⁰ *Airbus! Hark Bohm, Verlegen Bauer, Senator Uldall streiten beim Abendblatt*, Hamburger Abendblatt, at 3 (Mar. 2003) (in the original German, “Mit dem Zins alleine ware die Investition in der Tat unrentabel. Das Ganze muss volkswirtschaftlich betrachtet werden”) (Exhibit US-192) (discussed in U.S. FWS, para. 439).

¹⁷¹ U.S. SNCOS, para. 86.

¹⁷² Realisierungsgesellschaft Finkenwerder mbH (ReGe), A380-Werkserweiterung im Mühlenberger Loch - eine Bilanz, p. 10 (emphases added) (Exhibit US-182).

¹⁷³ Airbus, press release, *Airbus’ A380 Final Assembly Facility inaugurated by French President*, July 16, 2002 (Exhibit US-200) (discussed in U.S. FWS, para. 456); see also “AéroConstellation, nid de l’A380,” available at www.mairie-blagnac.fr (Exhibit US-640) (discussed in U.S. SNCOS, para. 91).

As in Hamburg, the French authorities did not undertake the conversion of agricultural land in the expectation of obtaining a market price that would enable them to recover their costs plus a commercial rate of return. The authorities undertook this project for Airbus and provided the infrastructure to Airbus at a price that did not include the authorities' investment into creating the infrastructure – something that a market provider of infrastructure would not have done.¹⁷⁴ As a result, Airbus received a valuable industrial site at a price that did not include the Euro 158,000,000 it would have had to invest to create the site itself (not to mention the government's related Euro 49,000,000 investment in road improvements).

119. As in Hamburg, the government's provision of infrastructure to Airbus in Toulouse bears no resemblance to the hypothetical set out in the Panel's question. This is not an instance in which a government provides a good at a market price which, due to prevailing market conditions, does not enable the government to recover the costs of creating the good. The government did not even seek a market price in the first place. As it provided infrastructure to Airbus for less than adequate remuneration, it conferred a benefit on Airbus within the meaning of Article 1.1(b) of the SCM Agreement.

155. Assuming that the Panel were to find that a private investor would not undertake a particular infrastructure activity because it would be unable to recoup the necessary investment in the market, would the United States argue that there is nonetheless a benefit to the recipient of such an infrastructure activity when carried out by a government?

Response:

120. With respect to each of the infrastructure activities at issue in this dispute, a finding that a private investor would not have undertaken the activity should not affect the Panel's benefit analysis. In each case, Airbus has received a valuable asset without paying a price that reflects the amount invested to create the asset. It has received the asset for less than the investment it would have had to make to create the asset for itself. Thus, in the words of the Appellate Body in *Canada - Aircraft*, Airbus has received a financial contribution that makes it "better off" than it would otherwise have been, absent that contribution."¹⁷⁵ Accordingly, provision of the financial contribution confers a benefit within the meaning of Article 1.1(b) of the SCM Agreement.

121. Preliminarily, it should be noted that the mere fact that a government has created infrastructure that the market would not otherwise have created does not automatically make the infrastructure "general infrastructure" within the meaning of Article 1 of the SCM Agreement.

¹⁷⁴ See U.S. FWS, paras. 456-477; U.S. FNCOS, paras. 87-88; U.S. Responses to First Panel Questions, paras. 140-148, 162-166; U.S. SWS, paras. 403-414; U.S. SNCOS, paras. 91-92.

¹⁷⁵ *Canada - Aircraft (AB)*, para. 157.

To attain that status, the infrastructure must be “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,” consistent with the ordinary meaning of “general infrastructure” in context and in light of the object and purpose of the SCM Agreement.¹⁷⁶ Infrastructure custom-made by the government to the specifications of a particular company for sole or predominant use by that company is not “general” simply because the market would not have created it.

122. With respect to benefit, the fact that the market would not have created such company-specific infrastructure means that it is not possible to refer to a market-set price as a benchmark to determine whether the remuneration paid is adequate or not, and whether a benefit is therefore conferred or not. Another basis for establishing a market benchmark must be identified. A logical basis is the government’s investment in creating the good plus a reasonable rate of return. Indeed, in *US - Softwood Lumber CVD Final*, the Appellate Body found that in the absence of a market-set price for a good in the country of provision, “alternative methods for determining the adequacy of remuneration could include . . . proxies constructed on the basis of production costs.”¹⁷⁷

123. In this dispute, the remuneration that Airbus paid to government providers of infrastructure unquestionably fell below the governments’ investment into creation of that infrastructure. The EC does not deny this. Instead, it argues that “{a} government may realize other forms of remuneration that are valued by governments, but not necessarily by private investors – such as higher tax revenues and increased employment.”¹⁷⁸

124. However, the possibility that the government may have anticipated “higher tax revenues and increased employment” from infrastructure it provided to Airbus and considered such effects to be part of its remuneration does not mean that it provided the infrastructure for adequate remuneration. Article 14(d) of the SCM Agreement – which contains guidelines for determining whether remuneration paid for government provision of goods or services is adequate –

¹⁷⁶ U.S. FNCOS, para. 79 (emphasis in original).

¹⁷⁷ *US - Softwood Lumber CVD Final (AB)*, para. 106. Also relevant is the report of the Appellate Body in *Canada - Dairy (Article 21.5)*. At issue in that dispute was whether milk producers’ provision of milk to processors constituted “payments” within the meaning of Article 9.1(c) of the *Agreement on Agriculture*. The Appellate Body’s analysis of “payments” under that provision was similar to its analysis of “benefit” under the SCM Agreement. See *Canada - Dairy (Article 21.5) (AB)*, para. 74 (“{T}he determination of whether ‘payments’ are involved requires a comparison between the price actually charged by the provider of the goods or services . . . and some objective standard or benchmark which reflects the proper value of the goods or services to their provider. . . .”). The Appellate Body found that where prices for the good at issue were set by government regulation, such prices would not serve as an appropriate benchmark. *Id.*, para. 81. In that situation, the Appellate Body found, it is appropriate to use “total cost of production” as a benchmark. *Id.*, para. 88.

¹⁷⁸ EC SNCOS, para. 216; see also EC SCOS, para. 27.

expressly provides that “{t}he adequacy of remuneration shall be determined in relation to the prevailing market conditions for the good or service in the country of provision or purchase (including price, quality, availability, marketability, transportation and other conditions of purchase or sale).” Tax revenues and increased employment are not among the factors listed in Article 14(d).

125. Indeed, as pointed out in the U.S. comments on the EC’s opening statement at the second Panel meeting, if “higher tax revenues and increased employment” were relevant to an evaluation of adequate remuneration for the provision of goods or services – and thus, an evaluation of benefit – “there would be virtually no SCM Agreement disciplines on the provision of infrastructure.”¹⁷⁹ Regardless of the amount of remuneration for which a government provided infrastructure to a company, it always would be able to argue that payment by the company must be viewed in conjunction with “higher tax revenues and increased employment,” that remuneration is “adequate,” and that, accordingly, no benefit is conferred by the provision of such infrastructure. Such circumvention of SCM Agreement disciplines would be contrary to the object and purpose of the SCM Agreement.¹⁸⁰

126. Moreover, anticipation of higher tax revenues and increased employment does not distinguish infrastructure provided for less than adequate remuneration from infrastructure provided for adequate remuneration. In either situation, the government may anticipate higher tax revenues and increased employment. For this additional reason, the Panel should reject the EC’s tax and employment argument.

127. In sum, a finding by the Panel that a private investor would not undertake a particular infrastructure activity because it would be unable to recoup the necessary investment in the market does not affect the analysis of the benefit conferred when the government provides that infrastructure. The question remains whether the government has received adequate remuneration for the infrastructure. Adequacy of remuneration in this case should be evaluated according to the government’s investment into creating the infrastructure plus a commercial rate of return. The remuneration that Airbus paid to government providers of infrastructure in Germany and France unquestionably did not cover the governments’ investment into creating the infrastructure. As a result, Airbus is “better off” than it would otherwise have been, absent that contribution.”¹⁸¹ Therefore, the provisions of infrastructure confer a benefit on Airbus.

E. CAPITAL INVESTMENTS AND SHARE TRANSFERS

¹⁷⁹ U.S. Comments on EC SNCOS, para. 16.

¹⁸⁰ See *US - Softwood Lumber CVD Final (AB)*, para. 95.

¹⁸¹ *Canada - Aircraft (AB)*, para. 157.

156. In its response to Panel Question 100, the EC argues (at paragraph 272) that, in determining whether the purchase of KfW’s 20% stake in Deutsche Airbus was completed on market terms, the question whether Daimler-Benz’s investment in Deutsche Airbus was assisted by a restructuring package is not relevant. Does the United States agree with this assertion, and with the EC’s contention (at paragraph 273 of its response to Panel Question 100) that, provided a government injects capital on equal terms with a private investor following the financial restructuring measures, such an injection does not confer a benefit on the recipient company within the meaning of Article 1.1(b) of the SCM Agreement?

Response:

128. The United States does not agree with either of the EC’s assertions.

129. First, as a factual matter, it is misleading for the EC to refer to Daimler-Benz’s investment in “Deutsche Airbus.” The German government financial contribution that confers a benefit on Airbus and thus constitutes a subsidy was, indeed, an investment in Deutsche Airbus. Specifically, the German state-owned bank, KfW, provided a DM 505 million equity infusion to Deutsche Airbus. Daimler-Benz, however, purchased a 50.3 percent shareholding in Messerschmitt-Bölkow-Blohm AG (“MBB”). Although MBB was the parent company of Deutsche Airbus, MBB also had a large portfolio of other activities, including, in particular, defense-related activities. The risks Daimler assumed when it invested in a company engaged in a diverse range of activities cannot be compared with the risks the German government assumed when it invested in a different company engaged in the single activity of producing large civil aircraft. In attempting to make that comparison, the EC compares apples to oranges.¹⁸²

130. Second, the fact that Daimler-Benz’s investment was assisted by a restructuring package is relevant, as it undermines the use of that investment as a benchmark for analyzing whether an element of the restructuring package – *i.e.*, the DM 505 million equity infusion – was consistent with the usual investment practice of private investors in Germany (and thus whether the infusion confers a benefit¹⁸³). The EC relies on the Daimler transaction to show that the government equity infusion was consistent with the usual investment practice of private investors.¹⁸⁴ But, as the Daimler transaction was heavily influenced by the very same government equity infusion being analyzed, it is not an appropriate benchmark. That is, the Daimler transaction is not an accurate indicator of whether making the investment the German government made was consistent with the usual investment practice of private investors.

¹⁸² See U.S. SWS, para. 452.

¹⁸³ See U.S. FWS, paras. 544-545 (discussing standard for analyzing whether equity infusion confers a benefit); EC FWS, para. 1215 (agreeing with standard articulated by United States).

¹⁸⁴ See EC FWS, para. 1216.

131. The EC tries to portray the German government's restructuring of Deutsche Airbus as entirely separate from its investment in Deutsche Airbus. According to the EC, the German government first undertook a restructuring of Deutsche Airbus, "a financially troubled company."¹⁸⁵ Subsequently, the EC contends, KfW invested in a healthy (restructured) Deutsche Airbus. Based on that hypothetical sequence of events, the EC concludes that "the KfW invested on exactly the same conditions" as Daimler, and that the terms of Daimler's investment were not "tainted" by the restructuring package.¹⁸⁶

132. However, the actual sequence of events was not as described by the EC. Rather, the KfW investment and support for Deutsche Airbus (as a subsidiary of MBB) was an integral part of the restructuring package itself and a prerequisite to Daimler's acquisition of a stake in MBB. Without the restructuring of Deutsche Airbus – including the German government's commitment to a continuing involvement in that company – Daimler would not have invested at all in Deutsche Airbus's parent, MBB. This link is demonstrated by the evidence adduced by the United States,¹⁸⁷ and the EC has confirmed it. Thus, in its first written submission, the EC explained:

{T}he German government found an industrial investor, Daimler-Benz AG ("Daimler"), who would take over Deutsche Airbus and Deutsche Airbus's parent company, Messerschmitt-Bölkow-Blohm GmbH ("MBB"), while being assisted by a one-time package of restructuring measures. . . . {T}he restructuring package contained the following principal elements: . . . 5) time-limited equity investment in Deutsche Airbus by {KfW}. The last element of the restructuring package reflected the continuing interest and stake of the German government in the outcome of the restructuring process."¹⁸⁸

133. In short, the EC's assertion of the irrelevance of the Deutsche Airbus restructuring package is based on the erroneous premise that it was following the restructuring that the German government provided the equity infusion at issue. Because the equity infusion was in fact an integral part of the restructuring, the premise is incorrect, as is the argument that flows from it. The restructuring package is relevant, precisely because it includes the equity infusion under consideration, and because the Daimler investment that the EC cites as a market benchmark would not have occurred without it.

¹⁸⁵ EC Responses to First Panel Questions, paras. 267-268.

¹⁸⁶ EC Responses to First Panel Questions, para. 267.

¹⁸⁷ See U.S. FWS, paras. 546-547.

¹⁸⁸ EC FWS, paras. 1178 and 1180 (emphases added); see also EC SNCOS, para. 258 (acknowledging that German government equity infusion was "part of the overall restructuring of an insolvent company").

134. For this same reason, the second EC contention referred to in the Panel’s question concerns a scenario not at issue in this dispute. This dispute does not involve a government injecting capital “on equal terms with a private investor *following* the financial restructuring measures.” The capital injection at issue was part of the restructuring measures. The Panel need not and should not speculate on the abstract question of whether a capital injection made under different circumstances would have conferred a benefit on the recipient.

135. Finally, the reference to “equal terms” in the second EC proposition is extremely misleading. Daimler’s provision of capital to MBB and the German government’s provision of capital to Deutsche Airbus were not made on “equal terms.”

136. When KfW purchased its Deutsche Airbus shares, it agreed in advance to sell the shares to MBB in 1999. At the same time, it accepted that Deutsche Airbus would not distribute any profits to its shareholders for at least the first eight years of the KfW investment (*i.e.*, from 1989 until 1996). KfW would be entitled only to a (very limited) share of the profits, if any, in 1997 and 1998. In essence, KfW excluded the possibility of realizing a return on its investment. It forfeited profits so that Deutsche Airbus could build its capital base.¹⁸⁹

137. Moreover, it is clear from the arrangement accepted by KfW that the German government was aware that the obligation to sell its Deutsche Airbus shares to MBB in 1999 could lead to a significant loss. Therefore, it was agreed that [

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138. In contrast, Daimler’s investment in MBB was not limited in time. Nor was the investment subject to any limitations as to the distribution of profits. And, as noted above, Daimler had the potential to benefit from profits generated by MBB’s other (*i.e.*, non-LCA) business segments. In fact, at the time of Daimler’s investment, about 75 percent of MBB’s total turnover and all of its profits were generated by activities other than Airbus-related activities. Thus, unlike KfW, Daimler-Benz (i) had no obligation to sell its shareholding in MBB (and

¹⁸⁹ See See Monopolkommission, Zusammenschlussvorhaben der Daimler-Benz AG mit der Messerschmitt-Bölkow-Blohm GmbH, Sondergutachten der Monopolkommission gemäss § 24 Abs. 5 Satz 7 GWB (“Monopolkommission” or “Monopolkommission Report”), para. 132 (Exhibit US-30). In this regard, it also is notable that in 1992, precisely when the German government terminated its equity investment in Deutsche Airbus seven years earlier than originally had been agreed, the terms of the company’s debtor warrant to the German government were amended in a way that, according to the EC, “increased the motivation of Deutsche Airbus to generate profit.” EC FWS, para. 1181. The EC’s acknowledgment that during the period of the government’s equity investment Deutsche Airbus had a lesser motivation to generate profit adds to the demonstration that making that investment was inconsistent with the usual practice of private investors.

¹⁹⁰ See EC FWS, para. 1209.

MBB, in turn, had no obligation to sell its shareholding in Deutsche Airbus) at a time when such a sale would result in a loss, (ii) had the opportunity (and still has it through its shareholding in EADS) to benefit from the expanded capital base of Deutsche Airbus (which had been built up at the expense of KfW), and (iii) in the longer term, will be able to benefit from profits generated and distributed after the Deutsche Airbus capital expansion period.

139. In conclusion, the conditions under which Daimler-Benz made its investment in MBB were far less restrictive than the conditions under which KfW made its investment in Deutsche Airbus and allowed for a far better chance to recoup the investment and to generate a healthy return on the investment. For these additional reasons, the EC's contention that the capital injections provided by Daimler and by KfW were made on "equal terms" is incorrect and should be rejected.

157. How does the United States respond to the EC's argument (at paragraph 268 of its SNCOS) that because it is not possible to conclude that the investment by KfW is a subsidy without a complete assessment of the 1989 restructuring of Deutsche Airbus (which the United States has not challenged), the United States' claims regarding a single element of the 1989 restructuring package (i.e. the KfW capital injection in Deutsche Airbus) should be rejected.

Response:

140. The EC's assertion that it is not possible to conclude that the investment by KfW is a subsidy without a complete assessment of the 1989 restructuring of Deutsche Airbus is incorrect. That assertion rests on the false premise that the U.S. claim regarding the KfW investment is based on "nothing more" than the proposition that "the 1989 restructuring constitutes a subsidy."¹⁹¹

141. The relevance of the 1989 restructuring does not depend on whether it constitutes a subsidy. The restructuring is relevant inasmuch as it was a necessary precondition to the decision by Daimler-Benz to make its investment in MBB. It thus undermines the EC's attempt to use the Daimler transaction as a market benchmark. Daimler's investment fails to show that the German government's earlier investment was consistent with the usual investment practice of private investors, because the Daimler investment would not have occurred but for a restructuring package that included the government investment as an essential component; it is circular reasoning for the EC to refer to the Daimler investment as a benchmark under these circumstances.¹⁹² That proposition is true as a matter of logic, regardless of whether the

¹⁹¹ EC SNCOS, para. 261.

¹⁹² See U.S. FWS, para. 547; U.S. SWS, paras. 451-459; U.S. Response to Panel Question 156, *supra*.

restructuring package constitutes a subsidy within the meaning of Article 1 of the SCM Agreement. For this reason alone, the EC assertion at issue in the Panel’s question is incorrect.¹⁹³

142. Additionally, the EC is wrong to suggest that the status of the KfW investment as an integral part of the 1989 restructuring is the sole basis for the U.S. argument regarding that transaction. The United States has shown that the German government’s equity infusion was inconsistent with the usual investment practice of private investors for a variety of reasons. In particular, the United States pointed to the significant liabilities on Deutsche Airbus’s balance sheet at the time of the infusion; the continued business risks from the falling value of the U.S. dollar vis-à-vis the Deutschmark; the lack of capital with which to finance production of the A320, A321 and A330/340; the impossibility of obtaining such capital from commercial banks; and the impossibility of selling Deutsche Airbus to commercial investors,¹⁹⁴ as admitted by the German government when it explained in November 1988:

{T}he sale {of Deutsche Airbus} to other Airbus partners or through the capital markets is currently impossible, due to the financial problems of the Airbus program.¹⁹⁵

143. The United States also called attention to the fact that the German government itself described the KfW investment in Deutsche Airbus as a “Subvention” or “subsidy.”¹⁹⁶

144. In conclusion, determining whether the German government’s equity infusion to Deutsche Airbus constitutes a subsidy depends on whether that infusion confers a benefit, which, in turn, depends on whether providing the infusion was consistent with the usual investment practice of private investors.¹⁹⁷ Whether other elements of the government’s restructuring package for Deutsche Airbus also constitute subsidies is not relevant to answering the question at hand. The EC’s assertion to the contrary misunderstands the point of referring to the restructuring package and ignores other evidence showing that the equity infusion was

¹⁹³ It is notable that the Tokyo Round Subsidy Code Panel that examined another element of the 1989 restructuring package – the exchange rate guarantee scheme – did so without examining other elements of the restructuring package. *See EEC - Airbus*, paras. 5.1 *et seq.*

¹⁹⁴ *See* U.S. FWS, para. 546; U.S. SWS, paras. 460-462.

¹⁹⁵ German Economics Ministry, Press Release (Nov. 1988), *reprinted in* Daimler-Benz - MBB/Erklärung des Bundesministeriums für Wirtschaft zur Neustrukturierung der Luftfahrtindustrie, Handelsblatt, at 24 (Nov. 3, 1988) (Exhibit US-259) (quoted in U.S. SWS, para. 461).

¹⁹⁶ *See* U.S. FWS, paras. 540, 547 (citing BT-Drs. 13/8409, at 13-14 (Exhibit US-31)).

¹⁹⁷ *See* U.S. FWS, paras. 544-545 (discussing standard for analyzing whether equity infusion confers a benefit); EC FWS, para. 1215 (agreeing with standard articulated by United States).

inconsistent with the usual investment practice of private investors.

158. The United States alleges (at paragraph 614 of its FWS) that the French government’s decision to transfer its shares in Dassault to Aérospatiale was motivated by political and industrial policy considerations. The United States also alleges (at paragraph 616 of its FWS) that, in its efforts to persuade Dassault to agree to the share transfer, the French government agreed to significant Dassault participation in Aérospatiale. In what way does the United States consider these considerations to be relevant to the question whether the transfer of the French government’s interest in Dassault to Aérospatiale conferred a benefit on Aérospatiale (as opposed to the French government or the other shareholders of Dassault)?

Response:

145. In analyzing whether a government equity infusion confers a benefit on the recipient, it is appropriate to consider whether “the investment decision can be regarded as inconsistent with the usual investment practice . . . of private investors in the territory of {the} Member.”¹⁹⁸ The usual investment practice of private investors is to seek to maximize their profits and, to that end, private investors rely on contemporaneous, objective analyses of indicators of a company’s financial and commercial health and performance.¹⁹⁹ In the case of the French government’s transfer of its interest in Dassault to Aérospatiale, therefore, the question is whether the transaction was consistent with this usual investment practice.

146. The United States has shown that it was not. The equity infusion was made at a time when Aérospatiale was experiencing serious financial difficulty.²⁰⁰ Moreover, in transferring its interest in Dassault, the French government gave up the double voting rights associated with its shares – thereby ceding control of Dassault – without receiving compensation from the Dassault family. As Ms. Lauren D. Fox explains in her expert report, “A general standard among financiers for the value of voting control in a typical entity is 30% beyond the value of the

¹⁹⁸ SCM Agreement, Art. 14(a); see U.S. FWS, paras. 561-564 (discussing standard for analyzing benefit conferred by equity infusions); EC SNCOS, para. 267 (agreeing with standard articulated by United States).

¹⁹⁹ See U.S. FWS, para. 564; see also Aswath Damodaran, *Corporate Finance: Theory and Practice* at 11 (2d ed., 2001) (“the objective in corporate finance is to maximize the value of the firm”) (Exhibit US-654); *US - Countervailing Measures (Panel)*, para. 7.60 (referring to owners of newly privatized firm as persons who “should be profit-maximizers, set on obtaining a market return on the entirety of their investment in the privatized company”).

²⁰⁰ See U.S. FWS, paras. 610-614.

individual shares held.”²⁰¹ Based on this standard, the French government’s relinquishment of control of Dassault without compensation translated into a loss of **[[HSBI]]** to the French government.²⁰² Thus, in order to provide new equity to Aérospatiale, the French government had to incur a substantial financial loss.

147. A private investor might knowingly incur such a loss if it had a reasonable expectation of an offsetting financial gain. In this case, the EC states that the French government’s transfer of its Dassault shares to Aérospatiale (resulting in the loss) was undertaken “to facilitate the consolidation and privatization of the French aerospace industry, *i.e.*, the combination of Aérospatiale with Matra Hautes Technologies (“MHT”) to form a new company, Aérospatiale-Matra (“ASM”), which was the subject of a public offering in June 1999.”²⁰³ If a private investor had reason to expect that the financial benefit it would receive from this consolidation and privatization would outweigh the loss it incurred as a result of ceding control of Dassault without compensation, then such an investor might have made the transfer to Aérospatiale that triggered the ceding of control. But, a private investor would first establish a solid basis for forming an expectation regarding the consolidation and privatization. For example, it would undertake studies to determine the financial benefit it could expect to reap from the consolidation and privatization.²⁰⁴

148. However, the government of France undertook no such studies. The EC has identified no basis for the government to have expected that its profit from the formation of ASM would outweigh its loss from ceding control of Dassault without compensation. And, in fact, by the end of the 13-month period following the formation of ASM during which ASM shares were publicly traded, the French government’s stake in the new company lost substantial value, compounding the loss the government had already willingly incurred by ceding control of Dassault without compensation.²⁰⁵

149. The foregoing facts demonstrate that the French government’s transfer of its Dassault shares to Aérospatiale was inconsistent with the usual investment practice of private investors. Having provided Aérospatiale with equity in a transaction that a private investor would not have undertaken, the government conferred a benefit on Aérospatiale within the meaning of Article

²⁰¹ Lauren D. Fox, 1998 Dassault Share Transfer Valuation Report at 6 (“Fox Report”) (Exhibit US-595) (HSBI).

²⁰² The HSBI number referred to above is set out in the Fox Report at 6 (Exhibit US-595) (HSBI).

²⁰³ EC FWS, para. 1165.

²⁰⁴ See U.S. FWS, para. 564 (citing *EC - DRAMs*, para. 7.208).

²⁰⁵ See Fox Report at 6 (Exhibit US-595) (HSBI).

1.1(b) of the SCM Agreement.

150. The two considerations cited in the Panel’s question help to reinforce this conclusion. The government’s agreement to significant Dassault participation in Aérospatiale is a further element of the cost that the government incurred – in addition to ceding control of Dassault without being compensated for the control value of its shares – in order to provide an equity infusion to Aérospatiale. Consideration of this additional cost factor increases the offsetting gain the government would have had to reasonably expect from the formation of ASM in order to make its transfer of the Dassault shares to Aérospatiale consistent with the usual investment practice of private investors.

151. Evidence of the government’s political and industrial policy motivations helps explain the absence of the sort of cost-benefit analysis a private investor would have made. It shows that the government was indifferent to whether its uncompensated loss of control of Dassault and other costs would be outweighed by expected profits from the formation of ASM, because its primary interests lay elsewhere. In view of its political and industrial policy motivations, the government (unlike a private investor) could not consider the relative merits (from a profit-maximizing perspective) of options other than transferring the Dassault shares to Aérospatiale, such as maintaining the status quo (*i.e.*, not forfeiting an element of substantial value associated with its stake in Dassault) or entering into transactions with foreign entities. In sum, evidence of the government’s motivations adds to the demonstration that the government’s equity infusion to Aérospatiale was not consistent with the usual investment practice of private investors.

159. At paragraph 607 of its FWS, the United States notes that, in return for transferring its 45.76% interest in Dassault Aviation to Aérospatiale, the French government received additional Aérospatiale stock in return. Yet, at paragraph 105 of its SNCOS, the United States asserts that, as a result of this transfer, Aérospatiale received a valuable asset “for which it paid nothing.” Does the United States challenge the exchange ratio for the new shares in Aérospatiale that were issued to the French government in exchange for the Dassault shares? If not, what is the benefit that the United States alleges was conferred on Aérospatiale as a result of the transfer of the Dassault shares?

Response:

152. It is accurate that the French government received additional Aérospatiale shares in exchange for the transfer of its Dassault shares to Aérospatiale. In fact, the net book value of the Dassault shares exceeded the nominal value of the newly issued Aérospatiale shares by about FF 1.731 billion (which difference Aérospatiale recorded as “additional paid-in capital”).²⁰⁶ While this difference could be construed as constituting a benefit to Aérospatiale, that is not the

²⁰⁶ See Aérospatiale Matra Offering Memorandum at 24 (Exhibit EC-53).

primary basis for the U.S. claim. As the EC points out, “the exchange ratio is of no economic significance,” due to the French government’s 100 percent ownership of Aérospatiale and of the transferred Dassault shares.²⁰⁷ It was in recognition of the fact that Aérospatiale’s share issuance in exchange for the Dassault shares was simply a matter of accounting that the United States explained, in its second non-confidential oral statement, that Aérospatiale “received a valuable asset for which it paid nothing.”²⁰⁸

153. The primary benefit to Aérospatiale from the French government’s contribution of the Dassault shares was that it received an equity infusion through a transaction inconsistent with the usual investment practice of private investors in France. For reasons explained in previous submissions and summarized in response to Question 158, above, a private investor would not have engaged in the transaction that resulted in Aérospatiale’s receipt of the Dassault shares. At a time when Aérospatiale was in dire financial circumstances, the government incurred considerable costs – including, notably, ceding control of Dassault without any compensation – in order to provide new capital to Aérospatiale. The consequence for Aérospatiale was a significant boost to its balance sheet – a 20 percent increase in its equity.²⁰⁹

154. The EC suggests that any benefit conferred by the government’s equity infusion to Aérospatiale was canceled by the compensation the government received for the Dassault shares in the formation of ASM.²¹⁰ Even if the EC were correct (which it is not) that the government received the fair market value of the Dassault shares in the ASM transaction, that still would not account for the government’s uncompensated sacrifice of the value attributable to its control of Dassault.²¹¹ Moreover, as the Fox Report shows, the investment bank valuations relied upon in the ASM transaction were not consistent with the usual investment practice of private investors. Based on information the EC has designated as HSBI, Ms. Fox shows that these valuations

²⁰⁷ EC FWS, footnote 939.

²⁰⁸ U.S. SNCOS, para. 105.

²⁰⁹ See U.S. FWS, para. 614.

²¹⁰ See EC Responses to First Panel Questions, para. 278.

²¹¹ The EC asserts that the French government did not receive compensation for relinquishing control of Dassault because it could not sell its right of control to a third party (*i.e.*, an entity other than the Dassault family). See EC SNCOS, paras. 276-280. But, the point is not that the government should have sold its control rights to a third party. Rather, the point is that by ceding control of the company to the Dassault family, the French government gave the Dassault family something of substantial value for which it received no compensation, even though a 30 percent premium usually attaches to control. (See Fox Report, p. 6 (Exhibit US-595 (HSBI)).) That was a significant cost of transferring the Dassault shares to Aérospatiale. A private investor knowing that it would not be compensated for relinquishing control to another shareholder of the company either would have retained control or relinquished it only upon a reasonable expectation of profits outweighing the substantial financial sacrifice. The French government did neither of these things.

appear to have been developed with a view to confirming the pre-negotiated valuation ratios of the parties to the transaction.²¹²

155. In conclusion, whatever the significance of the ratio between Dassault shares and Aérospatiale shares may be, the main benefit conferred on Aérospatiale by the infusion of Dassault shares was a substantial capital increase in a transaction that was inconsistent with the usual investment practice of private investors.

160. The EC argues (at paragraph 553 of its SWS) that the French government’s transfer of its interest in Dassault Aviation to Aérospatiale was undertaken for the purpose of consolidating its holdings in both Dassault and Aérospatiale in anticipation of a combined sale of both entities. Does the United States contend that such conduct is inconsistent with the usual investment practice of a private investor in the territory of the allegedly subsidizing Member?

Response:

156. Consolidating holdings in two different entities in anticipation of a combined sale could be consistent with the usual investment practice of a private investor in France if any financial losses knowingly incurred as a result of the consolidation were offset by a reasonable expectation of financial gains. However, that is not what happened when the French government transferred its Dassault shares to Aérospatiale, as discussed in the responses to Questions 158 and 159, above. In that case, the government knowingly forfeited something of substantial value – its control of Dassault. Assuming the value of control to be “30% beyond the value of the individual shares held” – an assumption the EC does not dispute – the government suffered a loss of **[[HSBI]]** in the transfer of Dassault shares that triggered its forfeiture of control.²¹³ A private investor would not have knowingly incurred such a substantial financial loss without having a reasonable expectation of an equally substantial or greater offsetting financial gain.

157. The EC repeatedly asserts that the French government transferred its Dassault shares to

²¹² See Fox Report, pp. 4-5 (Exhibit US-595 (HSBI)); see also U.S. SWS, paras. 483-486; U.S. Comments on EC SNCOS, paras. 10-11.

²¹³ The number designated as HSBI is set out in the Fox Report at 6 (Exhibit US-595) (HSBI). As noted in the response to Question 159, above, the EC dismisses the significance of the French government’s forfeiture of control because its control interest in Dassault was non-transferrable. See EC SNCOS, paras. 276-280. But, this misses the point. Whether the government could have sold its control interest to a third party or not does not change the fact that it gave up something of substantial value. It ceded control to the other major shareholder in Dassault, the Dassault family, without receiving any compensation. That was a significant cost of transferring the Dassault shares to Aérospatiale. A private investor knowing that it would not be compensated for relinquishing control either would have retained control or relinquished it only upon a reasonable expectation of profits outweighing the substantial financial sacrifice. The French government did neither of these things.

Aérospatiale in the hope that doing so would “realize synergies and create wealth.”²¹⁴ However, the EC offers no evidence that whatever wealth the government reasonably expected to create for itself offset the wealth that unquestionably was destroyed when the government ceded its valuable control interest in Dassault without compensation. The usual investment practice of a private investor in this situation would have been to undertake a study of the anticipated combination and sale of assets to determine how much wealth it could expect to be created by these transactions.²¹⁵ However, the EC offers no evidence of any such studies by the French government. Other evidence, as discussed in the U.S. first written submission, indicates that the “synergies” to which the EC refers are synergies relating to the government’s political and industrial policy considerations, rather than considerations of profit maximization.²¹⁶

158. In sum, in this case – where the government’s consolidation of assets in anticipation of a combined sale forfeited substantial value without a reasonable expectation of creating offsetting value for itself – the government’s action was inconsistent with the usual investment practice of private investors. As this action resulted in Aérospatiale receiving an equity infusion that a private investor would not have provided, Aérospatiale received a benefit within the meaning of Article 1.1(b) of the SCM Agreement.

161. At footnote 668 to para. 552 of its FWS, the United States contends that, if the Panel were to find that the 1992 transfer by KfW of its shares in Deutsche Airbus to MBB is in fact a grant (and thus a subsidy) in the amount of DM 505 million, the United States does not believe it would be necessary for the Panel to determine whether the original 1988 share purchase by KfW was also a subsidy. Given the bases on which the United States claims that each of the KfW transactions amounted to subsidies, can the United States please explain the reason for this contention?

Response:

159. When the United States submitted its first written submission, the EC had not yet provided any information concerning the 1992 transfer by KfW of its shares in Deutsche Airbus to MBB, despite efforts to clarify the details of that transaction during consultations and the

²¹⁴ See, e.g., EC SWS, para. 555; EC FWS, footnote 941.

²¹⁵ See, e.g., *Korea - Commercial Vessels*, para. 7.437; *EC - DRAMs*, para. 7.208; *Japan - DRAMs*, para. 7.128 (quoting findings of Japan investigating authorities).

²¹⁶ See U.S. FWS, para. 615; Adam Sage, *France makes first move in European defence shake-up*, The Times (May 16, 1998) (Exhibit US-312) (noting concern of French Defence Ministry that “France may find itself on the sidelines as Europe’s defence industry presses ahead with restructuring”).

Annex V process.²¹⁷ Accordingly, the United States laid out its argument in that submission based on publicly available information. That information showed that KfW had provided DM 505 million to Deutsche Airbus in 1989, at a time when the company's financial situation was exceedingly poor, in exchange for a 20 percent shareholding.²¹⁸ It also showed that KfW had agreed to return its shares not later than 1999, and that the return date was accelerated to 1992, following issuance of a report by a Tokyo Round Subsidy Code panel finding another element of the German government's aid package to Deutsche Airbus – an exchange rate guarantee scheme – to be a prohibited export subsidy. The publicly available information showed that the early return of shares was carried out to compensate Deutsche Airbus for termination of the exchange rate guarantee scheme. The logical inference to be drawn from this information was that KfW's shares in Deutsche Airbus were returned without payment.²¹⁹

160. KfW's 1992 uncompensated return of Deutsche Airbus shares could be considered as converting its original provision of a DM 505 million equity infusion to Deutsche Airbus in exchange for shares into an outright grant. Accordingly, the United States believed it to be unnecessary for the Panel to make a separate finding regarding the original 1989 transaction if it were to find that Airbus effectively had received a DM 505 million grant as a result of the 1992 return of shares. This was the point of footnote 668 in the U.S. first written submission.

161. Subsequently, in its first written submission, the EC provided information concerning the 1992 transaction. That information suggests that KfW's transfer of Deutsche Airbus shares to MBB was not uncompensated.²²⁰ If that information is accurate (an assumption that cannot be verified, due to the absence of supporting evidence from the EC), then the transfer should not be considered as converting the original equity infusion into an outright DM 505 million grant, although the transfer still amounts to a financial contribution that confers a benefit and thus constitutes a subsidy.²²¹

162. If the Panel were to accept the EC's unsubstantiated characterization of the terms of the 1992 share transfer, then the Panel should make findings regarding both the original DM 505 million equity infusion and the subsequent share transfer. In particular, as previously discussed, the Panel should find: (i) that the original equity infusion constitutes a subsidy (inasmuch as

²¹⁷ See EC Responses to Questions from the Facilitator, Responses to Questions 127-129 (Exhibit US-5 (BCI)).

²¹⁸ See U.S. FWS, paras. 540-547.

²¹⁹ See U.S. FWS, paras. 549-555.

²²⁰ See, e.g., EC FWS, paras. 1207-1209.

²²¹ See U.S. Responses to First Panel Questions, paras. 206-212; see also U.S. Response to Question 156, *supra*.

providing that infusion was inconsistent with the usual investment practice of private investors and thus confers a benefit),²²² and (ii) that, even assuming, *arguendo*, the payment the EC says KfW received when it sold its Deutsche Airbus shares to MBB in 1992, that equity infusion also constitutes a subsidy (inasmuch as providing that infusion was inconsistent with the usual investment practice of private investors and thus confers a benefit).²²³

F. ADVERSE EFFECTS

162. Given the number of different measures that the United States is challenging in this dispute, how does it respond to the EC’s suggestion, at para. 373 of its SNCOS, that any assessment of adverse effects must proceed on a subsidy-by-subsidy basis, unless it is demonstrated that the “structure, design and operation of the subsidies is sufficiently similar”.

Response:

163. As a preliminary matter, the United States notes that while the EC in its oral statement purports to be following the approach of the panel in *US – Cotton Subsidies*,²²⁴ the EC misstates that panel’s analysis. For the EC, the *Cotton* panel “stated that a cumulative assessment of the subsidies is only permitted if the structure, design and operation of the subsidies is sufficiently similar,”²²⁵ but the panel said no such thing. Rather, the panel stated that its view of the SCM Agreement would “permit an integrated examination of effects of any subsidies with a sufficient nexus with the subsidized product and the particular effects-related variable under examination.”²²⁶ Based on this legal interpretation, the panel stated that it would conduct “an analysis focusing on the existence and nature of the subsidies in question by examining their structure, design and operation with a view to discerning their effects.”²²⁷ Thus, it is not the “structure, design and operation” of the subsidies in themselves, considered apart from the alleged effects, that were relevant for the *Cotton* panel’s analysis. Rather, the key factor was whether different subsidies had cumulative effects with respect to the particular “effects-related variable” at issue, taking into account the “structure, design and operation” of each subsidy.

²²² See U.S. FWS, paras. 543-548; U.S. SWS paras. 447-462.

²²³ See U.S. Responses to First Panel Questions, paras. 206-212.

²²⁴ EC SNCOS, para. 360 (citing *US – Cotton Subsidies (Panel)*, paras. 7.1191-7.1194).

²²⁵ EC SNCOS, para. 360.

²²⁶ *US – Cotton Subsidies (Panel)*, para. 7.1192.

²²⁷ *US – Cotton Subsidies (Panel)*, para. 7.1194 (footnote omitted, emphasis added).

164. This can be seen from the cumulation analysis that the *Cotton* panel actually undertook. The panel considered cumulatively four different sets of payments – marketing loan program payments, user marketing (Step 2) payments, market loss assistance payments, and counter-cyclical payments. These payments shared a common attribute, in that all were linked, in one way or another, to the world price of cotton.²²⁸ At the same time, many aspects of the “structure, design, and operation” of these payments were quite different from one another. For example, marketing loan payments were made to producers of upland cotton, while user marketing (Step 2) payments were made to *purchasers* of upland cotton, and market loss assistance and counter-cyclical payments were made to holders of *historic acreage* without reference to current production of upland cotton.²²⁹ Other subsidies that were not directly related to world cotton prices were not cumulated with these “price-contingent subsidies.”²³⁰ For the *Cotton* panel, the point of similarity in the “structure, design, and operation” of different subsidies – their relationship to world cotton prices – outweighed points of difference in the “structure, design, and operation” of those subsidies – for example, the recipients of the different payments – precisely because of the “nexus” with the alleged adverse effect in that dispute, namely the alleged suppression of world cotton prices.²³¹

165. Thus, that the EC can identify differences in the various subsidy measures challenged by the United States in this dispute is not dispositive for determining whether a cumulative analysis is appropriate, and nothing in the report of the *Cotton* panel suggests otherwise. Rather, where the “structure, design, and operation” of different subsidies are such that the *subsidies* work along the *same causal pathway* to cause the same types of adverse effects, the effects of those subsidies may be cumulated. Likewise, if the “structure, design, and operation” of the different subsidies is such that they relate differently to the alleged effects, then cumulation would not be proper.

166. In this regard, the United States has shown that all of the challenged subsidies in this dispute share a key characteristic that leads them to have similar market effects: All of the subsidies provide capital at below-market rates to support specific LCA development projects. Without this subsidized support for LCA development, Airbus would not have been able to pursue the business strategy that it did – i.e., launching the LCA models that it did, when it did, and selling them for the prices that it did. This business strategy, in turn, leads directly to the adverse effects measured by each of the “effects-related variables” identified by the United States.

²²⁸ US – *Cotton Subsidies (Panel)*, para. 7.1290.

²²⁹ US – *Cotton Subsidies (Panel)*, paras. 7.1290, 7.1299, 7.1302.

²³⁰ US – *Cotton Subsidies (Panel)*, para. 7.1307.

²³¹ US – *Cotton Subsidies (Panel)*, para. 7.1303.

167. Thus, Launch Aid, EIB loans, infrastructure supports, and research grants all provide Airbus with capital to develop LCA at rates well below the market cost of each such form of capital. The EC has identified differences among these subsidies, but these differences – like those among the “price-contingent” subsidies in *Cotton* – do not alter the reality that each of them shares the key characteristic of providing below-market capital to Airbus to facilitate LCA development.

- The EC asserts that the EIB is an “independent institution,” but EIB loans work cumulatively along the same causal pathway with Launch Aid provided by the Airbus governments in providing funding for LCA development at below-market rates.
- The EC has failed to provide specific information about research funding, notwithstanding repeated requests. Nonetheless, publicly available information demonstrates that EU Framework programs such as TANGO, for example, “directly supported the development of production methods for . . . the A380.”²³² Likewise, Hamburg grants supported “the development, integration, and testing of the cabin systems of the Airbus A380 as part of the CASIV (Cabin System Integration and Verification testing) project.”²³³ These subsidies for model-specific design research worked cumulatively – particularly from the viewpoint of Airbus, the recipient of the subsidies – along the same causal pathway with Launch Aid in providing funding for LCA development at below-market rates.²³⁴
- That Airbus [] in dividing the final A380 assembly line between Hamburg and Toulouse does not change the fact that the infrastructure subsidies that defray the costs of building both A380 assembly facilities worked cumulatively – particularly from the viewpoint of Airbus, the recipient of the subsidies – along the same causal pathway with Launch Aid in providing funding for LCA development at below-market rates.

168. The United States has also identified HSBI evidence provided by the EC that illustrates

²³² Technologies Ltd., *The Impact of EU Framework Programmes in the UK* at 58 (July 2004) (“The TANGO project directly supported the development of production methods for the composite center wing box of the A380 and the design of the planned composite fuselage replacement for the A320.”) (Exhibit US-655).

²³³ Werum Software & Systems, Pressemitteilung Messdatenmanagementsysteme, Testdatenmanagementsystem von Werum im Einsatz für Tests des A380 (Exhibits US-483 and US-483a).

²³⁴ The chart in Exhibit US-634, which was prepared by the European Commission, highlights the contributions of EC and Airbus government research subsidies to a number of specific aspects of A380 development.

how Airbus itself links Launch Aid and infrastructure subsidies,²³⁵ as well as Launch Aid and research grants.²³⁶ The EC also explains how equity infusions operate to lower the cost of certain funds provided for LCA development and to strengthen the capital position of Airbus after it launched certain LCA models and as it prepared to launch new LCA models:

Aérospatiale used the new capital to fund expansion, including in its LCA operations. The late 1980s through the first half of the 1990s was a critical period for Airbus. 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 growth, especially as Boeing was itself investing in major new programmes.²³⁷

Contemporaneous documents show that Airbus, as the subsidy recipient, also viewed these equity infusions as necessary because [

].²³⁸ And the 1997 French Senate report on the future launch of the A380 points out that, even in the unlikely event that private financing for the A380 could have been found in the absence of Launch Aid, “such external financing would weigh heavily on the financial costs of the company and would throw its balance sheet out of equilibrium, taking account of the weakness of its own equity.”²³⁹ Through both equity infusions and debt forgiveness, the Airbus governments offset the impact of rapid product development on Airbus’s balance sheet, allowing Airbus to attract private capital and engage in pricing strategies that would not otherwise be possible.

169. Thus, each of the challenged subsidies provides Airbus with below-market capital for the development of particular LCA, allowing Airbus to launch new LCA models without regard for its financial position at the time of launch and strengthening its capital position as it sells existing LCA models and prepares for new launches. In this way, each of the challenged subsidies has led in the same way to each type of adverse effects demonstrated by the United

²³⁵ U.S. SCOS, paras. 51-53.

²³⁶ U.S. FWS, HSBI App., Section X.

²³⁷ EC FWS, para. 1133.

²³⁸ Aérospatiale Report to Credit Lyonnais (1994) at 1 (Exhibit US-296) (BCI).

²³⁹ French Senate Report (1997) at 72 (Exhibit US-18) (“Mais, surtout il apparaît qu’un tel financement extérieur alourdirait beaucoup les charges financières des entreprises et déséquilibrerait leur bilan compte tenu de la faiblesse de leurs fonds propres.”).

States. Accordingly, the “structure, design, and operation” of each subsidy demonstrates the existence of the “nexus” between each subsidy, Launch Aid, and the several effects-related variables in this dispute that permits the cumulative examination of their effects.

163. The EC suggests at paragraph 393 of its SNCOS, that the United States considers that the “effect of MSF loans extended exclusively to finance the development of the A380” is not different from “the effect of MSF loans extended exclusively to finance the development of the A320” and that “both sets of measures would have identical effects on sales campaigns for A320, A330, A340 and A380 aircraft”? Does the United States agree with the EC’s characterisation of its view? If so, would the United States please explain why it takes this view, in light of the difference in the age of the two measures. If not, would the United States please explain why not, and what differences in the effect of the two measures it considers relevant, and why?

Response:

170. As usual, the EC misrepresents the U.S. arguments. The United States does not suggest that each instance of Launch Aid, viewed in isolation, has an identical effect. Rather, the United States emphasizes that each instance of Launch Aid facilitates the development of a particular model that is part of the Airbus LCA family. What the United States has demonstrated is that the effects of each instance of Launch Aid are not limited to the particular LCA model for which funding was provided and, accordingly, each instance of Launch Aid operates in a similar way to affect sales campaigns involving all Airbus LCA. Specifically, the United States has shown that each provision of Launch Aid has allowed Airbus to add another LCA model to its product offerings, thereby reinforcing the marketability and strengthening the sales of its other LCA models, and that each provision of Launch Aid has shored up Airbus’s financial position, enabling Airbus to pursue its strategy of underpricing Boeing to gain sales and market share at the same time that it devotes its resources to develop new LCA models. These effects are not limited by the age of each Launch Aid disbursement, given that each LCA model is still being produced and sold and that Airbus continues to make below-market repayments on its outstanding Launch Aid debt.²⁴⁰

171. With respect to the two instances of Launch Aid referenced by the EC – the A320 and the A380 – the United States has shown that, in both cases, Airbus would not have launched the LCA model in question had the Airbus governments not provided Launch Aid. The EC does not contest this showing for the A320, and the EC efforts to rebut this showing for the A380 fail to contradict the statements of the Airbus governments themselves that Launch Aid was necessary

²⁴⁰ Although Airbus ceased production of the A300/A310 in July 2007, this model was being marketed and sold throughout the reference period.

for the launch of the A380.²⁴¹ Both LCA models are being actively marketed and sold at prices undercutting those of Boeing, and sales of these LCA models have contributed to Boeing's significant loss of market share. Further, as the recent U.S. Airways campaign illustrates, Airbus uses the A320 to assist in the marketing of other Airbus aircraft and uses newer Airbus models to help sell the A320.²⁴²

172. Without Launch Aid for the A320, Airbus would not have launched the A320 when it did. The United States has shown that the EC recognized at the time that both Boeing and McDonnell Douglas, as well as Airbus, were considering new launches in the single-aisle segment of the LCA market, and that there was "room for only two planes in this market."²⁴³ An Airbus that did not launch the A320 would be a very different Airbus from the one that exists today. Likewise, an Airbus that did not launch the A380 would be a very different Airbus from the one that actually exists, given the substantial impact of the A380 not only in the very large aircraft segment of the market but on all of Airbus's LCA models. The age of the A320 Launch Aid may make it more speculative to say precisely *how* Airbus would be different today "but for" the subsidy, but it is not speculative to say *that* Airbus – and thus the LCA market as a whole – would be different.

173. Likewise, Launch Aid for the A320 and Launch Aid for the A380 both contribute to relieving the financial constraints on Airbus during the reference period. Launch Aid for the A380 brought billions of Euro into Airbus on backloaded, success-dependent terms during the period when Airbus was spending billions to bring the A380 to market, but before it was able to begin collecting payments for delivered aircraft.²⁴⁴ These funds, provided at below-market interest rates and contingent upon the success of the program, greatly reduced the financial constraints that the massive and risky A380 launch program would otherwise have had on Airbus and enabled Airbus to pursue additional launches and price cuts for other LCA models, including the A320, during this period when its resources would otherwise have been even more greatly absorbed by the A380 project (not to mention the completion of the launch of the A340-500/600

²⁴¹ U.S. FWS, para. 833 and sources cited therein; *see also* Hansard (Apr. 7, 2000), col. 622W (answers of Mr. Alan Johnson) ("As part of the assessment of the BAe Systems application for launch investment, my Department received independent advice from Pricewaterhouse Coopers (PWC). In their report, PWC looked at the case for Government investment in the A3XX, including the other alternatives open to BAe Systems. Although the details of the report are commercially confidential, the conclusion was that, in the absence of launch investment from the UK, BAe Systems would not undertake the A3XX work in the UK.") (Exhibit US-656).

²⁴² U.S. SNCOS, para. 151 (citing Exhibits US-641 and US-642).

²⁴³ *Battle of the Aircraft Giants*, Industry Week (Dec. 14, 1981) (Exhibit US-435) (quoting European Commission aerospace analyst Ernesto Previdi).

²⁴⁴ *See* U.S. Comments on EC SNCOS at the Second Panel Meeting, para. 46.

and preparations for the launch of the A350, both also being undertaken at the same time).²⁴⁵

174. Launch Aid for the A320 had similar effects during the initial launch phase of the A320, which likewise came during a period when revenues from the A300 and A310 were coming in too slowly to support the development of the A320 in the absence of Launch Aid – as the chairman of an Airbus company stated publicly at the time²⁴⁶ – and when Airbus was also moving to launch the A330 and A340 in quick succession to the A320. In addition, the subsidized interest rate for A320 Launch Aid significantly reduced the per-plane repayments that Airbus had to make on A320 sales once A320 production had begun. Had the Airbus governments charged a market return for A320 Launch Aid, the per-plane repayment rate would have more than doubled – an increase ranging from [] would have been required.²⁴⁷ In this way, below-market financing for the A320 continues to provide benefits to Airbus as long as the A320 Launch Aid remains outstanding.

175. Thus, the United States does not assert that the impact of Launch Aid for the A320 and for the A380 is “identical.” Rather, the United States has shown that both instances of Launch Aid have operated in similar ways to distort the LCA market – to enable Airbus to launch aircraft models it could not have otherwise launched, and to relieve the financial constraints on Airbus, both to the detriment of the U.S. LCA industry.

164. Does the United States accept the view that lost sales must result from price competition alone in order to substantiate a claim of serious prejudice on this basis?

Response:

176. No. Article 6.3(c) provides that serious prejudice may arise where “the effect of the subsidy is . . . significant . . . lost sales in the same market.” To sustain a claim of lost sales under Article 6.3(c), therefore, the complaining Member must show that (1) there were lost sales, (2) the lost sales were significant, (3) the lost sales were in the same market, and (4) the lost sales were the effect of the subsidy. The nature of the competition leading up to the lost sale is relevant to assessing the third and fourth of these elements, but nothing in the SCM Agreement requires that *price* be the decisive element of this competition.

177. The existence of actual competition between Boeing LCA and Airbus LCA for the particular sales that the United States has alleged as “lost sales” demonstrates that Boeing LCA

²⁴⁵ See response to Question 169, below.

²⁴⁶ *Costs Push British Toward Joint Efforts*, Aviation Week & Space Technology (May 30, 1983) (citing Sir Austin Pearce, chairman of British Aerospace) (Exhibit US-439).

²⁴⁷ See Exhibit US-644 (BCI).

and Airbus LCA are competing in the “same market.” The United States has shown for each alleged lost sale that Boeing either offered an existing Boeing LCA model or, in the case of sales lost to the A380 at Singapore Airlines, Emirates Airlines, and Qantas, offered a proposed modification of the Boeing 747 that it was prepared to develop if customers could be found.²⁴⁸ Thus, Boeing LCA and Airbus LCA were in each case present in the “same market,” whether that market is defined as the world LCA market or any subdivision thereof.

178. The United States has shown that the lost sales were “the effect of the subsidy” in different ways, depending on the particular factors at issue in each individual sale. In some cases – particularly for Boeing 737 sales lost to the Airbus A320 at “low-cost” carriers such as easyJet, Air Berlin, AirAsia, Frontier Airlines, and Virgin America – the publicly available evidence demonstrates (and confidential evidence confirms) that Airbus won these sales primarily by offering a lower price than Boeing as part of a concerted effort by Airbus to increase its market share.²⁴⁹ In these cases, the United States has shown that, by significantly relieving the financial constraints that would otherwise have been imposed on Airbus by its aggressive product development strategy at the time of these sales, Launch Aid and other subsidies had a significant effect on the ability of Airbus to pursue its pricing strategy and therefore to win these sales.

179. The effects of the subsidy on Airbus’s pricing policies are therefore relevant to the analysis of these lost sales. However, this is not because the SCM Agreement requires that lost sales be demonstrated on the basis of competition on price. Rather, it is because the evidence shows that price was the key determining factor in the outcome of these particular sales. Thus, in order to show that *these* lost sales were “the effect of the subsidy,” the effect of the subsidy on Airbus prices is a relevant consideration.

180. However, in other sales the evidence indicates that the availability of an Airbus model with particular characteristics was also a significant factor in Airbus’s winning, and Boeing’s losing, the sale. According to the EC, the sales Boeing lost to the Airbus A340-500/600 (such as at Iberia Airlines, South African Airways, and Thai Airways International) and to the Airbus A380 are attributable to [

] ²⁵⁰ In these cases, the United States has shown that but for the challenged subsidies, Airbus would not have been able to offer the aircraft models that it did, at the time that it did.²⁵¹ Thus, even accepting the EC’s argument with respect to these sales, this is sufficient to show that these “lost sales” are the “effect of the subsidy,” distinct from any effect

²⁴⁸ U.S. FWS, paras. 779-796.

²⁴⁹ U.S. FWS, paras. 739-740, 779-787; U.S. SWS, HSBI App., paras. 15-26

²⁵⁰ EC FWS, paras. 2095, 2110, 2110.

²⁵¹ U.S. Responses to First Panel Questions, para. 309..

of the subsidy on the price of the Airbus aircraft in question.

165. Referring to paragraph 176 of the United States’ SNCOS, is it the United States’ view that, if the Panel finds that the adverse effects claimed by the United States exists, this demonstrates that the subsidies in dispute are of sufficient magnitude to have caused those effects? If so, could the United States explain how the existence of adverse effects demonstrates that the subsidies in dispute are of sufficient magnitude? Does the United States consider that any other factors that may have contributed to those effects need not be taken into account in the analysis of causation?

Response:

181. The United States does not suggest that the existence of indicators of adverse effects (declining market share, depressed prices, etc.), on their own, establish that the subsidies have caused those effects. Rather, the United States has argued that the magnitude of the subsidy is one factor among others that is relevant to assessing the existence of a causal link and that if the causal link is established by reference to other factors, further analysis of the magnitude of the subsidy is unnecessary. Indeed, the SCM Agreement does not impose any threshold in terms of the magnitude of the subsidy. Rather, the question is the magnitude of the effects – for example, “serious” prejudice, or “significant” price suppression.

182. According to the *Cotton* dispute, the SCM Agreement imposes no requirement to measure the subsidy benefit with precision in order to substantiate a claim of adverse effects. Rather, as the Appellate Body observed, the magnitude of the subsidy is one, but only one, factor that may indicate whether particular market developments are, in fact, the “effect of the subsidy,” and that the importance of any given factor may vary from one case to another.²⁵²

183. In paragraph 176 of its oral statement, the United States was simply observing that it is possible to demonstrate through other types of evidence that the subsidy did in fact have a material, indeed decisive, effect on all of Airbus’s major launch decisions and that, given this evidence, further inquiry into the magnitude of the subsidy was not necessary. These other types of evidence include the public statements of EC and Airbus officials, confidential analyses of the economics of particular launch decisions where available, and the EC’s admissions with respect to the launch decisions for the A300, A310, A320, A330, and A340.

184. However, it should be noted that the United States has also shown, through its analysis of the magnitude of the subsidy, that the subsidy was sufficient to materially affect the launch decisions of Airbus. The NERA study quantifying the effect of the subsidy on Airbus shows that, had Airbus obtained financing similar to Launch Aid at a commercial interest rate, the

²⁵² US – *Cotton Subsidies (AB)*, para. 461.

burden of such debt would have been unsustainable and would quickly have spiraled out of control.²⁵³ But this is simply another way of saying that Airbus could not have launched all of the LCA models that it has without subsidies – had it done so, it would be hopelessly mired in debt. Precisely how much debt, and exactly how hopelessly Airbus would be mired in it, is of far less importance than the essential fact that the magnitude of the subsidy is sufficient such that Airbus could not have done what it did without the subsidy. The SCM Agreement requires nothing more.

166. Referring to paragraphs 634 - 636 of its SWS, could the United States please specify how it considers that subsidies facilitating the development of one Airbus LCA model improve the marketability of all Airbus LCA models? Could the United States give examples of “technologies or production facilities developed as part of the launch of one Airbus LCA model ... used or incorporated into production of other Airbus LCA models, both those already in existence and those developed later”? Could the United States give examples of “commonality,” or common elements among different LCA models that reduce the cost of operating multiple Airbus LCA models”?

Response:

185. In paragraphs 633 to 639 of its second written submission, the United States set forth six independent reasons to support the conclusion that the “subsidized product” in this dispute is all Airbus LCA. The United States appreciates the opportunity to further clarify and summarize the evidence supporting the three particular such reasons identified by the Panel.

186. In paragraph 634 of its submission, the United States explained that “technologies or production facilities developed as part of the launch of one Airbus LCA model are used or incorporated into production of other Airbus LCA models, both those already in existence and those developed later.” Several types of evidence support this conclusion.

187. First, several Airbus models share production facilities. The A330 and A340 – separate subsidized products according to the EC – are produced on the same production line; indeed Airbus identifies a single production rate for the two models.²⁵⁴ Further, the location of different production lines in the same Airbus facility creates certain production efficiencies, as has been

²⁵³ See U.S. SWS, paras. 610-613 (citing NERA report submitted as Exhibit US-606); U.S. Responses to First Panel Questions, paras. 254-257 & Exhibit US-502.

²⁵⁴ Airbus press release, *Airbus boosts production rate for its single aisle aircraft to record levels* (May 16, 2007) (Exhibit US-660).

identified for the A319/A321 and the A380 lines in Hamburg.²⁵⁵

188. Second, LCA features developed for one LCA model are frequently incorporated into other LCA models. This has been an Airbus policy from the beginning:

“In the 1980s, we were able to widen our family by launching the A310 that incorporated many systems and power plant improvements that had occurred in the years since the A300 was designed,” an Airbus executive said. “Then we turned around and put many of the A310 improvements back into the A300 and came up with an updated aircraft that we designated the A300-600. The same philosophy will be followed with our new aircraft. Additionally, there is a strong possibility that the A320/A330/A340 technology can be used as well to create an advanced A300 and/or A310”²⁵⁶

This policy continues until the present day, as Airbus is currently touting how features developed for the A380 will be incorporated into the new A350:

The Integrated Modular Avionics (IMA) concept Airbus successfully developed for the A380 will also be adopted on the A350XWB. IMA on the A380 manages 23 functions of systems such as avionics, landing gear, fuel, brakes and pneumatics. IMA will be extended further on the A350XWB to manage up to 40 functions and include new ones such as the oxygen system, full cabin pressurisation system and fire detection.²⁵⁷

189. Third, production technologies that Airbus develops for one LCA launch can also be used to lower costs in producing other LCA. For example, Airbus explains:

It took 10 years of rigorous development and testing before composites were applied to the A310-300. Because of its R&D efforts and investment in composite technology, Airbus is now in a position to offer the benefits of greater use of composites to its customers for its new generation of aircraft.²⁵⁸

The United States would further refer the Panel to additional HSBI materials on this point

²⁵⁵ U.S. SNCOS, para. 153 (quoting AREA, *A380-Werkserweiterung im Mühlenberger Loch – eine Bilanz*, at 1 (Exhibit US-182) (stating that Hamburg is the only place where the synergies with the existing A319 and A321 standard fuselage airplanes could be utilized” in A380 production)).

²⁵⁶ Jeffrey Lenorovitz, *Airbus Industrie Launching Production for New A330/A340 Simultaneously*, *Aviation Week & Space Technology* (Feb. 24, 1986) (Exhibit US-391).

²⁵⁷ Airbus Letter (May/June 2007) at 6 (Exhibit US-657).

²⁵⁸ Airbus North America, *Key Determinants of Competitiveness in the Global Large Civil Aircraft Market: An Airbus Assessment* (Mar. 2005) at 13 (Exhibit US-379).

already cited by the United States.²⁵⁹

190. Next, in paragraph 625 of its submission, the United States explained that “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.” Airbus itself stresses the importance of this feature:

Airbus is sensitive to the way an airline’s profitability can stand or fall by how closely it matches capacity to demand and how quickly it can adapt its fleet. For this reason, Airbus aircraft offer the highest possible degree of commonality in airframes, on-board systems, cockpits and handling systems. This benefits pilots, crews and maintenance staff, while giving airlines lower training and maintenance costs as well as that all important flexibility. For example, pilots who hold a type rating on one Airbus aircraft type require minimal training to become qualified on another.²⁶⁰

{Fly-by-wire technology} enabled Airbus to introduce its commonality philosophy, creating a family of aircraft with near-identical cockpit design and handling features. The A320 Family, the A330/A340 Family, the A350 Family, and the A380 Family all share this unique commonality, so pilots need much shorter training times to transfer from one aircraft to another. ... By making it so simple and inexpensive for pilots to operate several aircraft types, Airbus also promotes the concept of mixed fleet flying, which gives airlines much greater flexibility in quickly adapting their fleet, cockpit and cabin crews, maintenance crews and schedules in response to changing demand.²⁶¹

191. Indeed, EADS attributes the fact that “Airbus has continually increased its market share,” in significant part, to the commonality that it offers its customers:

This is because every Airbus aircraft belongs to a single family, sharing the same cockpit, flight deck and spare parts, thus saving time and money for operators in terms of pilot training and maintenance as well as in other areas.²⁶²

192. And, although the EC has sought to diminish the importance of commonality to Airbus’s current sales strategy, the Airbus web site does not appear to have gotten the message, explaining in detail:

The Airbus aircraft families offer the highest degree of commonality amongst airframes,

²⁵⁹ U.S. FCOS, paras. 62, 64.

²⁶⁰ Airbus, *The Airbus Way*, at 4 (Jan. 2006) (Exhibit US-499).

²⁶¹ Airbus, *The Airbus Way*, at 9 (Jan. 2006) (Exhibit US-499).

²⁶² EADS Annual Report 2000 at 22 (Exhibit US-389).

on-board systems, cockpits, handling qualities and training of any commercial jetliner product line. The benefits of this unique approach include unmatched flexibility for flight crews, highly efficient operations and reduced costs, as pilots, cabin crews and maintenance engineers do not need extensive amounts of training to transfer from one aircraft type to another.

Airbus established the concept of commonality with its first two aircraft – the A300 and A310, which benefit from having the same flight decks, engines and other major components. Both have a common type rating for flight crews, allowing pilots to fly either family member with a single qualification. This common design philosophy was broadened with Airbus' development of its fly-by-wire family, which today includes 10 models that range in size from the 107-seat A318 to the world's largest passenger aircraft – the 555-seat A380. All feature very similar on-board systems, operating procedures and handling characteristics.

All members of the Airbus single-aisle A320 Family (comprised of the A318, A319, A320 and A321) share the same pilot type rating, enabling crews to fly any of them with a single licence endorsement. The larger A330 and A340 widebodies share the same basic handling qualities and common cockpit layout as the other Airbus fly-by-wire aircraft, so a pilot qualified on any of the A320 Family aircraft can easily transition to the A330/A340, and vice versa.

Conversion from one new-generation type to another involves a short differences training course, undertaken as part of the Cross Crew Qualification (CCQ) concept developed by Airbus. For example, pilots transitioning from the A320 Family to the A330 or A340 aircraft need only eight working days for their CCQ instead of 25 working days for a full type rating training course. Pilots transitioning from the A330 to the A340 require only three days, and it takes only one day to move from the A340 to the A330.²⁶³

193. As the United States has shown, Airbus cites the benefits of commonality in its marketing materials in order to induce airlines to purchase Airbus aircraft and, once they have purchased Airbus aircraft of one type, to induce them to purchase other Airbus aircraft in order to take advantage of commonality benefits.²⁶⁴ In addition, Airbus has also pointed to the need to maintain commonality as a reason to launch particular LCA models:

Many A310 and A300-600 operators are expressing the need for more range capability and, where they also operate A320s, A330s, or A340s, more commonality with the newer members of the Airbus family. . . .

Failure to launch these derivatives would mean that Boeing would pick up the airline

²⁶³ Airbus web site, "Commonality," <http://www.airbus.com/en/aircraftfamilies/commonality.html> (visited Aug. 31, 2007) (Exhibit US-658).

²⁶⁴ See Airbus, "Excellence Runs in the Family" (Exhibit US-390).

demand and increase its market share. This would happen not only in the narrow segment discussed here, but, via commonality and CCQ issues, would also extend to other market segments.²⁶⁵

194. Next, in paragraph 636 of the U.S. submission, the United States explained that there have been numerous instances in which Airbus (and Boeing) have sold aircraft of different models in a single “bundled” sale and that there are even more numerous examples in which previous purchases of one Airbus LCA model were an important factor in a customer’s decision to purchase other Airbus LCA models. The United States has already set forth many of those examples,²⁶⁶ and will not repeat them here. However, the United States would also note that in one of the largest LCA orders to date in 2007, Airbus made its successful offer to U.S. Airways conditional on the purchase of both A320s and A350s.²⁶⁷

167. Assume the Panel were to conclude that it is not appropriate to consider the effects of subsidies other than LA / MSF on an aggregated basis together with the effects of LA /MSF. Could the United States indicate what adverse effects it has identified as being caused by measures other than LA / MSF?

Response:

195. As explained in the response to Question 162, the effects of subsidies other than Launch Aid are similar to those of Launch Aid. Therefore, the adverse effects caused by measures other than Launch Aid are similar to those caused by Launch Aid – displacement and impedance of imports of U.S. LCA into the EC and of exports of U.S. LCA into third markets, significant lost sales, significant price undercutting, significant price suppression and depression, and material injury. At the same time, and for that reason, it is difficult to disaggregate the effects of other subsidies from the effects of Launch Aid.

196. With respect to the effect of subsidies on the launch decisions of Airbus, the United States has shown that “but for” Launch Aid, Airbus would not have launched any of the major LCA models that it did. The evidence indicates that, in at least some instances, the impact of other subsidies had an independent “but for” effect – that some launches would not have occurred even with Launch Aid, if additional subsidies had not been provided as well. In other words, even though Launch Aid was a *necessary* condition for Airbus to have pursued the business strategy that it did (to the detriment of the U.S. industry), it was not always a *sufficient*

²⁶⁵ Exhibit EC-776, paras. 4.1, 4.6 (HSBI). Note that the quoted paragraphs of this document have not been designated as HSBI or BCI by the EC.

²⁶⁶ U.S. Responses to First Panel Questions, paras. 422-428.

²⁶⁷ U.S. SOS, para. 151 (citing Exhibits US-641, US-642).

condition, in that other subsidies frequently made their own independent, necessary contributions to major elements of that strategy.

197. This can be seen, for example, with respect to the infrastructure subsidies for the A380. The 751 million Euro cost of the Hamburg site alone – [].²⁶⁸ For Airbus to locate at least some of the A380 assembly site in Germany without infrastructure subsidies, it would have had to incur these land development costs itself, as on its own admission no other site in Germany was suitable.²⁶⁹ Yet, [].²⁷⁰ Thus, just as Launch Aid was a necessary precondition for the launch of the A380, the infrastructure subsidies were also a necessary precondition for the launch of the A380.

198. Likewise, EIB loans contributed importantly to the funding available to Airbus at the time of LCA model launches. For example, in 2002 the EIB agreed to provide a loan of 700 million Euro to support the launch of the A380.²⁷¹ With respect to certain research and development subsidies, the United States would refer the Panel to the discussion in Section X of the HSBI Annex to the U.S. first written submission.

199. Finally, the evidence discussed with reference to debt forgiveness and equity infusions in response to Question 162 also demonstrates that, “but for” these subsidies, Airbus could not have developed its product line and maintained its pricing policies without doing significant, long-term harm to its balance sheet. The debt forgiveness and equity infusions received by the Airbus companies in the 1990s therefore were essential for Airbus to assimilate the launches of the 1980s, prepare for the launches of the 2000s, and still have the financial ability to pursue its market share gains in the early 2000s.

G. EXTINCTION AND EXTRACTION OF ALLEGED SUBSIDIES

168. Please comment on the view expressed by the EC at paragraphs 93 and 94 of its SWS that the fact that the Appellate Body’s previous statements regarding the extraction of subsidies were made in the context of one particular set of facts does not mean, as a matter of law, that its conclusions cannot also extend to other sets of facts. In particular, how does the United States respond to the EC’s assertion that the legal principles pronounced by panels and the Appellate Body in previous disputes are “extendable” to the

²⁶⁸ E.g., EC FWS, para. 1624.

²⁶⁹ EC SWS, para. 1084.

²⁷⁰ See U.S. SCOS, paras. 51-53 and sources cited therein.

²⁷¹ See U.S. FWS, paras. 395-406.

transactions summarized in the table at paragraph 311 of the EC’s response to Panel Question 110?

Response:

200. As an initial matter, the United States disagrees with the proposition that panels and the Appellate Body pronounce legal principles, to the extent that this proposition is understood to refer to something different from the rights and obligations contained in covered agreements. Panels and the Appellate Body clarify these rights and obligations, but the findings of panels and the Appellate Body do not themselves serve as the source of legal rights and obligations.²⁷²

201. As a general matter, the clarification of covered agreement provisions by a panel or the Appellate Body in the context of one dispute may be relevant to the consideration of a subsequent dispute to the extent that the reasoning underlying the clarification is persuasive and aids in the interpretation of covered agreement provisions in the subsequent dispute.²⁷³ However, what the EC is arguing for when it asserts that certain “legal principles” are “extendable”²⁷⁴ is not the application of reasoning derived from prior panel and Appellate Body reports to a new factual context but, rather, a substantial departure from that reasoning.

202. The problem with the EC’s “extinction” theory²⁷⁵ is not that “the facts and results of the transactions described by the European Communities do not precisely match those at issue in previous disputes.”²⁷⁶ (This mischaracterization by the EC of the U.S. critique of its theory is yet another example of the EC responding to an argument the United States has not made.²⁷⁷) Rather, the problem with the EC’s theory is that the EC misunderstands the reasoning underlying panel and Appellate Body findings in previous disputes.

203. In particular, the EC misunderstands the findings of the panel and Appellate Body in

²⁷² See *Understanding on Rules and Procedures Governing the Settlement of Disputes*, Art. 3.2.

²⁷³ See *Japan - Alcohol (AB)*, p. 14.

²⁷⁴ EC SWS, para. 93.

²⁷⁵ While the Panel’s question refers to “extraction of subsidies,” the EC’s argument at paragraphs 93 and 94 of its second written submission (and, indeed, throughout this section of its submission) pertains only to the EC’s “extinction” theory. As the United States noted in its opening statement at the second Panel meeting, nowhere in its second written submission does the EC even attempt to defend its “extraction” theory. See U.S. SNCOS, para. 134.

²⁷⁶ EC SWS, para. 93.

²⁷⁷ For other examples, see, e.g., U.S. SWS, paras. 211-214, 243-244, 592-598; U.S. SNCOS, paras. 20-22, 173-186; U.S. Comments on EC SNCOS, paras. 13, 19-23.

their *US - Countervailing Measures* reports. In its report, the panel found (in a dispute involving claims under Part V of the SCM Agreement) that a subsidy may be extinguished as a result of a sale of the subsidized entity characterized by four factors: (i) the sale is at arm's length; (ii) it is for fair-market-value; (iii) it involves all or substantially all of the subsidized entity; and (iv) it results in a relinquishment of any controlling interest the seller had in the entity.²⁷⁸ The Appellate Body agreed (although it found that the panel had erred in a different respect).²⁷⁹ The EC's request that the present Panel "extend" this finding to the facts of this dispute is really a request that the Panel reject that finding in favor of a substantially different finding, whereby a transaction extinguishes a subsidy when the transaction is characterized by the first two factors but not the second two.

204. None of the transactions that the EC alleges to have resulted in subsidy "extinction" involved all or substantially all of the company or relinquishment of a controlling interest by the seller.²⁸⁰ The EC does not contend that they did.²⁸¹ To the contrary, it asserts that even a transaction involving a stake as small as 0.93 percent of the shares in Airbus's corporate parent, EADS, resulted in a proportionate extinguishment of subsidy.²⁸² Accordingly, reaching the result the EC seeks would entail not an application to different facts of the reasoning of the panel and Appellate Body in *US - Countervailing Measures*, but a rejection of that reasoning in favor of very different reasoning.

205. Prior instances of applying similar reasoning from one dispute settlement context to another have not entailed the wholesale revision of that reasoning that the EC advocates. For

²⁷⁸ See *US - Countervailing Measures (Panel)*, paras. 7.60 - 7.72.

²⁷⁹ See *US - Countervailing Measures (AB)*, paras. 85, 117-118, 127; see also U.S. Responses to First Panel Questions, paras. 321-343; U.S. SNCOS, paras. 133-136.

²⁸⁰ As the United States previously noted, certain of the transactions on which the EC relies occurred after panel establishment and, therefore, are not relevant to this dispute. See U.S. SWS, paras. 529-530; U.S. Comments on EC SNCOS, para. 9.

²⁸¹ See U.S. SWS, para. 528 (noting that when asked how it responds to 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").

²⁸² In its first written submission, the EC identified two separate January 2001 sales of shares in EADS as allegedly extinguishing subsidy benefits: sale of a 2.07 percent stake by Lagardère, and sale of a 0.93 stake by the French government. See EC FWS, paras. 262, 282. Evidently embarrassed by the suggestion that sale of a less-than-one-percent stake in Airbus's parent company could extinguish subsidy benefits, the EC revised its characterization of these separate transactions in its response to the Panel's Question 111. It now groups the two separate transactions as a single "event," which it describes as "Lagardère and French State sell Direct shareholdings in EADS on the public market," with the alleged result of extinguishing 3 percent (*i.e.*, 2.07 percent plus 0.93 percent) of subsidy benefits. EC Responses to First Panel Questions, para. 311.

example, in *US - Hot-Rolled Steel*, the Appellate Body considered Article 3.5 of the *Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994* (“the Antidumping Agreement”) and, in particular, the requirement that injuries caused by known factors other than dumped imports not be attributed to the dumped imports. In discussing the interpretation of this non-attribution requirement, the Appellate Body relied on clarifications set out in earlier reports in disputes concerning Article 4.2(b) of the *Agreement on Safeguards*, which contains a similar non-attribution requirement.²⁸³ A key clarification in those reports was that a non-attribution analysis requires that injurious effects caused by different causal factors be separated and distinguished.²⁸⁴ In reaching its conclusion in *US - Hot-Rolled Steel*, the Appellate Body extended that “separate and distinguish” clarification from the safeguards context to the antidumping context, but it did not modify the clarification.

206. Similarly, in its report in *US - FSC*, the Appellate Body extended clarifications made in the context of construing the SCM Agreement to the context of a dispute under the *Agreement on Agriculture*. In particular, the Appellate Body considered the meaning of the term “subsidies contingent upon export performance” in Article 1(e) of the *Agreement on Agriculture* and found it “appropriate to apply the interpretation of export contingency that we have adopted under the SCM Agreement.”²⁸⁵ Once again, the Appellate Body did this without revising the previous clarification.

207. Contrary to the approach taken in these other disputes, the EC is not seeking the application of clarifications made in one context to a different context. Although it refers to the reasoning of previous panel and Appellate Body reports, it actually is seeking a significant departure from that reasoning. As already noted, a straightforward application of that reasoning to the transactions summarized in paragraph 311 of the EC’s response to the Panel’s Question 111 would lead to the conclusion that none of those transactions extinguish any of the subsidies previously provided to Airbus.

208. The way in which the earlier findings on extinction developed bears emphasis. As discussed in the U.S. response to the Panel’s Question 56, the issue of what types of transactions may extinguish the benefits conferred by subsidies was carefully considered in both the *US - Lead Bars* dispute and the *US - Countervailing Measures* dispute (including the compliance phase of that dispute).²⁸⁶ In both disputes, it was considered essential not only that the

²⁸³ See *US - Hot-Rolled Steel (AB)*, paras. 229-232.

²⁸⁴ *US - Hot Rolled (AB)*, paras. 231-232 (quoting Appellate Body reports in *US - Wheat Gluten* and *US - Lamb Meat*).

²⁸⁵ *US - FSC (AB)*, para. 141 and footnote 155.

²⁸⁶ See U.S. Responses to First Panel Questions, paras. 324-343.

transactions alleged to have extinguished subsidy benefits occurred at arm's length and for fair market value, but that they involved all or substantially all of the subsidized entity and resulted in the relinquishment of any controlling interest by the seller.²⁸⁷

209. In *US - Countervailing Measures*, the panel emphasized the “very particular and complex change in ownership” entailed in a privatization.²⁸⁸ It noted that in the countervailing duty cases before it, “the governments had severed their control over the state-owned producers upon privatization,” and that “{t}he privatized producers could no longer rely on government financing for their operations and could no longer receive things for free.”²⁸⁹

210. The panel recalled that – as in the present dispute – “{t}he European Communities initially argued that any change in ownership would necessitate a reevaluation of the benefit.” Also as in the present dispute, the United States pointed out the problem this would present in considering subsidies to publicly traded companies. “The European Communities responded 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.”²⁹⁰

211. In other words, the EC actively participated in giving the clarifications regarding subsidy extinction their shape. It was the EC that argued (successfully) that for a transaction to extinguish previously provided subsidies, “the change in ownership must be of a sufficient magnitude so as to change the control of the enterprise.”²⁹¹

212. Following adoption of the reports in *US - Countervailing Measures*, the U.S. Department of Commerce revised its methodology for determining whether privatization of an entity extinguishes pre-privatization subsidies to the entity. Under the revised methodology, the benefit conferred by a subsidy may be found to be extinguished pursuant to “a privatization . . . in which the government sold its ownership of all or substantially all of a company or its assets, retaining no control of the company or its assets, and . . . the sale was an arm's-length transaction

²⁸⁷ See U.S. Responses to First Panel Questions, paras. 325-327 (discussing panel and Appellate Body reports in *US - Lead Bars*); *id.*, paras. 329-335 (discussing panel and Appellate Body reports in *US - Countervailing Measures*); *id.*, paras. 336-339 (discussing panel report in *US - Countervailing Measures (21.5)*).

²⁸⁸ *US - Countervailing Measures (Panel)*, para. 7.60.

²⁸⁹ *US - Countervailing Measures (Panel)*, para. 7.65.

²⁹⁰ *US - Countervailing Measures (Panel)*, para. 7.62 (emphasis added).

²⁹¹ *US - Countervailing Measures (Panel)*, para 7.62 (emphasis added); *see also US - Countervailing Measures (AB)*, paras. 85, 117, 118 and footnote 177.

for fair market value.”²⁹² While the EC challenged application of this new methodology in particular cases, it expressly refrained from challenging the methodology itself.²⁹³ It was content to leave in place an approach to analyzing extinction of subsidies through privatization consistent with the very reasoning that the EC itself had helped to craft through its arguments in the underlying dispute.

213. In the present dispute, however, the EC seeks to abandon that reasoning. In particular, it asks the Panel to dispense with the premise that “the change in ownership must be of a sufficient magnitude so as to change the control of the enterprise.” It now takes the view that a transaction representing as little as 0.93 percent of Airbus’s parent company is sufficient to extinguish subsidy.²⁹⁴ As in the *US - Countervailing Measures* dispute, the United States confronted the EC with the logical implications of its position for subsidies to publicly traded companies. If the EC’s view were correct – which it is not – subsidies to such companies would be subject to constant extinguishment, as their ownership and market value change every day.²⁹⁵

214. The EC’s response to this point is quite telling. After avoiding the issue in each of its prior submissions and statements, the EC finally asserted, in its closing statement at the second Panel meeting, that this “is not a question the Panel must resolve, because we do not contend that daily trading activity involving EADS’ shares extinguishes prior subsidies.”²⁹⁶ That cursory approach to the issue misses the point entirely. It is irrelevant that the EC is not alleging subsidy extinction as a result of daily trading in EADS shares. The point is that under the EC’s logic, there is no meaningful basis for distinguishing the transactions it alleges to have resulted in subsidy extinction, on the one hand, from daily trading in the shares of a subsidized entity, on the other. Following the EC’s logic, a sale of a 0.93 percent share of a subsidized entity in daily trading should have the same effect as an initial sale on a public exchange of a 0.93 percent share of the entity by the original owner of that share. (The EC provides no basis to find otherwise.) The consequence of this approach would be a substantial and unsupported exception to the disciplines of the SCM Agreement for publicly traded companies. This hardly is the simple “extension” of reasoning from one context to another that the EC pretends it to be; it amounts to the invention of entirely new rights and obligations under the SCM Agreement – precisely the endeavor the EC originally pursued and then abandoned in *US - Countervailing Measures*.

²⁹² Notice of Final Modification of Agency Practice Under Section 123 of the Uruguay Round Agreements Act, 68 *Fed. Reg.* 37,125 at 37,127 (June 23, 2003) (Exhibit US-648).

²⁹³ See *US - Countervailing Measures* (21.5), para. 7.89 and footnotes 206 and 313.

²⁹⁴ See EC FWS, paras. 262, 282; EC Responses to First Panel Questions, para. 311.

²⁹⁵ See U.S. Responses to First Panel Questions, para. 335; U.S. SNCOS, para. 135; U.S. Comments on EC SNCOS, para. 6.

²⁹⁶ EC Closing Statement at Second Panel Meeting, para. 8.

215. Similarly, while the EC accuses the United States of “plac{ing} undue weight on the criteria of ‘change of control,’”²⁹⁷ it was the EC itself that emphasized this criterion in *US - Countervailing Measures*. Further, as the panel in that dispute explained:

Following privatization and consistent with commercial principles, the owners of the privatized company should be profit-maximizers, set on obtaining a market return on the entirety of their investment in the privatized company. Ultimately, therefore, the owners’ investment in the privatized company will be recouped through the privatized company providing its owners a market return on the full amount of their investment.²⁹⁸

216. Conversely, where a government seller of shares in a subsidized company retains an interest in that company that allows it to exert control, it may not be the case that the company’s owners are “profit-maximizers, set on obtaining a market return on the entirety of their investment in the privatized company.” Recent discussion by the Airbus governments about the possibility of enhancing their existing stakes in EADS underscores this point.²⁹⁹ For example, upon introduction of a bill in Spain’s Parliament that would encourage the government to increase its 5 percent stake in EADS, the party sponsoring the bill explained, “We cannot forget that around 9,000 Spanish jobs depend from the partnership and that 500 are lost in the adjustment plan Power 8 announced by the company.”³⁰⁰ Similarly, in reports of the German government seeking a golden share or other enhancement of its stake in EADS, the government has referred to the importance of “protect{ing} the strategic interest in EADS.”³⁰¹

217. In sum, transactions in which governments sold part of their interests in Airbus but retained controlling interests (and, as recent discussion in Spain and Germany illustrates, the possibility of enhancing those interests) are hardly comparable to the types of transactions the panel and Appellate Body were considering in *US - Countervailing Measures*. The panel and Appellate Body focused on the effects on pre-existing subsidies of a sale designed to result in “the privatized company providing its owners a market return on the full amount of their

²⁹⁷ EC Responses to First Panel Questions, para. 308.

²⁹⁸ *US - Countervailing Measures (Panel)*, para. 7.60.

²⁹⁹ Regarding the control of EADS today through the pooling of “indirect” shares by the company’s founders, see U.S. SWS, paras. 533-535.

³⁰⁰ *The Partido Popular {PP} asks the Spanish Government to increase its EADS stake to 12%*, Gaceta de los Negocios (Aug. 10, 2007) (Exhibit US-649).

³⁰¹ Andrea Thomas, *German Govt: No Decision Yet On Taking Golden Share In EADS*, Dow Jones (Aug. 6, 2007) (Exhibit US-650) (quoting Deputy Government Spokesman Thomas Steg); *German Government Wants to Buy “Golden Share” in EADS*, Der Spiegel Online International (Aug. 6, 2007) (Exhibit US-651).

investment.”³⁰² By contrast, the transactions that the EC now cites to support its extinction theory leave the Airbus governments in a position to pursue employment and other “strategic” objectives through their retained interest in Airbus.

218. Finally, a further aspect of what the EC refers to as the “extension” of previously articulated “legal principles” is that it would entail the application to a dispute under Parts II and III of the SCM Agreement of clarifications developed in the context of countervailing duty disputes under Part V of the SCM Agreement. As discussed in response to the Panel’s Question 56, the task before a panel under Parts II and III is very different from the task under Part V. A key question under Part V is whether an investigating authority has properly determined the amount of subsidy to be offset through countervailing duties. By contrast, the key inquiries under Parts II and III (export contingency in the case of the former and causing of adverse effects in the case of the latter) do not require a quantification of the amount of subsidy. Therefore, it is not necessarily the case that reasoning pertaining to the quantification of subsidies in the countervailing duty context is applicable in these other contexts.³⁰³

219. The EC’s single sentence response to this point is that “{t}he rationale for these cases {i.e., the panel and Appellate Body reports discussed in the U.S. response to the Panel’s Question 56} lies in the definition of what is a subsidy and the definition of subsidy in the *SCM Agreement* is common to the whole agreement.”³⁰⁴ However, the EC ignores the extensive discussion by the panels and the Appellate Body in those disputes explaining that their findings rested on their understanding of provisions in Part V of the SCM Agreement.³⁰⁵ The EC also fails to address the fact that unlike Part V of the SCM Agreement, Parts II and III do not require a precise quantification of subsidies, and that this difference may make the analysis of subsidy extinction under Part V inapplicable to an analysis under Parts II and III.

220. In conclusion, while there may be instances in which the reasoning underlying findings in one dispute is helpful to clarifying the rights and obligations at issue in a different dispute, that is not what the EC is asking the Panel to do. Rather, with no justification at all, the EC is asking the Panel to abandon clarifications made by prior panels and the Appellate Body in favor of a completely different clarification of SCM Agreement provisions. For the reasons discussed above and in previous U.S. submissions and statements, the Panel should reject that request.

³⁰² *US - Countervailing Measures (Panel)*, para. 7.60.

³⁰³ *See* U.S. Response to First Panel Questions, paras. 340-343.

³⁰⁴ EC SWS, para. 94.

³⁰⁵ *See* U.S. Responses to First Panel Questions, para. 340 and footnote 436 (citing discussions from panel and Appellate Body reports).

169. How does the United States respond to the EC’s argument, at paragraph 105 of its SWS, that where the effects of alleged subsidies involve “cash flow relief” to Airbus which allows it to lower the price of its products, it is critical for the United States to show, specifically, that Airbus SAS currently enjoys the subsidy-sourced cash flow relief to enable it to price down its products to the United States’ detriment, and that such cash flow relief was not interrupted, or exhausted, by intervening transactions conducted at arm’s length and for fair market value?

Response:

221. The EC characterization of the alleged U.S. “cash flow relief” argument in paragraph 105 of its second written submission, as elsewhere in its submissions, completely fails to reflect what the United States has in fact demonstrated with respect to the causal link between Launch Aid and the adverse effects in this dispute. When the U.S. showing is correctly presented, the EC’s arguments about the alleged extinction and extraction of subsidies – in addition to their other flaws – are seen to be completely irrelevant to the U.S. causation argument.

222. As the United States has explained, Launch Aid (both alone and together with other subsidies) distorts LCA markets by permitting the launch of aircraft models that could not otherwise have been launched *and* by enabling “Airbus to simultaneously invest in multiple LCA launches more quickly than it otherwise could *and* use its limited funds to reduce prices for already launched LCA models.”³⁰⁶ Thus, at any given moment, the impact of Launch Aid (and other subsidies) includes both (1) the existence of aircraft models that would not have been launched in the past without subsidies and (2) the present impact of subsidies that are *currently being provided* for the development of new Airbus LCA models on the financial constraints *currently* experienced by Airbus *as a whole*.

223. For example, consider the years 2001 and 2002. In these two years, Airbus not only enjoyed below-market repayment obligations on past Launch Aid, but also received further disbursements of more than [] million Euro in new Launch Aid for the A340-500/600 and more than [] million Euro plus [] million pounds in new Launch Aid for the A380.³⁰⁷ The Airbus governments required no repayment of these sums during this period – and indeed have not yet required any repayment of the A380 Launch Aid to this date. Although these sums represent less than half of the total Launch Aid disbursements for each of the two projects, both projects were clearly consuming significant financial resources of Airbus during these particular years. Further, according to Deutsche Bank, the free cash flow of EADS during this period (including

³⁰⁶ U.S. SNCOS, para. 173 (quoting U.S. Answers to First Panel Questions, para. 264)).

³⁰⁷ Exhibit EC-13 (BCI).

net cash flow from Launch Aid) was 867 million Euro in 2001 and 578 million Euro in 2002.³⁰⁸ Based on Deutsche Bank’s calculations, the free cash flow of EADS in 2001 and 2002 would have been negative but for the increase in net Launch Aid (outstanding balance minus repayments) in both of these years.³⁰⁹ Thus, the provision of [] Euro in long-term loans on below-market, backloaded, and success-dependent terms had a significant impact on the financial constraints facing Airbus in 2001 and 2002.

224. It is, of course, precisely in this period that Airbus began to significantly increase its LCA market share by winning sales from Boeing through greater pricing flexibility.³¹⁰ What the EC calls the U.S. “cash flow argument” is, in fact, a demonstration that the serious prejudice in the form of market share shifts, price suppression and depression, price undercutting, and lost sales that accelerated after 2001 and continued through 2005 and beyond is the “effect of the subsidy,” in part, because the subsidies provided to Airbus *during that period* had a significant effect on the financial flexibility of Airbus and on its ability to use price concessions to gain and hold market share.

225. It should be evident, therefore, that the particular U.S. argument at issue focuses on a causal link between the provision of subsidies and the *roughly contemporaneous* experience of serious prejudice. Although the subsidies in this dispute have also caused long-term distortions in the LCA market by permitting the launch of long-term aircraft programs that would not have occurred but for the subsidies, the United States has shown that there are shorter-term effects as well. For example, the evidence cited above refers only to the period after the formation of EADS. The EC’s arguments about the alleged extinction and extraction of subsidies during the period – their intrinsic lack of merit aside – do not apply even on their own terms to the effects that the United States has here described.

II. QUESTIONS TO THE EUROPEAN COMMUNITIES

210. Referring to paragraphs 433-434 of the EC’s SNCOS, it appears that the EC is arguing that the fact that Boeing made subsequent sales of LCA eliminated any adverse effect resulting from a prior lost sale. Is the Panel correct in its understanding of the point being made? Could the EC explain the basis for the view that mitigation of adverse effects caused by a subsidy precludes a finding that the prior lost sale was “significant”? Does such a view in the context of the aircraft sales discussed in the EC SNCOS not rest on a presumption of an absolute limit on production capacity?

³⁰⁸ Exhibit US-459 at 7.

³⁰⁹ Exhibit US-459 at 7.

³¹⁰ See U.S. Comments on EC SNCOS, paras. 44-46 (citing statements of Mr. Scherer of Airbus).

Response:

226. With respect to this question of the Panel to the EC, the United States would like to confirm its oral response at the second Panel meeting that Boeing is experiencing no “absolute limit on production capacity.”

227. In support of its contention that Boeing is “sold out” on several major LCA models through 2011 or beyond, the EC references statements by Boeing executives during an investor conference call in April 2007.³¹¹ The EC neglects to mention, however, that in the very same investor call, Boeing CEO Jim McNerney explained:

Q. Could you guys explain a little bit what you mean by sold out? Does that mean you’re not taking any more orders until, let’s say 2013 for the {787} and – what was the other year for the 737?

A. Yeah, I think when people, when some of the questioners use the word sold out, it really reflects extending lead times or getting farther out than average. And on most of our products now, they are – we’ve just come off two of the highest order years in our history, two of the highest order years in the industry’s history for that matter, and that leaves us extended farther out with deliveries than we averagely are. And so we’re not sold out. We just have positions that are a little further out than are available, and we’re aggressively selling them, we’re aggressively competing to fill those elements of our skyline. And there are people buying them.³¹²

228. At the Boeing Investor Conference one month later, Boeing Commercial Airplanes CEO Scott Carson further explained that Boeing’s current projected delivery schedule includes not only orders that have been actually placed, but also anticipated future orders:

In our skyline, when we say we’re sold out, we’ve also looked at the big carriers that are not in the market, and we have reserved slots in anticipation that they’ll be in. So we have some capacity to deal with the legacy carriers as they come back.³¹³

³¹¹ EC SNCOS, para. 301 (citing Boeing Company Earnings Conference Call, Apr. 24, 2007, at 11 (Exhibit EC-793)).

³¹² Boeing Company Earnings Conference Call, Apr. 24, 2007, at 13-14 (Exhibit EC-793) (emphasis added).

³¹³ Boeing Company Annual Investors Conference, May 23, 2007, available at <http://phx.corporate-ir.net/phoenix.zhtml?c=85482&p=irol-eventDetails&EventId=1548829>, relevant portion transcribed as Exhibit US-659.

229. Thus, if “sold out” means that Boeing has no more production slots available for sale, then Boeing is not “sold out.”

230. Further, the notion of an “absolute limit” on production capacity in the LCA industry is belied by the actual increases in production levels at both Boeing and Airbus as market demand has increased in recent years. For example, Airbus recently announced that it would increase production rates for the A320 from 32 to 40 aircraft per month and is considering further increases in A330/A340 production, already scheduled to increase from 7 to 9 aircraft per month.³¹⁴ And, when Boeing considers whether to increase its own production rates, it must take into account whether “Airbus at 40 {A320s per month} is going to put too much capacity into the market.”³¹⁵

231. The evidence therefore establishes that Boeing is not currently constrained by any lack of production capacity. Boeing is not prevented from increasing production levels if it considers that the market could sustain such an increase at profitable levels. And what the market can sustain is, at least in part, a function of the production and pricing levels set by Airbus.

III. QUESTIONS TO BOTH PARTIES

A. LA / MSF

215. In their general characterizations of the challenged measures, the Parties have advanced two different positions - the United States describes the LA / MSF loans as *hybrid* financing instruments; whereas, to the EC, they are *project-specific debt* financing instruments. To what extent do the Parties believe that either of their characterizations is dispositive of the question of which of the benchmarks identified in the Ellis or Whitelaw Reports is appropriate in this dispute?

Response:

232. In determining the appropriate market benchmark to use for a benefit analysis of Launch Aid, it is the characteristics of Launch Aid that are dispositive, not the label used to describe those characteristics. In particular, the Panel should consider the risks associated with Launch Aid, which are the same regardless of the label applied to Launch Aid. In light of those risks, the

³¹⁴ Airbus press release, *Airbus boosts production rate for its single aisle aircraft to record levels* (May 16, 2007) (Exhibit US-660).

³¹⁵ Statement by Boeing Commercial Airplanes CEO Scott Carson, in Boeing Company Annual Investors Conference, May 23, 2007, available at <http://phx.corporate-ir.net/phoenix.zhtml?c=85482&p=irol-eventDetails&EventId=1548829>, relevant portion transcribed as Exhibit US-659.

appropriate benchmark is the one set out in the Ellis Report and discussed further in the NERA Response to Whitelaw Report.³¹⁶

233. Certain essential features of Launch Aid are indisputable. First, a government's entitlement to repayment of Launch Aid depends entirely on sales of the covered aircraft. Second, while Launch Aid contracts may anticipate sales occurring according to a forecast schedule, Airbus's failure to meet that notional schedule does not trigger any new entitlement on the government's part; if sales fail to occur when anticipated, the government still is entitled only to repayment on delivery. Third, the government has no recourse in the event that sales are fewer than anticipated and less than all of the Launch Aid is repaid. Finally, Launch Aid contracts are structured so that no repayment or relatively low repayment is due on earlier deliveries, while higher repayments are due on later deliveries; thus, if total deliveries are fewer than forecast, it is the higher repayments that will not be made.³¹⁷

234. Given the foregoing risk profile, it is appropriate to characterize Launch Aid as a hybrid instrument, containing both debt-like and equity-like features. However, even if the Panel were to disagree and find that Launch Aid is more appropriately characterized as a project-specific debt instrument, it remains a project-specific debt instrument with the aforementioned traits contributing to its riskiness. The key question for the Panel is what premium a market provider of capital would demand for assuming the level of risk associated with Launch Aid.³¹⁸ The answer is not limited by the characterization of Launch Aid as a hybrid instrument or a project-specific debt instrument. As previously noted (in demonstrating the fallacy in the EC's "equity ceiling" hypothesis, for example), the risk associated with a single project of a given company may be greater than the average risk associated with all projects of the same company. In that case, the cost of debt financing for the single project may well be greater than the cost of equity for the company as a whole.³¹⁹

235. The United States maintains that the appropriate risk premium (and, hence, the appropriate market benchmark) is the one identified in the Ellis Report and further discussed in

³¹⁶ See NERA, *Economic Assessment of the Benefits of Launch Aid*, pp. 19-22 (Nov. 20, 2006) ("Ellis Report") (Exhibit US-80) (BCI); NERA Response to Whitelaw Report, pp. 2-6 (Exhibit US-534) (HSBI); see also U.S. FWS, paras. 112-147; U.S. SWS, paras. 82-112; U.S. SNCOS, paras. 54-60; U.S. SCOS, paras. 13-44; U.S. Comments on EC SNCOS, paras. 27-32.

³¹⁷ See, e.g., U.S. FWS, paras. 116-136; U.S. FNCOS, paras. 46-49; U.S. SWS, paras. 82-88; U.S. SNCOS, paras. 54-60; Ellis Report, pp. 2-5, 19-22 (Exhibit US-80) (BCI); NERA Response to Whitelaw Report, pp. 2-6 (Exhibit US-534) (HSBI).

³¹⁸ See U.S. SNCOS, para. 54.

³¹⁹ See U.S. SWS, para. 110; NERA Response to Whitelaw Report, pp. 6-12, 19-21 (Exhibit US-534) (HSBI).

the NERA Response to Whitelaw Report. That premium is based on research on financing for projects with risk profiles comparable to Launch Aid. To be conservative, Ellis used the lowest premium indicated by this research and then added it to the sum of a risk-free interest rate and Airbus's cost of debt (as opposed to its cost of equity or its weighted average cost of capital, either of which would have yielded a higher benchmark).³²⁰

236. By contrast, the Whitelaw Reports develop a benchmark based on a premium that grossly understates the risks associated with Launch Aid.³²¹ The risk premium identified by Whitelaw is based on contracts between Airbus and risk-sharing suppliers. The United States previously has explained in detail the factors that distinguish the relationships that such suppliers of goods and services have with Airbus from the relationships that banks and other financial institutions have with Airbus, resulting in risk-sharing suppliers demanding a relatively lower return on financing. These differences include the relative immobility of capital provided by risk-sharing suppliers and the array of other incentives influencing suppliers' relationships with Airbus, including the desire to access revenue from aftermarket sales and other sources.³²²

237. Moreover, the EC's and Whitelaw's understatement of the risk associated with Launch Aid is also highlighted by the cross-checks they use in an attempt to confirm their benchmark – notably, their reference to a 1998 financing contract between [], and a comparison to a supposed “equity ceiling.” The EC ignores numerous features in the [] contract that give it a debt-like risk profile – []

[].³²³ Likewise, Whitelaw's “equity ceiling” understates the risk associated with Launch Aid, including by focusing on the risk of diversified companies as opposed to particular, LCA-related projects.³²⁴

238. In conclusion, the key issue before the Panel in evaluating the benefit conferred by Launch Aid is not Launch's Aid's label, but its risk profile. For the reasons discussed in this response and in prior U.S. submissions and statements, the Ellis Report and NERA Response to Whitelaw Report properly account for the risk attributable to Launch Aid, while the Whitelaw Reports do not. Even under the flawed benchmark proposed in the Whitelaw Reports, however, the necessary conclusion remains that Launch Aid confers a benefit on Airbus and thus

³²⁰ See U.S. SWS, para. 89; Ellis Report, pp. 5-7 (Exhibit US-80) (BCI); NERA Response to Whitelaw Report, pp. 7-12 (Exhibit US-534) (HSBI).

³²¹ See, e.g., U.S. SNCOS, paras. 57-59; U.S. Comments on EC SNCOS, paras. 30-31.

³²² See U.S. FCOS, paras. 20-27; U.S. SWS, paras. 113-119; U.S. SNCOS, paras. 57-59; U.S. SCOS, paras. 27-44.

³²³ See U.S. FCOS, paras. 5-15; U.S. SWS, paras. 101-108; U.S. SCOS, paras. 41-43.

³²⁴ See U.S. FCOS, paras. 16-19; U.S. SWS, paras. 109-112; U.S. SCOS, para. 44.

constitutes a subsidy within the meaning of the SCM Agreement,³²⁵ as the EC acknowledged once again in response to a question posed by the Panel during the second meeting.

B. PROHIBITED EXPORT SUBSIDIES

216. The Panel understands that both parties have expressed the view that the legal standard for the determination of in fact and in law export contingent subsidies is the same, but that the type of evidence that may be relied upon to demonstrate one or other type of export contingent subsidy differs (United States, FWS, para. 327; EC, FWS, para. 606). To what extent are the Parties arguing that footnote 4 should inform the Panel’s assessment of the United States claims relating to the existence of *both* in fact, and in law, export contingent subsidies? For instance, are the Parties saying that the notion of “actual or anticipated exportation or export earnings” is of equal application to demonstrating the existence of both types of export contingent subsidies?

Response:

239. Footnote 4 of the SCM Agreement provides context for understanding the legal standard applicable to a determination of whether a subsidy is contingent (whether in law or in fact) upon export performance. This context shows that the phrase “contingent . . . upon export performance” in Article 3.1(a) should be understood to mean “tied to actual or anticipated exportation or export earnings.”

240. Footnote 4 is attached to the phrase “in fact” in Article 3.1(a), and it addresses the evidentiary question of how contingency in fact is demonstrated. In addressing this evidentiary question, footnote 4 restates the legal standard of contingency upon export performance. Thus, the first sentence of footnote 4 reads: “This standard is met when the facts demonstrate that the granting of a subsidy, without having been made legally contingent upon export performance, is in fact tied to actual or anticipated exportation or export earnings.”

241. This sentence is constructed in a way that equates the concepts “contingent upon” and “tied to,” as well as the concepts “export performance” and “actual or anticipated exportation or export earnings.” As a result, the only thing that distinguishes *de facto* export contingency from *de jure* export contingency is how contingency is demonstrated as an evidentiary matter.

242. The Appellate Body confirmed this point in *Canada - Autos*. At issue there (as discussed in response to Question 146, above) were claims of *de jure* export contingency. The Appellate Body explained:

³²⁵ See, e.g., U.S. SWS, paras. 72-78.

As the legal standard is the same for *de facto* and *de jure* export contingency, we believe that a ‘tie’, amounting to the relationship of contingency, between the granting of the subsidy and actual or anticipated exportation meets the legal standard of ‘contingent’ in Article 3.1(a) of the *SCM Agreement*.³²⁶

243. Accordingly, the concept of “actual or anticipated exportation or export earnings” is equally applicable to *de jure* and *de facto* contingency upon export performance.

217. To what extent do the Parties consider that the motivations or reasons for granting a subsidy are relevant to the inquiry into whether a subsidy is in fact contingent upon export performance?

Response:

244. Evidence that the authority granting a subsidy is doing so for export-related motivations or reasons is likely to be relevant to a finding of contingency in fact upon export performance. Such evidence would tend to establish the tie between provision of the subsidy and actual or anticipated exportation or export earnings contemplated by footnote 4 of the *SCM Agreement*. Conversely, evidence that the granting authority may have had additional or other motivations for providing the subsidy would not necessarily undermine the establishment of a tie to actual or anticipated exportation or export earnings demonstrated through other evidence and, even if the EC’s allegations to this effect were substantiated, does not do so in this dispute.

245. In analyzing whether the provision of a subsidy is in fact contingent upon export performance, “the relationship of contingency, between the subsidy and export performance, must be *inferred* from the total configuration of the facts constituting and surrounding the granting of the subsidy, none of which on its own is likely to be decisive in any given case.”³²⁷ As Australia explained in its third party oral statement, “the total configuration of the facts” may include “official statements by governments indicating the intention behind the granting of the subsidies.”³²⁸ The United States agrees with that analysis.

246. In suggesting that the United States takes a contrary view, the EC mischaracterizes U.S. arguments.³²⁹ As previously discussed, the EC takes statements from the U.S. second written

³²⁶ *Canada - Autos (AB)*, para. 107 (internal citation to *Canada - Aircraft (AB)* omitted).

³²⁷ *Canada - Aircraft (AB)*, para. 167 (italicized emphasis in original; underscored emphasis added); *see also* Australia Third Party Oral Statement, para. 9.

³²⁸ Australia Third Party Oral Statement, para. 10.

³²⁹ *See* EC SNCOS, paras. 130-131 (as-delivered version).

submission entirely out of context.³³⁰ The discussion in the U.S. second written submission of a government’s motivations for providing a subsidy was a response to the EC’s so-called “countervailing explanations” argument.³³¹

247. The United States previously had shown that Airbus’s contractual commitment to repay Launch Aid on a per sale basis over a level of sales that Airbus can attain only by exporting amounts to a commitment to engage in export performance. As this commitment is made in exchange for the governments’ commitment to provide Launch Aid, the provision of Launch Aid is tied (through contract) to actual or anticipated exportation or export earnings within the meaning of footnote 4 of the SCM Agreement.³³²

248. The EC responded to this aspect of the U.S. *prima facie* case by arguing that there are “countervailing explanations” – that is, non-export-related explanations – for the design of Airbus’s obligations under the Launch Aid contracts. It cited two such explanations. First, it asserted that “{d}eliveries of the aircraft provide the most reliable indication that sufficient cash will be on hand to make repayments.”³³³ Second, it stated that “timing repayment with deliveries also serves to allocate risk between the company and the United Kingdom.”³³⁴

249. Neither of the EC’s “countervailing explanations” addressed the level of sales over which Launch Aid is to be repaid, even though this is an essential element of Airbus’s contractual obligation, demonstrating that Launch Aid is provided in exchange for an undertaking by Airbus that it can fulfill only if it exports. Instead, each “countervailing explanation” addressed only the fact that the obligation to repay Launch Aid is triggered by sales. Moreover, much like Canada in the *Canada - Aircraft* dispute,³³⁵ the EC adduced no evidence to substantiate its countervailing explanations.³³⁶

³³⁰ See U.S. Comments on EC SNCOS, para. 18.

³³¹ See U.S. SWS, paras. 230-234.

³³² See U.S. FWS, paras. 352-360, 372-375, 383-386.

³³³ EC FWS, para. 659.

³³⁴ EC FWS, para. 662. The EC laid out its “countervailing explanations” argument with respect to the A380 contract between Airbus and the UK government. See *id.*, paras. 657-666. Although it acknowledged that “{e}ach measure must be considered individually” (*id.*, para. 584), it purported to apply its argument regarding the UK A380 contract to each of the other Launch Aid contracts at issue “*mutatis mutandis*” (*id.*, para. 614).

³³⁵ See *Canada - Aircraft (Panel)*, para. 9.344

³³⁶ See EC FWS, paras. 657-666. As noted above, the EC laid out its “countervailing explanations” argument in the context of discussion of the UK A380 Launch Aid contract. During this entire, ten-paragraph discussion, the EC does not cite to a single shred of evidence to support its argument. Later, in an apparent effort to

250. Finally – and this is the point the United States made in its second written submission – even assuming (*arguendo*) the EC’s alleged “countervailing explanations” to be true, they are not relevant. The possible existence of additional, non-export-related motivations that could (according to the EC) explain the design of Airbus’s obligations under the Launch Aid contracts does not sever the tie between the provision of Launch Aid and actual or anticipated exportation or export earnings.³³⁷ Such motivations, even if the EC had substantiated them, would not alter the fact that in exchange for the governments’ provision of Launch Aid, Airbus undertakes a contractual obligation that it cannot fulfill without exporting.³³⁸

251. However, the fact that the EC’s alleged “countervailing explanations” are irrelevant does not mean that evidence of export-related motivations for the provision of Launch Aid is also irrelevant. In other words, while even properly substantiated “countervailing explanations” would not vitiate Launch Aid’s tie to actual or anticipated exportation or export earnings demonstrated by other evidence, evidence of export-related motivations or reasons for providing Launch Aid does help to establish the existence of that tie in the first place. Thus, in other disputes, panels have cited evidence of export-related motivations in analyzing whether the provision of subsidies was tied to actual or anticipated exportation or export earnings.

252. In *Canada - Aircraft*, for example, in establishing that Technology Partnership Canada (“TPC”) grants were tied to anticipated exportation or export earnings, the panel cited an Industry Minister’s Message stating that ““with investments from TPC, and with industry’s concerted efforts, this sector {i.e., the aerospace and defense sector} will be better equipped to compete effectively in the world marketplace and could grow to fourth place.””³³⁹

253. Similarly, in *Australia - Leather*, in establishing that the Australian government’s grant contract to the Howe company was export contingent, the panel took into account that Howe’s

incorporate its argument “*mutatis mutandis*” (*id.*, para. 614) in other contexts, the EC simply asserts that “there are legitimate countervailing explanations to explain why the contract contains a provision providing for repayment in case of delivery, which have nothing to do with export contingent subsidies” (*id.*, paras. 677, 681), once again offering no evidence.

³³⁷ See U.S. SWS, paras. 230-234.

³³⁸ See *Australia - Leather*, para. 9.63 (rejecting Australia’s argument that grant to the Howe company was not export contingent because it was motivated in part by “the government’s concern for job retention in the region in the absence of support for the company”).

³³⁹ *Canada - Aircraft (Panel)*, para. 9.340, fourth bullet point (quoting Industry Minister’s Message included in 1996-1997 TPC Annual Report) (emphases supplied by panel); see also *id.*, para. 9.340, seventh bullet (quoting Leader of Government in House of Commons stating that ““building of exports”” was ““just what the government had in mind””).

receipt of that grant replaced its participation in programs that “give incentives to Australian companies to export certain products.”³⁴⁰

254. In the present dispute, the United States has adduced ample evidence demonstrating that increasing exports is among the motivations of the Airbus governments for providing Launch Aid. This evidence includes, for example, the statement by former French Prime Minister Lionel Jospin – remarkably similar to the above-quoted statements by Canadian officials referred to in the *Canada - Aircraft* dispute – that the French government “will give Airbus the means to win the battle against Boeing.”³⁴¹ Other evidence that promotion of exports is part of the governments’ motivation for the provision of Launch Aid for the A380, A340-500/600, and A330-200 includes:

- The UK government’s statement, upon announcing the provision of Launch Aid for the A380, that “{w}ithin 25 years Airbus has grown to take 55% of the civil aircraft production market and contributes £1 billion to the UK’s trade balance,”³⁴²
- The British Prime Minister’s statement, upon the public unveiling of the A380, that “{t}he export gains will run into the billions of pounds.”³⁴³
- The communiqué issued by ministers of the Airbus governments at the July 2006 Farnborough air show in which they “reaffirmed their agreement to support Airbus to continue to innovate and to develop programmes in the context of international competition,”³⁴⁴

³⁴⁰ *Australia - Leather*, para. 9.65; *see also id.*, footnote 210 (panel explaining reliance on press and company reports describing government’s reasons for providing grant as “relevant to our analysis of the facts and circumstances surrounding the design and grant of that assistance”).

³⁴¹ French Prime Minister Lionel Jospin in a speech before the French Parliament, quoted in *Jospin pledges to aid Airbus in fight against Boeing*, Reuters (Mar. 8, 2000) (Exhibit US-1) (discussed in U.S. FWS, paras. 1, 92).

³⁴² Press Release, *Byers Announces £530 Million Government Investment in Airbus*, Department of Trade and Industry (Mar. 13, 2000) (Exhibit US-360) (emphasis added) .

³⁴³ *Blair Says Airbus A380 will Repay 530 Mln Stg UK Govt Investment*, AFX.com (Jan. 18, 2005) (Exhibit US-361).

³⁴⁴ Communiqué text, Airbus Ministerial meeting at Farnborough International (July 17, 2006), reprinted in UK House of Commons Hansard Written Answers (July 24, 2006) (pt. 1989, Column 1014W) (July 17, 2006) (Exhibit US-63) (emphasis added).

- The Spanish A380 Launch Aid contract’s identification of []³⁴⁵
- The acknowledgment in the preamble to the Spanish A340-500/600 Launch Aid contract that []³⁴⁶ and
- The statement by Airbus, in its application to the German government for Launch Aid for the A380, that a benefit of providing the requested Launch Aid would be an []³⁴⁷

255. Other evidence that the EC has designated as HSBI further substantiates the export-related motivations of the Airbus governments.³⁴⁸

256. In sum, while evidence of the governments’ export-related motivations is not the only evidence establishing that the provision of Launch Aid is tied to actual or anticipated exportation or export earnings, it supports that conclusion and, thus, the conclusion that Launch Aid for the A380, A340-500/600, and A330-200 is prohibited under Article 3.1(a) of the SCM Agreement.

C. EIB LOANS

218. Please describe what you consider to be the attributes of a “subsidy programme” - that is, the factors that make it possible to identify the existence of a “subsidy programme” - for the purpose of Article 2.1(c). To what extent can such attributes or factors be found in the lending activities of the EIB?

Response:

257. First, the Panel should note that Article 2.1(c) of the SCM Agreement does not require that a subsidy be granted pursuant to a subsidy program in order to be *de facto* specific.³⁴⁹

³⁴⁵ Spanish A380 Agreement, DS316-EC-BCI-0000549, at “Sexto” (Exhibit US-73) (BCI).

³⁴⁶ Spanish A340-500/600 Agreement, DS316-EC-BCI-0000534, at 1 (first paragraph under “Primero”) (Exhibit US-37) (BCI).

³⁴⁷ Anlage 1 zum A380 Darlehensvertrag, DS316-EC-BCI-0000369, p. 44 (Exhibit US-357) (BCI).

³⁴⁸ See, e.g., U.S. FWS, HSBI App., paras. 34-36, 55; U.S. SCOS, paras. 5-6.

³⁴⁹ See U.S. SNCOS, para. 128.

Subparagraph (c) of Article 2.1 presumes that a specificity analysis already has occurred under subparagraphs (a) and (b). Thus, subparagraph (c) sets out factors to be considered “{i}f, notwithstanding any appearance of non-specificity resulting from the application of the principles laid down in subparagraphs (a) and (b), there are reasons to believe that the subsidy may in fact be specific.” Neither of subparagraphs (a) or (b) refers to a subsidy program.

258. Subparagraph (c) does refer to a subsidy program, indicating that “use of a subsidy programme by a limited number of certain enterprises” or “predominant use by certain enterprises” could support a finding of specificity. But, subparagraph (c) also refers to other factors – such as “the granting of disproportionately large amounts of subsidy to certain enterprises” and “the manner in which discretion has been exercised by the granting authority in the decision to grant a subsidy” – that do not necessarily require the existence of a subsidy program.

259. As the United States discussed in response to the Panel’s Question 119, to evaluate a factor such as disproportionality, it is necessary to identify an appropriate baseline against which to measure the subsidies at issue.³⁵⁰ When those subsidies are provided under the auspices of a particular program, the program may serve as the appropriate baseline. However, the absence of a subsidy program does not preclude a finding of the granting of disproportionately large amounts of subsidy to certain enterprises. In that case, other ways in which the granting authority classifies its provision of subsidies should be examined.³⁵¹ Nor does the absence of a subsidy program preclude a finding of *de facto* specificity based on a consideration of factors other than disproportionality.

260. It is the EC that suggests that Article 2.1(c) requires an evaluation of specificity of subsidies relative to a subsidy program. It is surprising, therefore, that the EC has not even tried to establish the legal standard for identifying a subsidy program. Instead, the EC simply asserts that the subsidy program against which EIB loans to Airbus must be evaluated is all lending by the EIB over its entire 50-year history.³⁵² In fact, this approach does not comport with the ordinary meaning of the term “subsidy programme” in context and in light of the object and purpose of the SCM Agreement.

³⁵⁰ See U.S. Responses to First Panel Questions, paras. 365-370.

³⁵¹ See U.S. Responses to First Panel Questions, para. 366; *see also id.*, paras. 103-107.

³⁵² See, e.g., EC FWS, para. 1039; EC Responses to First Panel Questions, para. 367; EC SWS, paras. 434-436, 478; EC SNCOS, para. 184; *see also* EC SWS, para. 629 (asserting, in the context of argument regarding research and development grants, that “specificity within the meaning of Article 2 of the *SCM Agreement* must be assessed at the programme level”).

261. While the SCM Agreement sets forth, in Article 1, what constitutes a “subsidy,” it is silent as to what constitutes a “programme.” The ordinary meaning of “programme,” as relevant here, is: “A plan or outline of (esp. intended) activities. . . . {A} planned series of activities or events.”³⁵³ Thus, a “subsidy programme” is a plan or outline of subsidies or a planned series of subsidies. This definition suggests that to constitute a subsidy program a series of subsidies must be circumscribed in some way; it is not just any series of subsidies that constitutes a subsidy program, but a “planned series” of subsidies. (Emphasis added.)

262. The foregoing understanding is confirmed by the context of the term “subsidy programme” in Article 2 – in particular, other uses of the term “subsidy programme” in the SCM Agreement. For example, footnote 31 uses the term “subsidy programmes” in connection with defining “a general framework of regional development” within the meaning of Article 8.2(b). It states:

A ‘general framework of regional development’ means that regional subsidy programmes are part of an internally consistent and generally applicable regional development policy and that regional development subsidies are not granted in isolated geographical points having no, or virtually no, influence on the development of a region.

263. This provision suggests that the drafters of the SCM Agreement understood a subsidy program to be a concept narrower than a “framework” or “policy.” That the drafters understood that a “framework” or “policy” could encompass “subsidy programmes” as its components helps confirm the understanding of a “subsidy programme” as a series of subsidies that is circumscribed in some way, as opposed to a diverse series of subsidies that happen to be conferred by a single granting authority operating under a particular “framework” or “policy.”

264. The foregoing understanding also is confirmed by Article 8.3, which concerns the notification to the Committee on Subsidies and Countervailing Measures of subsidy programs alleged to be non-actionable. The second sentence of Article 8.3 states that “{a}ny such notification shall be sufficiently precise to enable other Members to evaluate the consistency of the programme with the conditions and criteria provided for in the relevant provisions of paragraph 2.” This provision suggests that the drafters understood a subsidy program to be something that could, in fact, be described with precision and in a way that would permit evaluation according to specified conditions and criteria. A similar understanding is reflected in Article 25.3, which concerns the information to be provided in a notification of a subsidy program. Again, these provisions indicate that for a series of subsidies to constitute a subsidy program, they must be circumscribed in a way that would enable the type of evaluation contemplated.

³⁵³ *The New Shorter Oxford English Dictionary*, vol. 2, p. 2371 (1993).

265. In light of the foregoing understanding of “subsidy program,” factors that make it possible to identify the existence of a subsidy program are factors indicating that a series of subsidies is circumscribed in a way that distinguishes it as a planned series of subsidies. Such factors could include: (i) designation by the granting authority of a series of subsidies as a program; (ii) a common set of objectives; and (iii) dedicated funding.

266. All of these factors are on display in the EIB’s i2i program. As previously discussed, the EIB itself described i2i as a “dedicated EUR 12-15 billion lending programme.”³⁵⁴ The EIB described the “programme” as “intended to target lending” towards five objectives, identified as: “development of SMEs and entrepreneurship;” “diffusion of innovation;” “research and development;” “information and communications technology networks;” and “human capital formation.”³⁵⁵ The EIB dedicated Euro 12-15 billion towards achieving the i2i objectives from the program’s launch in 2000 through the end of 2002. In early 2003, the EIB declared that it “had fully achieved its i2i objectives” upon extending some Euro 14.4 billion in loans.³⁵⁶

267. Even if the Panel were to find that the entirety of the EIB’s lending activity over 50 years constitutes a single subsidy program for purposes of Article 2.1(c) of the SCM Agreement, that would not deprive the i2i program of its status as a subsidy program. The Panel would be confronted with the question of how to analyze specificity with respect to a subsidy provided pursuant to a program within a program. The last sentence of Article 2.1(c) indicates that the Panel should evaluate the 2002 EIB loan to EADS within the frame of reference of the particular program under which it was granted rather than the broader program consisting of all activity of the EIB as a whole.

268. The last sentence of Article 2.1(c) requires account to be taken of “the length of time during which the subsidy programme has been in operation.” As explained in response to the Panel’s Question 13, in the case of a subsidy program that has been in operation for decades, taking account of this factor means identifying a more meaningful temporal frame of reference in which to examine the subsidies at issue. In such a case, using the entire program as a frame of reference would have the absurd result that subsidies would escape findings of specificity simply

³⁵⁴ *The Innovation 2000 Initiative, Actively promoting a European economy based on knowledge and innovation*, European Investment Bank, at 3 (Exhibit US-154) (discussed in U.S. Responses to First Panel Questions, para. 93). The EC asserts that “{t}he use of the word ‘programme’ by the granting authority naturally is not dispositive of the legal nature of the measure under the *SCM Agreement*.” EC SWS, para. 445. However, as just discussed, the SCM Agreement uses the term “programme” consistently with its ordinary meaning. The fact that the granting authority itself considers a series of subsidies to constitute a “programme,” therefore, is highly relevant.

³⁵⁵ *The Innovation 2000 Initiative, Actively promoting a European economy based on knowledge and innovation*, European Investment Bank, at 2-3 (Exhibit US-154).

³⁵⁶ European Investment Bank, Annual Press Conference 2003, Background Note No. 1: Innovation and Knowledge-Based Economy, at 1 (Exhibit US-164) (discussed in U.S. Responses to First Panel Questions, para. 96).

by virtue of being granted under the auspices of a program that had been in operation for decades.³⁵⁷ The logical alternative is to base a specificity analysis on the particular program within a program pursuant to which subsidies are granted. Thus, if the Panel were to view both the entire lending activity of the EIB and the i2i program as “subsidy programs” within the meaning of Article 2.1(c), it should evaluate whether the 2002 loan to EADS is specific by using the i2i program as its frame of reference.³⁵⁸

269. The same reasoning also applies to the EIB loans provided to Airbus from 1988 to 1993. Even though these loans were not provided pursuant to particular subsidy programs, such as the i2i program, treating the entire lending activity of the EIB over the course of 50 years as the frame of reference for a specificity analysis is inappropriate, for the reasons discussed in response to the Panel’s Questions 13, 15, and 119. In view of the length of time the EIB has been in operation, it is necessary to adopt a more meaningful frame of reference, such as the categories that the EIB itself uses to describe its lending activity.³⁵⁹

D. INFRASTRUCTURE

219. At paragraphs 51-53 of its SCOS, the United States makes an argument concerning the French-German compromise solution to the question of the location of the A380 site (in response to an argument made by the EC that the decision to co-locate the A380 assembly site []). Would the parties please comment on the United States’ argument, including its underlying premises, and discuss the implications for assessing the ‘benefit’ conferred on Airbus if this argument were accepted.

Response:

270. In its second written submission, the EC argued that even if the City of Hamburg’s provision to Airbus of an industrial site adjacent to an existing Airbus site were found to be a subsidy, that subsidy has not caused adverse effects to the interests of the United States. In essence, the EC asserts that Airbus’s decision to co-locate the A380 assembly operation in Toulouse and Hamburg [] and that this [] offset the [] The EC contends that, therefore, Airbus has not been able to use the subsidy received from the City of Hamburg to []³⁶⁰

³⁵⁷ See U.S. Responses to First Panel Questions, paras. 85-91.

³⁵⁸ See U.S. Responses to First Panel Questions, paras. 92-102.

³⁵⁹ See U.S. Responses to First Panel Questions, paras. 85-91, 103-107, 365-370.

³⁶⁰ See EC SWS, paras. 1080 and 1089.

271. Even if the EC's allegation regarding Airbus's motivations for accepting Hamburg's provision of infrastructure were relevant to a benefit analysis (which, as discussed below, it is not), the EC's argument still would fail. As a factual matter, the EC's assertion that Airbus's decision to co-locate A380 assembly in Toulouse and Hamburg [

] ³⁶¹ is wrong. In its second confidential oral statement, the United States demonstrated the inaccuracy of this assertion, using Airbus' own internal documents as submitted by the EC. The United States showed that Airbus made a fundamentally economic decision, valuing the pros and cons of co-locating A380 assembly in Toulouse and Hamburg and coming to the conclusion that the overall impact on the [] ³⁶².

272. Secondly, the Panel should note that the EC does not argue that the alleged [] from co-locating the A380 assembly operation in Toulouse and Hamburg reduces or eliminates the benefit to Airbus conferred by Hamburg's provision of infrastructure. Rather, the EC confines its argument to the issue of whether that provision of infrastructure (if, as the United States has shown, it constitutes a subsidy within the meaning of Article 1 of the SCM Agreement) is causing adverse effects to the interests of the United States. Accordingly, the response to the EC in the U.S. second confidential oral statement focuses on adverse effects, not on benefit. ³⁶³

273. In fact, the EC's allegation that Airbus might have located the A380 assembly site entirely in Toulouse if Hamburg had charged it a price that included the cost of creating the infrastructure is irrelevant to a consideration of the benefit conferred by the Hamburg infrastructure. The relevant benchmark for determining whether or not a financial contribution confers a benefit within the meaning of Article 1 of the SCM Agreement is the marketplace. The question for the Panel is whether Airbus "has received a 'financial contribution' on terms more favorable than those available to {it} in the market."³⁶⁴ Why Airbus may have accepted that financial contribution (and whether accepting it made economic sense) has no bearing on the answer to that question.

274. As the United States has shown in previous submissions and statements (and in response to Questions 154 and 155, above), Airbus received a benefit from Hamburg's creation and

³⁶¹ EC SWS, para. 1089.

³⁶² See U.S. SCOS, paras. 51-53.

³⁶³ See U.S. SCOS, paras. 50-53. The Panel also should note that the EC's argument addresses only the question of whether the infrastructure subsidy contributes to []. It does not address the question of whether the infrastructure subsidy causes other types of adverse effects included in the U.S. claim. See EC SWS, paras. 1077-1089.

³⁶⁴ *Canada - Aircraft (AB)*, para. 157; see also U.S. FWS, para. 110.

provision of a custom-made industrial site, which necessitated (among other investments) the reclamation of land immediately adjacent to Airbus's existing site at Finkenwerder. A market participant would have created the plot of land needed by Airbus only in exchange for adequate remuneration, which, at a minimum, would have compensated it for its investment into creating the land. The government of Hamburg, however, charged Airbus a price that did not include Hamburg's Euro 751 million investment into creating the site.³⁶⁵

275. Furthermore, even if the EC were correct in asserting that the decision to co-locate A380 assembly [] its argument would amount to a sort of "inefficiency defense," which has no basis in the SCM Agreement and which would lead to absurd results. Following the EC's logic, a government granting a subsidy can successfully defend itself against a claim under Article 5 of the SCM Agreement if it can show that the subsidy is offset by losses that the recipient incurred because it inefficiently allocated its resources as a result of receiving the subsidy. In the EC's view, such offsets negate the possibility of causing adverse effects through the use of the subsidy.

276. The implications of permitting this non-text-based "inefficiency defense" would be quite dramatic. Subsidies are often provided to offset some comparative disadvantage (real or imagined) that a country or region is perceived to have as compared to another country or region. The EC's proposed "inefficiency defense" would amount to an exemption from SCM Agreement disciplines for such subsidies. And, for all types of subsidies, the EC's proposal would seem to be an invitation for Members facing claims under the SCM Agreement to retroactively identify alternative business decisions that subsidy recipients would have made and that would have been more efficient than accepting the subsidy.

277. Further, interpreting the SCM Agreement as permitting a carve-out for inefficient subsidies would have the perverse effect of diverting resources away from their "optimal use," contrary to one of the stated objectives of the *Marrakesh Agreement Establishing the World Trade Organization* (of which the SCM Agreement, of course, is a part).³⁶⁶ It also would be contrary to the objective of "ensur{ing} that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development."³⁶⁷ If locating economic activities in a developing country would be efficient due to a comparative advantage in labor, infrastructure, and raw material costs, the EC's argument would excuse a subsidy inducing an inefficient diversion away from that location.

³⁶⁵ See U.S. FWS, paras. 423-442; U.S. FNCOS, paras. 82-83; U.S. FCOS, paras. 38-45; U.S. SWS, paras. 311-315, 332-338, 352-361; U.S. SNCOS, paras. 86-87; U.S. SCOS, para. 48.

³⁶⁶ *Marrakesh Agreement Establishing the World Trade Organization*, first preambular clause.

³⁶⁷ *Marrakesh Agreement Establishing the World Trade Organization*, second preambular clause.

278. In conclusion, Airbus's motives for accepting Hamburg's provision of infrastructure on advantageous terms, as well as the alternative business decisions Airbus might have made had it not accepted the infrastructure, are irrelevant to an analysis of whether provision of the infrastructure confers a benefit and to an analysis of whether (as a subsidy) it causes adverse effects. The reasons for making a given business decision may be manifold. Rather than attempting to discern the different motives for Airbus's decision to accept Hamburg's provision of infrastructure on advantageous terms – an exercise with no basis in the SCM Agreement – the Panel should take that decision as a given and undertake its benefit analysis and its adverse effects analysis against the background of that decision.

220. In determining whether there has been a financial contribution within the meaning of Article 1.1(a)(1)(iii) of the SCM Agreement, which party bears the onus of establishing that goods or services provided by a government are not (or are) general infrastructure?

Response:

279. Given the way in which the evidence and arguments in this dispute have developed, the Panel need not address the general issue identified in this question in order to make findings necessary to settle the dispute as it relates to the U.S. infrastructure-related claims. The United States has shown that in Hamburg, Bremen, and Toulouse, government authorities created infrastructure custom-made for Airbus and provided it to Airbus for its exclusive use, and that, as the provision of goods or services other than general infrastructure, these provisions are financial contributions within the meaning of Article 1 of the SCM Agreement.³⁶⁸

280. In response, the EC has not argued that the United States failed to make a *prima facie* case that the government-provided goods or services at issue were other than general infrastructure. Rather, it has tried (unsuccessfully) to rebut that *prima facie* case by advancing what it refers to as its “general infrastructure defence.”³⁶⁹ This is in marked contrast to the EC's response to certain other U.S. claims, in which the EC has asserted (incorrectly) a failure to make a *prima facie* case.³⁷⁰

³⁶⁸ See, e.g., U.S. FWS, paras. 423-430 (Hamburg); 450-452 (Bremen); 456-463, 481-483 (Toulouse).

³⁶⁹ EC SWS, para. 345; see also EC FWS, paras. 858, 875, 922, 940 (claiming that various provisions of goods or services constitute general infrastructure).

³⁷⁰ See, e.g., EC FWS, paras. 348 (alleging lack of *prima facie* case regarding Launch Aid for A350), 937 (alleging lack of *prima facie* case regarding benefit conferred by provision of certain facilities at Airbus's Aéroconstellation site).

281. In making its “general infrastructure defence,” however, the EC fails to rebut the U.S. showing that the infrastructure provided to Airbus is “goods or services other than general infrastructure.” The EC relies on an overly broad understanding of what constitutes “general infrastructure,” which encompasses any infrastructure created for purposes of “fulfilling a public policy objective.”³⁷¹ As the United States has discussed in prior submissions and statements, the EC’s approach causes the general infrastructure exception to swallow the rule as to when a government provision of goods or services constitutes a financial contribution.³⁷² A government can identify a public policy objective – such as increasing tax revenue or employment³⁷³ – for virtually any project it undertakes. Thus, following the EC’s logic, it is difficult to conceive of infrastructure a government might provide that would not be general. In other words, the EC would render the word “general” in Article 1.1(a)(1)(iii) redundant with the word “infrastructure,” contrary to customary rules of interpretation of public international law. As the EC’s understanding of what constitutes “general infrastructure” is contrary to the ordinary meaning of that term in context and in light of the object and purpose of the SCM Agreement, the “general infrastructure defence” built on that understanding fails.

282. Because the EC has failed either to show that the goods or services provided to Airbus in Hamburg, Bremen, and Toulouse are general infrastructure, or to rebut the U.S. showing that they are other than general infrastructure, the Panel should not need to make a generic finding as to which party has the burden to show that government-provided goods or services are general infrastructure or not. To the extent the Panel believes, nevertheless, that making such a finding would aid in the settlement of this dispute, the view of the United States is that it is the complaining party that must demonstrate that government-provided goods or services are “other than general infrastructure” and that, therefore, a financial contribution exists. As noted above, in this dispute, the United States has made that demonstration, and the EC has failed to rebut it.

221. What factors are relevant to the determination as to whether infrastructure is ‘general’ for purposes of Article 1.1(a)(1)(iii) of the SCM Agreement and how does this determination differ from the determination as to whether a subsidy is ‘specific’ within the meaning of Article 2?

Response:

³⁷¹ EC FWS, para. 716; *see also id.*, paras. 706, 711, 719, 721, 724, 923; EC FNCOS, para. 88; EC Responses to First Panel Questions, paras. 218, 221, 229; EC SWS, paras. 349, 375-380. Also, the EC takes the unsupported view that infrastructure is presumed to be general and becomes non-general only when limitations on the use of the infrastructure are “clearly specified” and “restricted by regulation.” EC SWS, paras. 333, 336-339.

³⁷² *See* U.S. SNCOS, paras. 79-82; U.S. SWS, paras. 305-310; U.S. FNCOS, para. 79; U.S. Responses to First Panel Questions, paras. 136-139.

³⁷³ *See* EC SNCOS, para. 216 (asserting that government’s return from provision of infrastructure to a particular company includes not just the purchase price but also “higher tax revenues and increased employment”).

283. As discussed in response to Question 152, above, based on the ordinary meaning of the word “general,” infrastructure is “general infrastructure” as that term is used in Article 1.1(a)(1)(iii) of the SCM Agreement if it 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.³⁷⁴ Thus, the two key factors for the Panel to consider in determining whether infrastructure is “general” are (1) openness to all or nearly all users on a universal, non-discriminatory basis, and (2) absence of *de jure* or *de facto* limitations on use. In addition to being consistent with the ordinary meaning of the term “general” in context and in light of the object and purpose of the SCM Agreement, this interpretation is confirmed by the preparatory work of the SCM Agreement.³⁷⁵

284. During negotiation of the SCM Agreement, an exception for general infrastructure originally was discussed as part of an effort to define “non-actionable” subsidies, a subject ultimately dealt with in Article 8. In an intervention discussing the rationale for making certain types of measures, including measures relating to general infrastructure, non-actionable, the EC explained:

Action in these fields may have an effect on the economy of a country, and thus on the international economy, but they are not normally subsidies, because they merely contribute to setting the terms and conditions of a country’s economic and business environment. {T}herefore they do not alter the competitive position of firms.³⁷⁶

285. Other parties made similar interventions. For example, the United States indicated that “basic infrastructure where there are no *de jure* or *de facto* limitations on use” should be treated as non-actionable.³⁷⁷ Canada proposed that “assistance to furnish or support basic infrastructure for general public use” should be non-actionable.³⁷⁸

³⁷⁴ See U.S. FNCOS, para. 79; U.S. Responses to First Panel Questions, paras. 136-137.

³⁷⁵ See *Vienna Convention on the Law of Treaties*, Art. 32 (“Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31. . . .”).

³⁷⁶ Elements of the Negotiating Framework, Submission by the European Community, MTN.GNG/NG10/W/31, p. 8 (Nov. 27, 1989) (emphases added); see U.S. SWS, para. 308.

³⁷⁷ Elements of the Framework for Negotiations, Submission by the United States, MTN.GNG/NG10/W/29, p. 9 (Nov. 22, 1989).

³⁷⁸ Framework for Negotiations, Communication from Canada, MTN.GNG/NG10/W/25, p. 9 (June 28, 1989) (emphasis added); see also Elements of the Framework for Negotiations, Submission by India, MTN.GNG/NG10/W/33, pp. 2-3 (Nov. 30, 1989) (stating that subsidies that should be considered non-distortive and thus non-actionable include “regional development assistance to support basic infrastructure for general public use” (emphasis added)).

286. Moreover, as discussed in the U.S. second written submission, the foregoing understanding of general infrastructure also is the approach taken by the EC in its state aids regime.³⁷⁹

287. The two factors indicated above – (1) openness to all or nearly all users on a universal, non-discriminatory basis, and (2) absence of *de jure* or *de facto* limitations on use – resemble factors relating to specificity of subsidies, described in Article 2 of the SCM Agreement. However, there is a fundamental difference between the inquiry under Article 1.1(a)(1)(iii) and Article 2 of the SCM Agreement. The question under Article 1.1(a)(1)(iii) is whether infrastructure is general or not, and thus whether the goods or services a government provides are “other than general infrastructure.” The question under Article 2 is whether a subsidy is specific or not.³⁸⁰

288. Finding that infrastructure is not general infrastructure means that the government’s provision of that infrastructure constitutes a “financial contribution” within the meaning of Article 1.1(a)(1). If that financial contribution confers a benefit within the meaning of Article 1.1(b), then a subsidy is deemed to exist. However, the fact that such a subsidy exists does not automatically mean that it is specific within the meaning of Article 2. For example, if a government decides to provide energy at reduced prices to small enterprises, this might be considered the provision of a good or service other than general infrastructure which (because of the reduced prices) confers a benefit and, therefore, constitutes a subsidy. However, because this subsidy is provided to all companies below a certain size threshold, it might be considered non-specific as a matter of law within the meaning of Article 2.1(b) and footnote 2.

289. Having said this, certain of the principles set out in Article 2 for determining whether a subsidy is specific or not also may be relevant to determining whether infrastructure is general or not. For example, under Article 2.1(a), “{w}here the granting authority, or the legislation pursuant to which the granting authority operates, explicitly limits access to a subsidy to certain enterprises, such subsidy shall be specific.” Similarly, as noted above, an explicit limitation on access to infrastructure indicates that the infrastructure is “other than general.”

290. Likewise, Article 2.1(c) refers, *inter alia*, to “use of a subsidy programme by a limited number of certain enterprises” and “predominant use by certain enterprises” as factors indicating that a subsidy is specific. And, as noted above, *de facto* limitations on the use of infrastructure show that the infrastructure is “other than general.”

³⁷⁹ See U.S. SWS, para. 309 and footnote 365.

³⁸⁰ The EC appears to agree with this analysis. See EC SWS, paras. 327-328.

291. Notwithstanding these similarities, however, it would not be appropriate simply to apply all of the principles for determining whether a subsidy is specific to the determination whether infrastructure is general. Given the fundamental difference in the nature of the relevant inquiries, noted above, this would be unworkable. For example, while “extent of diversification of economic activities within the jurisdiction of the granting authority” and “length of time during which the subsidy programme has been in operation” may be relevant to the specificity inquiry, as indicated in the last sentence of Article 2.1(c), it is not at all clear that these factors would be relevant to the general infrastructure inquiry.

E. EXTINCTION AND EXTRACTION OF ALLEGED SUBSIDIES

222. Are there any circumstances in which the transfer of funds or other assets by the recipient of a subsidy to an entity other than the granting authority constitutes a ‘repayment’ or withdrawal of the subsidy for purposes of the SCM Agreement? Are there any circumstances in which the transfer of funds or other assets by the recipient of a subsidy to the granting authority would not constitute the ‘repayment’ or withdrawal of the subsidy for purposes of the SCM Agreement?

Response:

292. The transfer of funds or other assets by the recipient of a subsidy to an entity other than the granting authority does not constitute withdrawal of the subsidy for purposes of the SCM Agreement. Under the two articles on withdrawal of subsidy relevant to this dispute – Article 4.7 (regarding withdrawal of prohibited subsidies) and Article 7.8 (regarding withdrawal of actionable subsidies) – it is incumbent on the Member to withdraw subsidies. These provisions are not drafted in the passive voice. They do not provide merely that subsidies “shall be withdrawn.” Rather, they are drafted in the active voice, focusing in particular on action that the Member must take. Thus, Article 4.7 provides for a recommendation “that the subsidizing Member withdraw the subsidy without delay.” (Emphasis added.) Likewise, Article 7.8 provides that “the Member granting or maintaining such subsidy {i.e., a subsidy that has resulted in adverse effects to the interests of another Member} shall take appropriate steps to remove the adverse effects or shall withdraw the subsidy.” (Emphasis added.) Accordingly, it is the Member that must affirmatively do something by “remov~~ing~~” or “taking away” the subsidy.³⁸¹ A transfer of funds or other assets by the subsidy recipient to an entity other than the

³⁸¹ *Brazil - Aircraft (Article 21.5) (AB)*, para. 45; *US - FSC (Article 21.5) (AB)*, paras. 226-227; *see also Australia - Leather (Article 21.5)*, para. 6.27.

granting authority does not amount to such removal or taking away of the subsidy by the Member; it is not the act of withdrawal provided for in Article 4.7 or 7.8.³⁸²

293. As for “repayment” of subsidy, this is not a term used in the SCM Agreement. In *Australia - Leather (Article 21.5)*, the panel did find that repayment of a subsidy was one way to “effectuate withdrawal of the subsidy by a subsidizing Member.”³⁸³ What the panel in that dispute considered as “repayment” was a payment back to the government by the subsidy recipient,³⁸⁴ which is consistent with the ordinary meaning of “repayment.”³⁸⁵ The act of paying subsidy back to the government (absent the government giving anything new in return) necessarily implies a taking away of subsidy by the government, consistent with the ordinary meaning of “withdraw,” as noted above. The act of paying a third party, by contrast, carries no such implication, and the *Australia - Leather (Article 21.5)* panel did not suggest otherwise.

294. In this dispute, the EC has not alleged that transfers of funds or assets by Airbus to entities other than the government grantors of subsidies amounted to the repayment of subsidies. It has alleged, however, that the Euro 3.133 billion that Deutsche Airbus paid to its parent, DaimlerChrysler, in 2000 constituted a withdrawal of subsidies.³⁸⁶ For the reasons discussed above, that transaction does not amount to a withdrawal of subsidies within the meaning of Article 4.7 or 7.8 of the SCM Agreement.

295. Additionally, as discussed in prior U.S. submissions and statements, the so-called “extraction” theory on which the EC bases its allegation regarding the effects of the Deutsche Airbus transaction (as well as its similar allegation regarding CASA’s Euro 342.4 million

³⁸² This understanding of the term “withdraw” does not exclude other ways by which a Member might come into compliance with its SCM Agreement obligations. With respect to a finding of breach of Article 5, a Member has the option to “take appropriate steps to remove the adverse effects.” SCM Agreement, Art. 7.8. Also, the sale of a subsidized entity in a transaction at arm’s length, for fair market value, involving all or substantially all of the entity and a relinquishment of control by the seller could result in the extinguishment of subsidies. Such a sale could obviate the need for a Member to take further action to come into compliance with its SCM Agreement obligations.

³⁸³ *Australia - Leather (Article 21.5)*, para. 6.28.

³⁸⁴ *Australia - Leather (Article 21.5)*, para. 1.3 (“Australia stated that on 14 September 1999, Howe had repaid the Australian Government \$A8.065 million, an amount which covered any remaining inconsistent portion of the grants made under the grant contract.”).

³⁸⁵ *The New Shorter Oxford English Dictionary*, vol. 2, p. 2548 (1993) (defining “repayment” as “payment back of money etc.”).

³⁸⁶ See, e.g., EC FWS, paras. 255, 287; EC Responses to First Panel Questions, para. 315. In its confidential opening statement at the second Panel meeting, the EC clarified that it does not allege that the Deutsche Airbus cash transfer to its parent constituted “repayment” of subsidies. EC SCOS, para. 5.

transfer to its owner, the government of Spain) is without any basis in the SCM Agreement.³⁸⁷ In fact, the EC acknowledges as much, citing instead what it deems to be “economic common sense”³⁸⁸ and asserting the existence of a supposed “‘but for’ test” for analyzing the effects of a subsidized entity’s cash transfers to its parent³⁸⁹ (even though elsewhere the EC abjures the use of non-text-based “but for” tests³⁹⁰).

296. As noted in previous U.S. submissions, if it were the case that subsidies could be “extracted” or withdrawn through transfers of funds or assets to entities other than the granting authority, opportunities to circumvent the SCM Agreement would be numerous. For example, every time a subsidized company bought stock back from or paid a dividend to its shareholders – both examples of transfers in which cash is “removed from {a company’s} reach”³⁹¹ – it would be extracting subsidy, under the EC’s theory. The SCM Agreement simply does not provide for this circumvention of its disciplines.³⁹²

297. With respect to the second part of the Panel’s question, there are circumstances in which the transfer of funds or other assets by the recipient of a subsidy to the granting authority would not constitute the “repayment” or withdrawal of the subsidy for purposes of the SCM Agreement. One such circumstance is when the transfer of funds or other assets is subject to a *quid pro quo* – that is, when the government gives the subsidy recipient something of value in exchange for the transfer or foregoes the taking from the subsidy recipient of something to which the government otherwise would be entitled. An example of this circumstance is the payment by CASA of Euro 340 million to the company’s majority owner, the government of Spain (which was accompanied by a payment of Euro 2,447,535.12 to its other shareholders, primarily

³⁸⁷ See, e.g., U.S. FNCOS, paras. 122-124; U.S. Responses to First Panel Questions, paras. 344-348; U.S. SWS, paras. 537-555. In its non-confidential opening statement at the second Panel meeting, the United States pointed out that the EC seemed to have abandoned its “extraction” theory, as it offered no defense of that theory in its second written submission. See U.S. SNCOS, para. 134 and footnote 190. In an apparent attempt to revive that theory, the EC discussed it in a cursory manner in its confidential opening statement at the second Panel meeting, repeating assertions it previously had made and still offering no basis in the SCM Agreement for its theory. See EC SCOS, paras. 2-7.

³⁸⁸ EC FWS, para. 225.

³⁸⁹ EC Responses to First Panel Questions, para. 313.

³⁹⁰ EC Responses to First Panel Questions, para. 146.

³⁹¹ EC Closing Statement at First Panel Meeting, para. 10.

³⁹² See, e.g., U.S. SWS, paras. 537-555; U.S. Responses to First Panel Questions, paras. 344-348; U.S. FNCOS, paras. 122-124.

DaimlerChrysler), in 2000, in preparation for CASA's participation in the newly created EADS.³⁹³

298. As the EC explains:

Based on these assessments {by various investment banks}, and after extensive discussion, the parties {i.e., ASM, DASA, and CASA} agreed on the relative valuations of their assets. They recognized that the relative values of CASA and DASA were far in excess of their agreed participation in EADS. As a result, in order to bring CASA's value into parity with its agreed pre-IPO 6.25 percent share of EADS, it was agreed that CASA would pay the Spanish State € 342.4 million in cash before CASA was contributed to EADS.³⁹⁴

299. Subsequently, the EC explains, "the Spanish State exchanged its 99.29 percent interest in CASA for 44,690,871 EADS shares."³⁹⁵

300. In other words, the shares that the government of Spain received in EADS represented its 99.29 percent interest in CASA following the Euro 342.4 million cash transfer from CASA to the government and other shareholders. Had that transfer not occurred, the value of the CASA assets that Spain contributed to the newly formed EADS would have been greater.³⁹⁶ Consequently, Spain's share in EADS represented by its 99.29 percent interest in CASA would have been greater. Put another way, the government of Spain gave up a larger stake in EADS – that is, it brought the value of its contribution to EADS (i.e., the assets of CASA) "into parity with its agreed pre-IPO 6.25 percent share of EADS" – in exchange for the cash transfer from CASA. Because the government gave something of value – relinquishment of a larger stake in EADS – in exchange for the cash transfer from CASA, that transfer did not amount to a repayment, withdrawal, or "extraction" of subsidy, as the EC alleges.

³⁹³ See EC FWS, para. 253. The EC describes this transaction as a payment by CASA to the government of Spain of Euro 342.4 million, following which the government "passed € 2.4 million to other shareholders." *Id.*, para. 253 and footnote 170. However, the EADS Offering Memorandum that the EC cites describes the transaction as follows: "SEPI {the entity holding the Spanish government's stake in CASA} has extracted an amount of Euro 340 million from CASA by way of distribution of reserves and reduction of capital pursuant to a decision of the general meeting of shareholders of CASA dated April 27, 2000. The cash extraction corresponding to CASA's shareholders other than SEPI amounts to Euro 2,447,535.12 (i.e. a total cash extraction of Euro 342,447,535.12)." EADS Offering Memorandum at 143 (Exhibit EC-24).

³⁹⁴ EC FWS, para. 253 (internal footnotes omitted) (emphasis added).

³⁹⁵ EC FWS, para. 259. The remaining 0.71 percent interest in CASA was held by DaimlerChrysler, and was exchanged by DaimlerChrysler, along with its interest in DASA, for shares of EADS. *Id.*

³⁹⁶ See EC FWS, footnotes 168 and 173 (setting forth the valuation ratios of the founders of EADS before and after the "cash extractions").

301. The EC asserts that “{i}n no case was a ‘larger stake’ {in EADS for the government of Spain} on offer.”³⁹⁷ But, this assertion misses the point. The point is not that the founders of EADS actually considered the option of giving Spain a larger share of EADS in exchange for a larger contribution of CASA assets by Spain (*i.e.*, a contribution that included the Euro 342.4 million in funds). The point is that the share of EADS that Spain actually received represented Spain’s contribution of CASA assets; that contribution was smaller as a result of the cash transfer. Spain agreed to take a stake in EADS that was smaller than the stake that would have been attributable to the CASA assets had the cash transfer not occurred. Accordingly, the cash transfer was not a repayment of subsidies, but a payment in exchange for the government’s acceptance of a smaller stake in EADS.

223. Could the Parties please comment on the assertion at para. 55 of the EC’s SNCOS that United States and international accounting standards “require the purchaser of a company to adjust the balance of any loan carrying a below market rate to reflect a market interest rate, thereby recognizing that the seller extracted the value of the below market rate loan in the price of the business”? Does the change in the “book” value of the liability impact the repayment terms of any such loans transferred to the purchaser?

Response:

302. The EC cites the U.S. and international accounting standards at issue as evidence of the supposed “economic reality” of its proposed approach to analyzing whether certain transactions extinguished or extracted subsidies provided to Airbus.³⁹⁸ As previously discussed, all but one of the transactions alleged to have extinguished subsidies involved less than 10 percent of the shares in the entities concerned. None of the transactions at issue involves the sale of a subsidized entity (i) at arm’s-length; (ii) for fair-market-value; (iii) involving all or substantially all of the subsidized entity; and (iv) resulting in a relinquishment of any controlling interest the seller had in the entity.³⁹⁹

303. Based on the EC’s own description of the cited accounting standards, they have no relevance to the point the EC is trying to make. According to the EC, those standards set out requirements pertaining to “the purchaser of a company.”⁴⁰⁰ They do not set out requirements

³⁹⁷ EC SCOS, para. 7.

³⁹⁸ EC SNCOS, para. 56 (as delivered).

³⁹⁹ See, e.g., U.S. SWS, paras. 520-555; U.S. Responses to First Panel Questions, paras. 324-348; U.S. Response to Panel Question 168, *supra*.

⁴⁰⁰ EC SNCOS, para. 56 (as delivered) (emphasis added).

pertaining to the purchaser of some portion of a company (a portion that the EC alleges may be as small as 0.93 percent of the company's shares⁴⁰¹). Nor do they have any relevance to the cash transfers from a company to its owner that the EC refers to as "extractions." As none of the transactions alleged by the EC to have extinguished or extracted Airbus subsidies involved the purchase of a company (as opposed to small blocks of shares of a company), the accounting standards cited by the EC do nothing to support the "economic reality" of its proposed approach to "extinction" and "extraction" of subsidies.

304. Moreover, even with respect to transactions to which the cited accounting standards do apply, the standards have nothing to do with "recognizing that the seller extracted the value of the below market rate loan in the price of the business."⁴⁰² The standards simply concern accurately reflecting on the purchaser's balance sheet the present, fair market value of the obligations it has assumed. Each debt obligation the purchaser assumes (whether at a subsidized rate or not) will entail a stream of payments to be made over time. The standards cited by the EC require a determination of the present value of that stream of payments by applying an "appropriate current interest rate {}," which will be a market-based rate.⁴⁰³

305. In other words, the transaction that resulted in the purchaser assuming a debt obligation has no relevance to the accounting standards cited by the EC. The standards take the debt obligation as a given, merely requiring the purchaser to account for the present, fair market value of the obligation. As should be evident from the foregoing explanation, this accounting step does not impact the repayment terms of any such obligation. Absent a provision in the loan itself that causes its terms to change upon assumption by a new debtor, the repayment terms would remain exactly as they had been when the loan was granted to the original debtor.

F. CAPITAL INVESTMENTS AND SHARE TRANSFERS

224. What is the relevant test for determining whether, in a claim concerning Part III of the SCM Agreement, government provision of equity capital can be considered to confer a 'benefit' under Article 1.1(b)? To the extent that the parties consider that it is relevant whether the investment decision can be regarded as consistent with the usual investment practice of private investors in the territory of the Member, do the parties consider that the usual investment practice of private investors should be determined in light of the specific circumstances surrounding the government investment? Specifically, how (if at all) do the

⁴⁰¹ See U.S. SWS, para. 526.

⁴⁰² EC SNCOS, para. 56 (as delivered).

⁴⁰³ Statement of Financial Accounting Standards No. 141, Business Combinations, section 37(g) (Exhibit EC-837); International Financial Reporting Standard 3, Business Combinations, Appendix B, Application supplement, section B16(j) (Exhibit EC-838).

parties consider the following circumstances, in which a government provision of equity capital was made, to be relevant to determining the usual investment practice of private investors:

- (a) where the recipient entity is financially distressed, the government is a significant creditor of that entity and the capital contribution occurred in the context of a restructuring of that entity;**
- (b) where the recipient entity is wholly-owned by the government, and the capital contributions were made in order to meet the ongoing capital requirements of the entity;**
- (c) where the recipient entity is wholly-owned by the government and the capital contribution occurred in the context of a consolidation of the government’s assets in anticipation of a sale of shares in that entity.**

Response:

306. Part III of the SCM Agreement does not set out a “test” for determining whether a government provision of equity capital can be considered to confer a “benefit” under Article 1.1(b). Following customary rules of interpretation of public international law, the term “benefit” should be construed in accordance with its ordinary meaning, in context, and in light of the object and purpose of the SCM Agreement. As the Appellate Body explained in *Canada - Aircraft*, “the ordinary meaning of ‘benefit’ clearly encompasses some form of advantage.”⁴⁰⁴ The Appellate Body also found that, to identify whether such an advantage exists, an appropriate inquiry is “whether the recipient has received a ‘financial contribution’ on terms more favorable than those available to the recipient in the market.”⁴⁰⁵

307. Moreover, the Appellate Body found that while Article 14 of the SCM Agreement sets forth guidelines applicable to Part V of the agreement, it also “constitutes relevant context for the interpretation of ‘benefit’ in Article 1.1(b).”⁴⁰⁶ As relevant to the present question, the guideline in Article 14 concerning government provision of equity infusions states:

{G}overnment provision of equity capital shall not be considered as conferring a benefit, unless the investment decision can be regarded as inconsistent with the usual investment

⁴⁰⁴ *Canada - Aircraft (AB)*, para. 153.

⁴⁰⁵ *Canada - Aircraft (AB)*, para. 157.

⁴⁰⁶ *Canada - Aircraft (AB)*, para. 155.

practice (including for the provision of risk capital) of private investors in the territory of that Member.⁴⁰⁷

308. In this dispute, both the United States and the EC have stated that in determining whether a government equity infusion confers a benefit and thus constitutes a subsidy, it is appropriate for the Panel to consider whether providing the infusion was consistent with the usual investment practice of private investors in the territory of the Member at issue.⁴⁰⁸ Regarding how the Panel should determine the usual investment practice of private investors, the United States will discuss each of the circumstances identified by the Panel, in turn.

Part (a)

309. The circumstances described in part (a) of the Panel's question correspond to the circumstances of the equity infusion the German government provided to Deutsche Airbus in 1989 as an integral part of the restructuring of Deutsche Airbus. In this regard, the United States refers the Panel to its responses to Questions 156 and 157, above, as well as to its discussion of this issue in previous submissions and statements.⁴⁰⁹

310. The United States notes that other panels have had occasion to consider circumstances similar to those described in part (a) of the Panel's question. For example, in *Korea - Commercial Vessels*, the panel examined the restructuring of the Daewoo company, which involved debt-for-equity swaps (a form of equity infusion).⁴¹⁰ It considered whether the participation of certain creditors in these swaps was consistent with the usual investment practice of private investors.⁴¹¹ At the outset of its analysis, the panel noted Korea's argument that "Daewoo's creditors acted on the basis of a report by {the accounting firm} Anjin to the effect that the going concern value of Daewoo exceeded its liquidation value."⁴¹² The panel considered that "the evidence and arguments concerning the Anjin report are very relevant to the

⁴⁰⁷ SCM Agreement, Art. 14(a).

⁴⁰⁸ See, e.g., U.S. FWS, paras. 544-545, 561-564; EC FWS, para. 1215; EC SNCOS, para. 267.

⁴⁰⁹ See, e.g., U.S. FWS, paras. 546-547; U.S. SWS, paras. 451-462; U.S. SNCOS (as delivered), paras. 109-111.

⁴¹⁰ See *Korea - Commercial Vessels*, para. 7.413.

⁴¹¹ Earlier in its report, the panel found these creditors to be "public bodies." See *Korea - Commercial Vessels*, para. 7.426.

⁴¹² *Korea - Commercial Vessels*, para. 7.436.

commercial reasonableness of the decision to restructure Daewoo.”⁴¹³ Later in its report, the panel noted that “when a company is insolvent, a creditor operating on a commercially reasonable basis will be seeking to minimize its losses/maximize its recovery.”⁴¹⁴ The panel concluded, relying heavily on the Anjin report (among other factors), that the creditors’ participation in the Daewoo restructuring was consistent with such “commercially reasonable conduct.”⁴¹⁵

311. The *Korea - Commercial Vessels* report is relevant to the present dispute in part because of the panel’s analysis of circumstances similar to those described in part (a) of the present question, but also because of the EC’s discussion in that earlier dispute of the very issue now at hand. The *Commercial Vessels* panel asked the EC “what criteria should determine whether to keep an insolvent company in operation” and “what weight or importance should be given to a going concern analysis or assessment.”⁴¹⁶ In response, the EC stated:

{W}here the outcome of a bankruptcy proceeding or a corporate restructuring is determined by public bodies – or private bodies acting under their direction – and leads to a more beneficial outcome for the enterprise than would have arisen if the creditors had acted according to market principles, all of the components of a subsidy are present. There is no basis in the *SCM Agreement* to allow insolvency to be a loophole in the subsidy disciplines.⁴¹⁷

312. The EC then enumerated “relevant criteria to determine whether to keep an insolvent company in operation.” Among them was, “{w}ith respect to a debt for equity swap, . . . whether a rationale {sic} private investor operating in a market economy would have purchased the equity at the price provided in the restructuring plan.”⁴¹⁸

313. Finally, the EC stated, “As to evidence, the EC considers that the primordial indicia is the behaviour of actual other creditors that were not influenced by the government.” It added that “the existence of a going concern analysis can be an indicia that a hypothetical private creditor

⁴¹³ *Korea - Commercial Vessels*, para. 7.437 (emphasis added).

⁴¹⁴ *Korea - Commercial Vessels*, para. 7.493.

⁴¹⁵ *Korea - Commercial Vessels*, paras. 7.494 - 7.495.

⁴¹⁶ *Korea - Commercial Vessels*, p. D-19 (Question 23 from the panel to the EC).

⁴¹⁷ *Korea - Commercial Vessels*, p. D-20, para. 97 (EC response to Question 23 from the panel).

⁴¹⁸ *Korea - Commercial Vessels*, p. D-20, para. 98 (EC response to Question 23 from the panel) (emphasis added).

would have acted in the same manner, if that analysis contains the above elements and was provided to the creditors in sufficient time so as to take an informed decision.”⁴¹⁹

314. Other panels have relied on similar considerations in analyzing whether a financial contribution was consistent with the usual investment practice of private investors and thus whether it conferred a benefit. In the recently circulated report in *Japan - DRAMs*, for example, a panel reviewed findings by the Japan investigating authorities (“JIA”) in a countervailing duty investigation. As relevant here, the JIA had found that the government of Korea had entrusted or directed certain creditors to participate in two debt restructurings involving the Hynix company, giving rise to “financial contributions” within the meaning of Article 1.1(a)(1)(iv) of the SCM Agreement. Among the factors on which the JIA had relied was a finding that the creditors’ conduct was commercially unreasonable. The panel upheld that finding with respect to one of the debt restructurings and, based on the same reasoning, also upheld the JIA’s finding that the restructuring conferred a benefit.⁴²⁰ In reaching its conclusion that the JIA had laid out an appropriate framework for its commercial reasonableness analysis, the panel quoted at length from the JIA’s findings, including the following passage:

‘{I}rrespective of whether one is an existing creditor or not, financial institutions examine a variety of factors from a profit-maximization or loss-minimization perspective such as the financial conditions of the pertinent company, its future potential, comparison of its going-concern value with its liquidation value when making investment or lending decisions. If such an examination was carried out in a reasonable manner, then it can be said that a commercially reasonable decision had been made based on the results of the examination even if the result was the incurrence of a loss. On the other hand, in the case where the examination was insufficient, then one cannot make a finding that a commercially reasonable decision had been made even if it resulted in generation of profit.’⁴²¹

315. The same actions by the government of Korea at issue in *Japan - DRAMs* also were at issue in *EC - DRAMs*. In the latter dispute as in the former, Korea argued that “the banks invested in Hynix because they believed that the going concern value of Hynix was greater than its liquidation value.” In rejecting that assertion, the panel in *EC - DRAMs* cited with approval

⁴¹⁹ *Korea - Commercial Vessels*, p. D-20, para. 99 (EC response to Question 23 from the panel) (emphases added).

⁴²⁰ *Japan - DRAMs*, paras. 7.246, 7.252, 7.281.

⁴²¹ *Japan - DRAMs*, para. 7.128 (quoting from JIA Final Determination, Annex 3 (Rebuttals and Surrebuttals), para. 142) (emphases added).

the EC's argument that "the banks do not seem to have based this conclusion on independent assessment studies, as could be expected given the situation of Hynix."⁴²²

316. The very same observation could be made with respect to the German government's 1989 decision to provide a DM 505 million equity infusion to Deutsche Airbus as an integral part of a restructuring package. By the standard that the EC itself laid out in the *Korea - Commercial Vessels* dispute and repeated in the *EC - DRAMs* dispute, the conduct of the German government was inconsistent with the usual investment practice of private investors and thus conferred a benefit within the meaning of Article 1 of the SCM Agreement.

317. Unlike the United States – which has offered substantial evidence showing that investing in Deutsche Airbus on the terms and conditions that KfW accepted was inconsistent with the usual investment practice of private investors⁴²³ – the EC has made sweeping and unsubstantiated assertions regarding the 1989 restructuring aid package in general (rather than the equity infusion by KfW in particular). Thus, the EC asserts that "the German government took action to minimize its losses under the circumstances,"⁴²⁴ and that the government got "the best deal any investor could have achieved in this situation,"⁴²⁵ though it provides no evidence for either assertion. In particular, the EC has offered no evidence showing that the German government based its provision of equity to Airbus – as a company "facing imminent insolvency"⁴²⁶ (according to the EC) – on "independent assessment studies,"⁴²⁷ such as studies comparing the going-concern value of Deutsche Airbus with its liquidation value.

318. In the absence of such evidence, the EC has tried to defend the KfW investment as consistent with the usual investment practice of private investors by referring to what it characterizes as a contemporaneous provision of capital to Deutsche Airbus by Daimler-Benz.⁴²⁸ That investment, however, does not make up for the lack of independent assessment studies supporting the German government's investment, because, among other things, the Daimler

⁴²² *EC - DRAMs*, para. 7.208.

⁴²³ See U.S. FWS, para. 546; U.S. SWS, paras. 460-462; see also U.S. Responses to Questions 156 and 157, *supra*.

⁴²⁴ EC SWS, para. 564. See also EC FWS, para. 1179.

⁴²⁵ EC SNCOS, para. 253.

⁴²⁶ EC FWS, para. 1177.

⁴²⁷ *EC - DRAMs*, para. 7.208.

⁴²⁸ Regarding the EC's mischaracterization of this transaction, see U.S. Response to Question 156, *supra*.

investment was heavily “influenced by the government.”⁴²⁹ As the Chairman of Germany’s Monopolkommission observed at the time:

{I}t is known and undisputed that the Federal Government took the initiative for the Daimler-Benz AG/MBB concentration. To this day, {the Federal Government continues to} make it known that it welcomes the formation of the company tie-up. Through agreements with Daimler-Benz AG, MBB and Deutsche Airbus GmbH (Framework Agreement dated March 14, 1989), the companies involved were provided with the financial basis to implement the transaction.⁴³⁰

319. In conclusion, with respect to part (a) of the Panel’s question, the absence of the very indicia of the usual investment practice of private investors that the EC itself identified in earlier disputes and on which the panels in those disputes relied supports a finding that the government provision of equity capital confers a benefit.

Part (b)

320. Turning to part (b) of the Panel’s question, the circumstances described correspond to the circumstances of the equity infusions the French government provided to Aérospatiale from 1987 to 1993. As discussed in previous U.S. submissions and statements, the provision of these infusions was not consistent with the usual investment practice of private investors, due to the extremely poor financial state of Aérospatiale during the periods at issue and the absence of any contemporaneous, independent financial analysis supporting the French government’s decisions.⁴³¹

321. In this case, the specific circumstances of the government’s equity infusions are relevant to a benefit analysis only insofar as they give rise to a need to identify a benchmark other than the market price for the equity. That is, precisely because the company is wholly owned by the government, there is no trading in its shares and thus no possibility of comparing the price the government paid for new shares with a market price. Accordingly, the Panel must consider a different benchmark.

⁴²⁹ *Korea - Commercial Vessels*, p. D-20, para. 99 (EC response to Question 23 from the panel); see U.S. FWS, para. 547; U.S. SWS, paras. 453-459; see also *Korea - Commercial Vessels*, para. 7.434 (panel recognizing that “there could be circumstances in which a government influences the market to such an extent that it becomes distorted, so that private entities no longer operate pursuant to purely commercial principles”).

⁴³⁰ Monopolkommission, para. 249 (Exhibit US-652). Other portions of the Monopolkommission report were provided as Exhibit US-30. However, the above-quoted paragraph was not part of that exhibit.

⁴³¹ See U.S. FWS, paras. 568-573, 581-589, 597-604; U.S. FNCOS, para. 106; U.S. Responses to First Panel Questions, paras. 173-175, 179-186; U.S. SWS, paras. 464-478; U.S. SNCOS, paras. 99-104.

322. The mere fact that the government believed the equity infusions to be necessary to “meet the ongoing capital requirements of the entity” does not cause the infusions to be consistent with the usual investment practice of private investors and thus not to confer a benefit. If it were otherwise, government provisions of capital to state-owned enterprises would almost never be subject to SCM Agreement disciplines; even equity infusions to enterprises in the most dire financial situations could be defended on the grounds of “meet{ing} the ongoing capital requirements of the entity.”

323. It must be borne in mind that the relevant basis for comparison in a benefit analysis is the marketplace.⁴³² While meeting an enterprise’s ongoing capital requirements may be a concern of management or the enterprise’s sole owner, it is not a concern of the market.⁴³³ A market investor, with virtually limitless options for investing its capital, is interested in maximizing returns, regardless of whether that interest coincides with the interest of a particular enterprise in meeting ongoing capital requirements.

324. In view of that objective, as the United States previously explained:

The usual practice of private investors considering whether to invest in a company is to analyze indicators of the company’s financial and commercial health and performance, as reflected in financial statements, and to conduct an objective analysis and in-depth due diligence on the firm to determine whether to invest. Contemporaneous independent analyses of the finances and prospects of the company are among the key types of evidence available to show whether an equity infusion was consistent with the usual investment practice of private investors.⁴³⁴

325. In the case of the French government equity infusions to Aérospatiale between 1987 and 1993, there is no evidence of the government having relied on any such analyses. This is all the more problematic, given that it provided those infusions at a time when the financial indicators to which a private investor would look showed the company to be in a dire situation – leading its CEO to describe the company as “repellant” from an investor’s point of view.⁴³⁵ Accordingly,

⁴³² See *Canada - Aircraft (AB)*, para. 153.

⁴³³ See U.S. FNCOS, para. 106; U.S. Responses to First Panel Questions, para. 183; U.S. SWS, paras. 472-474; U.S. SNCOS, para. 103.

⁴³⁴ U.S. FWS, para. 564 (citing *EC - DRAMs*, para. 7.208).

⁴³⁵ *EC to review Aérospatiale capital injection*, Aerospace Adily, at 217-18 (Feb. 9, 1994) (Exhibit US-275) (quoted in U.S. FWS, para. 602).

the Panel should find that the government's provision of these equity infusions was inconsistent with the usual investment practice of private investors and thus conferred a benefit.

Part (c)

326. The circumstances described in part (c) of the Panel's question correspond to the French government's 1998 transfer of its 45.76 stake in the Dassault company to Aérospatiale. In this regard, the United States refers the Panel to its response to Question 158, 159, and 160, above, as well as to its discussion of this issue in previous submissions and statements.⁴³⁶

327. As discussed in response to Questions 158 and 160, there may well be circumstances in which consolidation of a government's assets in a single entity in anticipation of a sale of shares of that entity would be consistent with the usual investment practice of private investors. That could be the case where, for example, based on a contemporaneous independent financial analysis, the government had a well founded expectation of maximizing its profits through a consolidation of its assets. But, the French government had no such expectation when it transferred its Dassault shares to Aérospatiale.

328. Quite the contrary, in transferring its shares, the government knew with a certainty that it was forfeiting something of significant value – the control over Dassault that it exercised through double voting rights. It ceded that control to the Dassault family without any compensation. A private investor would knowingly incur such a loss only if it had a well founded basis for believing that its loss would be offset by the profits it would make from the eventual sale of its consolidated assets. Contemporaneous, independent financial analyses of the type described in the earlier parts of this response could enable the investor to form such a belief. But, in the case at hand, the EC has provided no evidence of the French government having relied on any such analyses. Indeed, the evidence indicates that the government's decision to transfer its shares was motivated by political and industrial policy concerns, which would have obviated the need for the financial analyses on which a private investor would have relied.⁴³⁷

329. In short, the specific circumstances in part (c) of this question do not affect the relevance of basic propositions about the usual investment practice of private investors. In particular, private investors seek to maximize profits, and they knowingly incur losses only if they have a well founded basis for expecting offsetting gains. It is not consistent with the usual investment practice of private investors to ignore these principles simply for the sake of consolidating assets in anticipation of a combined sale. Precisely because the French government's transfer of its Dassault assets to Aérospatiale was contrary to these principles, the Panel should find that it is

⁴³⁶ See U.S. FWS, paras. 609-619; U.S. SWS, paras. 479-486; U.S. SNCOS, paras. 105-106.

⁴³⁷ See U.S. Responses to Questions 158, 159, 160, *supra*.

inconsistent with the usual investment practice of private investors and that, therefore, it confers a benefit.

G. ADVERSE EFFECTS

225. The EC has argued that there are multiple subsidized products at issue in this dispute, and multiple corresponding like products. If the Panel were to accept the EC's view, would the Panel be required to assess the question of injury under Article 5(a) with respect to more than one domestic industry? If so, how do the Parties consider that the Panel might undertake such an assessment, in view of the fact that there is only one company in the United States producing large civil aircraft?

Response:

330. As the United States has already indicated orally at the second Panel meeting, that a single producer manufactures all the various U.S. aircraft models that are “like” the several “subsidized products” alleged by the EC – just as there is a single EC producer that manufactures each of those “subsidized products” and is the current recipient of the benefit of all the challenged subsidies – is yet another factor that militates *against* finding multiple subsidized and like products in this dispute.

331. The EC recognizes that “no manufacturer of a single product or family of products, no matter how compelling, has survived in the LCA industry.”⁴³⁸ The EC is correct; LCA producers do not participate only in one or two segments of the LCA product range but must be present in all segments of the LCA market in order to be successful in any of them. Thus, it is not mere happenstance that the only U.S. producer in the EC’s so-called “100-200 seat LCA market” and the only U.S. producer in the EC’s so-called “200-300 seat LCA market,” “300-400 seat LCA market,” and “400-500 seat LCA market” are in fact the same producer. Rather, the one U.S. producer is present in each of these market segments because LCA producers must offer what the EC rightly describes as “a variety of complementary products” to meet the needs of its customers.⁴³⁹

332. The recent “bundled” sale of A320s and A350s to U.S. Airways⁴⁴⁰ well illustrates the difficulty with the EC’s proposed approach. As Airbus insisted on making this customer a bundled offer of both aircraft models, this airline has contracted to import subsidized 100-200

⁴³⁸ EC FWS, para. 30.

⁴³⁹ EC FWS, para. 31.

⁴⁴⁰ U.S. SNCOS, para. 151 (citing Exhibits US-641 and US-642).

seat aircraft as well as subsidized 200-300 or 300-400 seat aircraft⁴⁴¹ from the EC in coming years. The subsidized imports of the A320s therefore do not contribute to the threat of material injury only to what the EC would call the U.S. “100-200 seat LCA domestic industry,” and the subsidized imports of the A350 do not contribute to the threat of material injury only to the “200-300 seat LCA domestic industry.” Rather, all of the subsidized imports threaten injury to the LCA domestic industry, which is comprised of Boeing Commercial Airplanes.

333. In this way, the artificial division of the like product, and therefore the domestic industry, that the EC has proposed would prevent the full consideration of the material injury caused, and threatened to be caused, by the subsidized imports of Airbus LCA.⁴⁴² Nothing in the SCM Agreement contemplates the strained approach advocated by the EC.

334. Moreover, any application of Article 16.5 – which incorporates the provisions of Article 15.6 to the whole of Article 16 – would simply compound the difficulties with the EC approach. Under these provisions, where it is not possible to identify the effect of the subsidized imports on the domestic production of like goods alone, it is permissible to examine data for “the production of the narrowest group or range of products, which includes the like product, for which the necessary information can be provided.” Under the EC theory, if this provision were applied, the impact of imports of each category of subsidized LCA on Boeing’s overall LCA operations would be analyzed separately, and the separate impact of each category of imports would have to rise to the level of causing, or threatening to cause, material injury to the U.S. LCA industry as a whole. Once again, the EC’s excessively narrow approach to the definition of the subsidized product would result in an artificially constrained analysis of the effects of the subsidy that is simply not required or contemplated by the SCM Agreement

⁴⁴¹ The A350, as the EC has explained, can belong to either alleged market, depending on the model. EC FWS, para. 1523.

⁴⁴² The United States has already explained that the EC’s approach would cause similar problems in the context of the Panel’s analysis of serious prejudice. U.S. SWS, para. 645.

LIST OF ADDITIONAL U.S. EXHIBITS

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

<u>U.S. Exhibit</u>	<u>Description</u>
648.	Notice of Final Modification of Agency Practice Under Section 123 of the Uruguay Round Agreements Act, 68 <i>Fed. Reg.</i> 37,125 at 37,127 (June 23, 2003)
649.	<i>The Partido Popular {PP} asks the Spanish Government to increase its EADS stake to 12%</i> , Gaceta de los Negocios (Aug. 10, 2007)
650.	Andrea Thomas, <i>German Govt: No Decision Yet On Taking Golden Share In EADS</i> , Dow Jones (Aug. 6, 2007)
651.	<i>German Government Wants to Buy “Golden Share” in EADS</i> , Der Spiegel Online International (Aug. 6, 2007)
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