

EU/US Large Civil Aircraft WTO Disputes

Background fact sheet

(See also "Measures Affecting Trade in Large Civil Aircraft" : complaint from the EU ([DS 353](#)) and against the EU ([DS 316](#))).

There has been recent speculation in the press on the release of the confidential interim report of the US WTO challenge to EU support for Airbus. The timing and substance of panel procedures in WTO dispute cases is confidential. The EC therefore cannot confirm or comment on statements by third parties on the timing of the issuance of an interim report.

In addition to this dispute, it must be recalled that there is a separate, pending dispute brought by the EU challenging a broad range of WTO-incompatible US Federal, State and local subsidies benefiting Boeing, including benefits under the US Foreign Sales Corporation act which has repeatedly been found to violate WTO rules. Further background information on both cases is presented below.

The US WTO challenge to EU support for Airbus (DS316)

- Since 1992 direct and indirect government support to aircraft industry in the US and the EU has been regulated by the bilateral EU-US Agreement on Trade in Large Civil Aircraft. The EU in good faith has continuously met all commitments under this agreement whereas US compliance had been less than adequate, in particular by covering up large hidden subsidies to Boeing including unprecedented prohibited production subsidies in Washington State for the 787 and other Boeing commercial aircraft.
- Nevertheless, during the course of the Summer 2004 the United States purported to unilaterally withdraw from the bilateral 1992 Agreement (a move that the EU considers invalid as it did not respect the required conditions) and unexpectedly filed a WTO challenge of all EU support even though it had been granted in accordance with the Agreement.
- On 6 October 2004 the US requested formal WTO consultations with the EU regarding alleged subsidisation of Airbus by the EU and certain of its Member States, and a WTO panel was set up thereafter.
- The major bone of contention is that of EU Member State co-financing of R&D for new Airbus aircraft ("Member State Financing" or "reimbursable launch investment"). This form of support is expressly agreed under the bilateral EU-US Agreement and has been used on three of the nine Airbus aircraft launched since 1990. It provides for government funding to Airbus repaid with interest under terms specified in the Bilateral Agreement (loan rates of return are cost to government plus 1%, and interest and principal is repaid on deliveries, even

before the programs break-even). In some cases the terms are more onerous than those commercially available in that the lending governments are receiving royalty payments that will last through the life of a particular aircraft program even though the original loan and interest are completely repaid. In fact, EU governments so far have made handsome returns on their initial “investments”, even though there are instances where Airbus has been able to obtain financing on more favourable terms from private lenders, compared with government offers. Airbus has repaid in excess of 7 billion euros (USD 9 billion). Since 1992, Airbus has repaid 40 percent more than it has received from EU governments. Airbus currently repays loans at the rate of 300 to 400 million euros a year.

- The US also claims that a number of infrastructure projects were allegedly built or upgraded exclusively for Airbus, or that Airbus enjoyed preferential treatment. However, unlike infrastructure projects in the State of Washington (which were designed for Boeing and for which Boeing benefited from preferential treatment), Airbus pays a market-based rent and clearly did not benefit from any preferential treatment for these projects, or they were for the use of the general public.
- As regards research and technology support in the EU (be it at EU or EU Member State level), such activities are co-financed by the industry and receive no more than a 50 % maximum contribution from the EU or Member States, and the EU abides by the cap provided in the bilateral EU-US agreement for such support. The amounts budgeted by NASA and the Department of Defense for R&D support to Boeing's LCA business are estimated to be at least 10 times higher. And not a cent of it is repaid.
- The US also argues that Airbus benefited from preferential loans from the European Investment Bank (EIB). The EIB has indeed provided loans to Airbus but it has done so in full conformity with its lending rules and policy on conditions strictly similar to that of loans to other clients. For instance, the EIB has provided loans to European airlines for the purchase of Boeing aircraft, as well as to several other large US companies for investments in the EU.

The EU WTO challenge to US subsidies to Boeing (DS353)

- Following the United States' unjustified and unilateral withdrawal from the 1992 bilateral EU-US Agreement on Trade in Large Civil Aircraft and the initiation of WTO dispute settlement procedures against the EU, the EU for its part on 6 October 2004 decided to mirror the US steps by initiating WTO dispute settlement procedures regarding a number of US measures, including federal and state subsidies. A WTO panel was set up thereafter.
- In its WTO case against the US, the EU is challenging various US Federal, State and local subsidies benefiting Boeing, totalling USD 23.7 billion in WTO-inconsistent subsidies over the past two decades and up to 2024.
- At federal level, Boeing benefits from numerous types of R&D support provided by NASA and the Department of Defense (DOD). This support includes contracts for R&D work to be carried out by Boeing (ultimately benefiting Boeing's LCA division and Boeing's aircraft models), reimbursement of Boeing's own R&D expenses, extensive cooperation with NASA and DOD engineers at no cost to Boeing, and use of testing facilities and equipment, also at no cost to Boeing. This support is coupled with the transfer of patents and other vital knowledge to Boeing, and reinforced by stringent restrictions on the application and use of such knowledge by foreign competitors. The EU estimates the benefits of US federal research programs to Boeing at around USD 16.6 billion over the last two decades.
- At federal level Boeing also enjoys significant tax breaks under the Foreign Sales Corporation and successor legislation. That legislation has already been found to constitute prohibited export subsidies by multiple WTO panels and the WTO Appellate Body. The EU estimates these tax benefits at a value to Boeing's LCA division of USD 2.2 billion over the period 1989-2006.
- At the State and local level, illustrative examples of subsidies to Boeing include a USD 4 billion package in the State of Washington (combining tax breaks, tax exemptions or tax credits and infrastructure projects for the exclusive benefit of Boeing) and a USD 900 million package in the State of Kansas in the form of tax breaks and subsidised bonds, some of which are known as "Boeing Bonds". These will be enjoyed by Boeing until 2024.
- The EU will demonstrate before the WTO panel that the lavish subsidies benefiting Boeing has allowed Boeing to engage in aggressive pricing of its aircraft which has caused lost sales, lost market share and price suppression to Airbus on a number of select markets. It will also show that Boeing received illegal export subsidies: in addition to the Foreign Sales Corporation programme, the Washington State package was made contingent upon Boeing's export performance. Finally, the EU will also demonstrate that the US has caused serious prejudice to the EU's interests by violating the EU-US 1992 Agreement.

Details of the US subsidies to Boeing challenged by the EU

1. State and Local Subsidies

- a. State of Washington: incentive package of measures benefiting the development, production and sales of US LCA¹. These incentives include but are not limited to tax and other advantages
- b. State of Kansas: incentives, including bond financing, tax benefits and other advantages, to the US LCA industry.
- c. State of Illinois: incentives, including tax incentives, relocation assistance and other advantages, to the US LCA industry

2. NASA Subsidies

NASA transfers economic resources on terms more favourable than available on the market or not at arm's length to the US LCA industry, *inter alia*, by:

- a. allowing the US LCA industry to participate in research programmes, making payments to the US LCA industry under those programmes, or enabling the US LCA industry to exploit the results thereof by means including but not limited to the foregoing or waiving of valuable patent rights, the granting of limited exclusive rights data ("LERD") or otherwise exclusive or early access to data, trade secrets and other knowledge resulting from government funded research.
- b. providing the services of NASA employees, facilities, and equipment to support the R&D programmes listed above and paying salaries, personnel costs, and other institutional support, thereby providing valuable services to the US LCA industry on terms more favourable than available on the market or not at arm's length.
- c. providing NASA Independent Research & Development, and Bid & Proposal Reimbursements.
- d. allowing the US LCA industry to use the research, test and evaluation facilities owned by the US Government, including NASA wind tunnels, in particular the Langley Research Center.
- e. entering into procurement contracts with the US LCA industry for more than adequate remuneration.
- f. granting the US LCA industry exclusive or early access to data, trade secrets, and other knowledge resulting from government funded research.
- g. allowing the US LCA industry to exploit the results of government funded research, including, but not limited to, the foregoing or waiving of valuable patent rights or rights in data as such.

¹ Large Civil Aircraft(s)

3. Department of Defense Subsidies

The Department of Defense ("DOD") transfers economic resources to the US LCA industry on terms more favourable than available on the market or not at arm's length, *inter alia*, by:

- a. allowing the US LCA industry to participate in DOD-funded research, making payments to the US LCA industry for such research, or enabling the US LCA industry to exploit the results of such research, by means including but not limited to the foregoing or waiving of valuable patent rights, and the granting of exclusive or early access to data, trade secrets and other knowledge resulting from government funded research.
- b. allowing the US LCA industry to use research, test and evaluation facilities owned by the US Government, including the Major Range Test Facility Bases.
- c. entering into procurement contracts, including those for the purchase of goods, from the US LCA industry for more than adequate remuneration, including in particular but not limited to the US Air Force contract with Boeing for the purchase of certain spare parts for its Airborne Warning and Control System (AWACS) aircraft, the National Polar-orbiting Operational Environmental Satellite System-Conical Microwave Imager Sensor, the C-22 Replacement Program (C-40), the KC-135 Programmed Depot Maintenance, the C-40 Lease and Purchase Program, the C-130 avionics modernisation upgrade program, the C-17 H22 contract (Boeing BC-17X), the US Navy contract with Boeing for the production and maintenance of 108 civil B-737 and their conversion into long-range submarine hunter Multi-Mission Aircraft, the Missile Defense Agency's Airborne Laser (ABL) Program, and the Army's Comanche Program.
- d. by allowing the US LCA industry to exploit the results of government funded research, including, but not limited to, the foregoing or waiving of valuable patent rights or rights in data as such.

4. National Institute of Standards & Technology (US Department of Commerce) Subsidies

The US Department of Commerce ("DOC") transfers economic resources to the US LCA industry on terms more favourable than available on the market or not at arm's length, through the Advanced Technology Program operated pursuant to the Omnibus Trade and Competitiveness Act of 1988, as amended, and the American Technology Preeminence Act of 1991, by allowing the US LCA industry to participate in this programme, making payments to the US LCA industry under this programme, or allowing the US LCA industry to exploit the results of this programme, including but not limited to the foregoing or waiving of valuable patent rights, and the granting of exclusive or early access to data, trade secrets and other knowledge resulting from government funded research.

5. US Department of Labor

The US Department of Labor transfers economic resources to the US LCA industry on terms more favourable than available on the market or not at arm's length, through the Aerospace Industry Initiative, an element of the President's High Growth Training Initiative, under the authority of the Workforce Investment Act, by granting to Edmonds Community College in the State of Washington funds for the training of aerospace industry workers associated with the Boeing 787.

6. Federal tax incentives

The US Government transfers economic resources to the US LCA industry through the federal tax system, and in particular through the following tax measures:

- a. Sections 921-927 of the Internal Revenue Code (prior to repeal) and related measures establishing special tax treatment for "Foreign Sales Corporations" ("FSCs");
- b. FSC Repeal and Extraterritorial Income Exclusion Act of 2000; and
- c. American Jobs Creation Act of 2004.

SUPPORT TO AIRBUS AND BOEING: SEPARATING THE MYTHS FROM THE FACTS

What is launch investment?

“Launch aid” is a term sometimes used by the US as a misnomer for royalty based financing granted by certain EC Member States in individual circumstances to a number of companies, including Airbus. Since its creation in 1970, some Airbus aircraft development programmes have been financed in part by royalty based financing, otherwise known as “launch investment”. This kind of finance works in the same way as commercial investments.

The US itself has agreed with the EC in a 1992 international agreement² that Airbus may receive such financing within specific and detailed limits. As laid down in the Agreement,

- Member State governments advance money to Airbus up to the limit agreed with the US, namely 33% of the total development costs of a new aircraft model.
- This advance is then repaid by means of a levy on the sale of each aircraft.
- The levy is set so that, once an agreed sales target is reached, the whole amount should be repaid with a rate of return, i.e. with interest, over a repayment period of 17 years (i.e. 11-12 years from the first delivery).
- The sales target is based on a conservative forecast of future sales, which is established when the investment is made.
- The interest rate reflects the investing government’s objective to earn a good return on its money. It is always in excess of the government’s borrowing rate (i.e. typically 6-8% nominal) and may be considerably higher, depending, for instance, on the anticipated commercial success of the project and on the Member State (Some Member States insist on a higher return).
- Once the actual sales exceed the target, as has happened, investing governments continue to collect “royalties” or “upside” on the additional sales, which will further increase their rate of return.

Airbus has paid significant amounts of royalties to the Member States which exceed by far the Member States’ investments since 1992. Therefore, this instrument is characterised by “*success-sharing*” (i.e. extra profit for the investing government) rather than a certain element of risk inherent in any kind of investment (in the present case insofar as payback is linked to the actual sale of aircraft).

None of the individual launch investments granted by the Member States since 1992 has ever exceeded the limits, terms and conditions to which the US government agreed.

² 1992 EU-US Agreement on Trade in Large Civil Aircraft.

If launch aid is such a good investment, why don't other countries do it?

They do. Launch investment schemes are in fact, a widely-used form of financing the development, and outside Europe, also the production, of civil aircraft. They are used, for instance, in Canada and Japan.

In fact, Boeing benefits from a Japanese scheme for development and production of Boeing's 787 aircraft, which competes with the Airbus A350. In effect, 35% of the B787 will be produced in Japan and it is understood that Boeing's risk-sharing partners have received financing from the Japanese government of up to 70% of development costs (the ceiling in the EU is 33%). And this is on top of the other forms of support Boeing receives.

The example of Japan demonstrates that even if the Airbus-Boeing dispute is presented as a US jobs issue, Boeing increasingly outsources its R & D projects to non-US firms, and therefore non-US workers, while continuing to receive US government support. The opposite is true for Airbus which imports more and more jobs into the US, but does not benefit from US government funding.

It is also noteworthy that Boeing itself sought royalty-based launch investment from the US government in the 1970's. However, Boeing is significantly better off under the current system since the company benefits from subsidies (e.g. \$3.2 billion tax subsidies by the State of Washington for the B787 alone) which do not have to be repaid.

How much launch investment has Airbus received?

Since 1992, the Member States concerned have granted royalty based financing subject to the strict limits agreed with the US in the 1992 EC-US agreement.

Since then, Member States have committed a total of €3.7 billion in launch investment to Airbus. Of the Airbus programmes since 1992 the A330-200 and the A340-500/600 and the A380 received launch investment. The A318 was developed without launch investment.

How much launch investment has Airbus repaid?

Since 1992, Airbus has repaid to the Member States concerned around €6 billion, or €9 billion (\$12 billion) in real present value. This means that since 1992, Airbus has repaid over 40 percent more than it has received from EU governments.

Airbus currently repays €300-400 million per year. Principal and interest of launch investment to Airbus have been and continue to be re-paid on the delivery of each aircraft, along with royalty payments thereafter.

How is Boeing supported if it does not receive launch investment from the US government?

Boeing receives different forms of support from the US federal and state governments that benefit the development, production and sales of its civil aircraft. Taken together (e.g. tax breaks, R&D and infrastructure support), US support has consistently exceeded the limit allowed under the EU-US Agreement of 1992 by 2 to 3 times. These sums have not been reimbursed.

Does Boeing receive R&D support?

Boeing relies on the R&D subsidies it receives from a variety of quarters.

In the US, Boeing receives subsidies from NASA's and Department of Defense programmes and contracts (estimated at being at least \$22 billion), as well as the Department of Commerce and the Department of Labor, e.g. by providing funds for specific research into composite technology from which the 787 airframe will be constructed and sophisticated software tools that Boeing will use for 787 design and manufacture. Civil R&D support in the EU is granted in the form of generally available programmes (e.g. the EU R&D Framework Programme) in which a large number of companies participate, including Boeing.

Surely, the subsidies Boeing receives benefit only its military or space business?

No. So-called "military" and "space" subsidies provide considerable benefits for Boeing's civil aircraft business. Department of Defence and NASA subsidies have helped Boeing develop technologies (e.g. composites) which the company uses in its civil planes. Boeing uses DoD centres and testing facilities to work on the design and wings of its civil planes. E.g. these subsidies have enabled Boeing to develop the technologies used in its 787 and other civil aircraft, but are not available to Airbus. This reduces, and effectively subsidises, Boeing's production costs and puts Airbus at a competitive disadvantage.

Another issue are non-competitive "military" contracts at inflated prices which benefit Boeing's civil aircraft business. The situation is therefore problematic: Boeing receives a number of benefits courtesy of US government programmes, its non-competitive military contracts, awarded at inflated prices by the US government, benefits which are passed on to its civil airplane production. In other words, R&D for Boeing's civil airplanes is effectively being paid for from US military budgets, rather than Boeing's own pocket.