

*United States – Measures Affecting Trade in Large Civil Aircraft  
(Second Complaint)*

**(AB-2011-3/DS353)**

**Opening Statement of Australia**  
**Second Session of the Oral Hearing**

**Geneva, 11 October 2011**

Members of the Division,

1. Thank you for the opportunity to present the views of Australia with respect to the adverse effects issues raised by this appeal.
2. Australia will not comment on every issue raised by the Participants. Rather, we will focus on two issues of systemic importance to adjudicating claims under Articles 5 and 6.3 of the *Agreement on Subsidies and Countervailing Measures* (the SCM Agreement). The first issue concerns the requirements for determining that a subsidy caused adverse effects, and the United States' argument that the Panel was required to consider (as part of its counterfactual analysis) whether Boeing would have funded the research performed under the aeronautics R&D subsidies, had those subsidies not been granted. The second issue concerns the circumstances in which it is appropriate to aggregate the effects of subsidies, and the European Union's argument that the Panel erred in declining to assess the cumulative effects of the groups of subsidies at issue in this dispute.

*Determining that a subsidy has caused adverse effects*

3. The Panel found that the aeronautics R&D subsidies caused adverse effects to the European Union through enabling Boeing to launch the 787 as and when it did.<sup>1</sup> This finding was based on the Panel's determination that the aeronautics R&D subsidies, through their structure, design and operation, "contributed in a genuine and substantial way to Boeing's development of technologies for the 787".<sup>2</sup> The Panel determined that, "absent the aeronautics R&D subsidies, Boeing would not have been able to launch an aircraft incorporating all of the technologies that are incorporated on the 787 in 2004, with promised deliveries commencing in 2008."<sup>3</sup> The Panel consequently found that the alleged market phenomena – that is, the significant price suppression, significant lost sales and threat of displacement and impedance of exports from third

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<sup>1</sup> Panel Report, paragraph 7.1775.

<sup>2</sup> Ibid, paragraph 7.1773.

<sup>3</sup> Ibid, paragraph 7.1775.

country markets with respect to the 200-300 seat wide-body LCA product market – were the effect of the aeronautics R&D subsidies, because these market phenomena were attributable to the introduction of the 787 in 2004 (which would not have occurred without the aeronautics R&D subsidies).<sup>4</sup>

4. The United States argues that the Panel erred in reaching this finding because it did not conduct a proper counterfactual analysis that took account of the fact that “Boeing had sufficient funds to achieve the same learning and experience provided by the government’s aeronautics R&D expenditure at issue”.<sup>5</sup> The United States argues that a “proper counterfactual” would have considered that, “in the absence of subsidies, Boeing would have funded this ‘critical’ research itself”; and this “establishes that the aeronautics R&D subsidies are not a genuine and substantial cause of adverse effects”.<sup>6</sup>
5. Australia has two key concerns with this argument. First, it detracts from the proper focus of adjudicating claims under Articles 5 and 6.3 of the SCM Agreement, which is on whether or not a subsidy has caused adverse effects to the interests of another Member.<sup>7</sup> Second, it misconstrues the proper role and scope of a counterfactual analysis.
6. In relation to Australia’s first concern, the implication of the United States’ argument is that a subsidy cannot be found to have caused adverse effects where some other (hypothetical) factor could have happened had the subsidy not been granted, and could have had the same effect as that subsidy. Australia notes that Articles 5 and 6.3 of the SCM Agreement do not require a complaining Member to establish that, had the subsidy not been granted, there were no alternative ways in which the same market phenomenon could possibly have arisen.

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<sup>4</sup> Panel Report, paragraph 7.1780 and 7.1854.

<sup>5</sup> *Other Appellant Submission of the United States*, paragraph 268.

<sup>6</sup> *Ibid*, paragraph 270.

<sup>7</sup> See Article 5 of the *Agreement on Subsidies and Countervailing Measures*.

7. Further, while evaluating the effects of other *actual* factors may attenuate the causal link between the subsidy and the alleged market phenomena, speculating about the effect a *hypothetical* factor may have had in the place of the subsidy does not assist in determining whether or not the challenged subsidy did in fact cause adverse effects (which is the proper focus of an adverse effects analysis).
8. Therefore, in Australia’s view: (i) it is irrelevant for a responding Member to speculate that, had the subsidy not been granted, alternative sources of funding could have given rise to the same effects as the challenged subsidy; and (ii) it is incorrect to conclude that this possibility displaces a finding that the subsidy in fact caused the alleged market phenomena.
9. Australia’s second concern with the United States’ argument is twofold. First, as we will explain, it misconstrues the proper *role* of a counterfactual analysis, which is to determine the effect of the subsidy on the market. Second, it misconstrues the *scope* of a counterfactual analysis by introducing additional hypothetical factors (other than the assumption that the challenged subsidy was not paid).
10. The Appellate Body’s previous guidance establishes that: a counterfactual analysis is undertaken “to isolate and properly identify the effects” of a subsidy;<sup>8</sup> and “entails comparing the actual market situation that is before the adjudicator with the market situation that would have existed in the absence of the challenged subsidies”.<sup>9</sup> This enables a panel ultimately to determine whether or not a subsidy caused the market phenomena alleged.
11. Australia observes that, in establishing adverse effects claims under Articles 5 and 6.3 of the SCM Agreement, there will likely be links in the causal chain between the grant of the subsidy at issue and the particular market phenomena alleged – that is, the grant

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<sup>8</sup> *European Communities – Measures Affecting Trade in Large Civil Aircraft* (Appellate Body), paragraph 1110.

<sup>9</sup> *Ibid.*

of a subsidy may cause the particular market phenomena *through* a particular effect or mechanism,<sup>10</sup> rather than *directly* giving rise to the alleged market phenomena.

12. Therefore, the causation analysis required to determine whether or not a subsidy causes adverse effects involves a number of discrete analytical steps. In Australia's view, a panel must *first* determine the effect that a subsidy has had, through considering the nature of the subsidy (its structure, design and operation), taking care not to attribute to the subsidy the effects of other factors. A panel can *then* undertake a counterfactual analysis to examine the effect of that subsidy on the market – this involves determining what the market would have looked like absent the subsidy (or, more precisely, absent the effect of the subsidy) and comparing this with the actual market situation before the panel. Together, these analytical steps allow a panel *ultimately* to determine whether or not the alleged market phenomena are caused by, or are the result of, the subsidy – in other words, these collective steps establish whether or not there is “a genuine relationship of cause and effect between the subsidy and the alleged market phenomena”.<sup>11</sup>

13. In Australia's view, the United States' argument that a “proper counterfactual” would have established that the aeronautics R&D subsidies did not cause adverse effects (because Boeing could have funded the relevant research itself)<sup>12</sup> improperly suggests that the Panel was required to conduct a counterfactual analysis to determine the effect that the subsidies had – that is, to determine whether or not the subsidies contributed to Boeing's ability to develop and launch the 787 as and when it did. However, this was the Panel's *first* analytical step. The Panel concluded that, due to their structure, design and operation, the aeronautics R&D subsidies “contributed in a genuine and substantial way to Boeing's development of technologies for the 787”.<sup>13</sup> In

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<sup>10</sup> Panel Report, paragraph 7.1596.

<sup>11</sup> *US – Subsidies on Upland Cotton* (Appellate Body), paragraph 438; *US – Subsidies on Upland Cotton (Recourse to Article 21.5 of the DSU by Brazil)* (Appellate Body), paragraph 374; *European Communities – Measures Affecting Trade in Large Civil Aircraft* (Appellate Body); paragraph 1231.

<sup>12</sup> *Other Appellant Submission of the United States*,

<sup>13</sup> Panel Report, paragraph 7.1773. Australia does not express a view on whether this conclusion is sufficiently supported by the facts on the record.

Australia's view, a counterfactual analysis has no role to play in this step of the causation analysis.

14. Rather, in Australia's view, the proper role of a counterfactual analysis is to determine what the market would have looked like absent the subsidy. Therefore, in this case, the proper role of a counterfactual was to determine what the market would have looked like absent the aeronautics R&D subsidies (and, consequently, absent Boeing's ability to launch the 787 as and when it did, which the Panel had attributed to the effect of the subsidies) – not whether “in the absence of subsidies, Boeing would have funded this ‘critical’ research itself”.<sup>14</sup>
15. Australia further considers that the United States' argument misconstrues the *scope* of a counterfactual analysis. In Australia's view, the only relevant hypothetical factor in a counterfactual analysis is the assumption that the subsidy was not granted. The consideration of hypothetical factors *other* than this undermines the purpose of the counterfactual analysis, because taking account of additional variables does not “isolate and properly identify” the effects of the challenged subsidy.<sup>15</sup> Rather, in order for a counterfactual analysis to properly assess the effects of a subsidy, a panel should examine what the market would have looked like had the subsidy not been granted *holding all else equal*.
16. Australia therefore considers that, even if the proper *role* of a counterfactual analysis were to determine whether “in the absence of subsidies, Boeing would have funded this ‘critical’ research itself”,<sup>16</sup> examining whether alternative sources of funding could, hypothetically, have taken the place of those subsidies is beyond the proper *scope* of such an analysis.

#### Aggregating the effects of subsidies

17. We now turn to the issue of aggregating the effects of challenged subsidies.

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<sup>14</sup> *Other Appellant Submission of the United States*, paragraph 270.

<sup>15</sup> *European Communities – Measures Affecting Trade in Large Civil Aircraft* (Appellate Body), paragraph 1110.

<sup>16</sup> *Other Appellant Submission of the United States*, paragraph 270.

18. In Australia's view, there are two key questions directly before the Appellate Body.

First, whether or not it is permissible to aggregate the effects of subsidies with a sufficient nexus with the same subsidised product and the same market phenomena alleged under Article 6.3 of the SCM Agreement, even where such subsidies operate through different "causal mechanisms".<sup>17</sup> Second, whether or not a panel is required to aggregate the effects of subsidies where the conditions for aggregation are met.

19. In relation to the first question, Australia recalls the approach taken in *United States – Subsidies on Upland Cotton* (which we will subsequently refer to as *Cotton*). The panel found that the reference in Article 6.3(c) to "the effect of the subsidy" (singular) did not mean that "a serious prejudice analysis of price suppression must clinically isolate each individual subsidy and its effects".<sup>18</sup> The panel noted that, if such an approach were "[t]aken to an extreme, this could mean that separate dispute settlement proceedings, or at least separate claims, would need to be brought with respect to the serious prejudice caused by each and every individual subsidy, even where these subsidies exist contemporaneously and interact in concert in respect of a single subsidized product to produce a single result in the form of a price phenomenon".<sup>19</sup>

20. Instead, the panel in *Cotton* determined that it was legitimate to conduct "an integrated examination of effects of any subsidies with a sufficient nexus with the subsidised product and the particular effects-related variable under consideration".<sup>20</sup> It found that "in our price suppression analysis under Article 6.3(c), we examine one effects-related variable – prices – and one subsidized product – upland cotton. To the extent that a sufficient nexus with these exists among the subsidies at issue so that their effects manifest themselves collectively, we believe that we may legitimately treat them as a 'subsidy' and group them and their effects together".<sup>21</sup>

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<sup>17</sup> Panel Report, paragraph 7.1805.

<sup>18</sup> *United States – Subsidies on Upland Cotton* (Panel), paragraph 7.1192.

<sup>19</sup> *Ibid*, footnote 1307.

<sup>20</sup> *Ibid*, paragraph 7.1192.

<sup>21</sup> *Ibid*, paragraph 7.1192.

21. The Panel in the present dispute referred to this approach in *Cotton*,<sup>22</sup> and appears to have interpreted this to mean that “in order to conduct an aggregated analysis of the effects of subsidies in the context of this dispute, it should be possible to discern from their structure, design and operation that they affect Boeing’s behaviour in a similar way”.<sup>23</sup> The Panel therefore declined to aggregate the effects of the B&O tax subsidies on Boeing’s pricing of the 787 with the effects of the aeronautics R&D subsidies, on the basis that “the two groups of subsidies operate through entirely distinct causal mechanisms”.<sup>24</sup>
22. In Australia’s view, this approach is incorrect. In *Cotton*, the panel’s analytical focus on the particular “effects-related variable” (that of price) stemmed from its implicit assumption that *only* measures with a sufficient nexus with price could cause price suppression (the particular market phenomenon at issue). The Appellate Body rightly questioned this in its review of the panel’s decision, noting that “[w]e do not exclude the possibility that challenged subsidies that are not ‘price-contingent’ ... could have some effect on production and exports and contribute to price suppression”.<sup>25</sup> When viewed within the context of the panel’s erroneous assumption, the panel’s references to the ‘effects-related variable’ essentially serve as a proxy for the particular market phenomenon at issue – that is, if only price-contingent subsidies could cause price suppression, then it follows that only the effects of measures with a sufficient nexus with *price* could be aggregated for the purposes of a price suppression analysis.
23. In this way, the panel in *Cotton* did not find that it could not aggregate the effects of the price-contingent subsidies and the non-price contingent subsidies because they operated through different ‘causal mechanisms’. Rather, the panel was not satisfied that the non-price contingent subsidies had a sufficient nexus with the particular market phenomenon at issue (price suppression). As the panel expressly stated, it declined to aggregate the effects of the two groups of subsidies because, in its view,

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<sup>22</sup> Panel Report, paragraph 7.1804.

<sup>23</sup> Ibid, paragraph 7.1805.

<sup>24</sup> Panel Report, paragraph 7.1824.

<sup>25</sup> *United States – Subsidies on Upland Cotton* (Appellate Body), paragraph 450, footnote 589.



Brazil had “not established that...significant price suppression...was ‘the effect’ of these non-price contingent subsidies”.<sup>26</sup>

24. However, as the panel itself acknowledged, its approach was “tailored to the particular facts and circumstances of this dispute and of the measures before [it]”.<sup>27</sup> Further, the panel had indicated that it considered that aggregating the effects of subsidies would be appropriate “where these subsidies exist contemporaneously and interact in concert in respect of a single subsidized product to produce a single result in the form of a price phenomenon.”<sup>28</sup>

25. Australia recalls that the Appellate Body’s recent finding in *European Communities – Measures Affecting Trade in Large Civil Aircraft* further supports the view that a panel may assess the cumulative effects of two groups of subsidies where both subsidies have a sufficient nexus with the same subsidised product and the same alleged market phenomena (regardless of whether both subsidies operate through the same ‘causal mechanism’).<sup>29</sup>

26. In that case, the Appellate Body found that, “[o]nce the Panel determined that LA/MSF subsidies were a substantial cause of the observed displacement and lost sales, it was not necessary to establish that non-LA/MSF subsidies were also substantial causes of the same phenomena”.<sup>30</sup> Rather, “it was permissible and sufficient for the Panel to assess whether a genuine causal connection between non-LA/MSF subsidies and the same market phenomena existed such that these non-LA/MSF subsidies complemented or supplemented the effects of LA/MSF”.<sup>31</sup> A cumulative assessment of the relevant subsidies was permitted “provided that a genuine causal link between the non-LA/MSF subsidies and the market phenomena

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<sup>26</sup> *United States – Subsidies on Upland Cotton* (Panel), paragraph 7.1350.

<sup>27</sup> *Ibid.*, paragraph 7.1192, footnote 1308.

<sup>28</sup> *United States – Subsidies on Upland Cotton* (Panel), paragraph 7.1192, footnote 1307.

<sup>29</sup> *European Communities – Measures Affecting Trade in Large Civil Aircraft* (Appellate Body), paragraph 1378. However, Australia notes that the Appellate Body stated (in paragraph 1374) that it did not consider that the panel had *aggregated* the effects of the subsidies in assessing whether the effects of one group of subsidies “complemented and supplemented” the effects of other subsidies.

<sup>30</sup> *Ibid.*

<sup>31</sup> *Ibid.*

alleged under Article 6.3 is established”.<sup>32</sup> In other words, if multiple subsidies cause the same market phenomena, a cumulative assessment of their effects is permitted.

27. Australia therefore agrees with the European Union that the Panel did not need to find that the B&O tax subsidies would “on their own” have such an effect on Boeing’s prices of the 787 as to cause significant price suppression, significant lost sales and threat of displacement and impedance of exports from third country markets, with respect to the 200-300 seat wide-body product market.<sup>33</sup> Rather, the Panel could have considered whether the B&O tax subsidies “complemented or supplemented” the effects of the aeronautics R&D subsidies (which it had already found caused these market phenomena in respect of that product market).<sup>34</sup> The fact that the two groups of subsidies operated through “distinct causal mechanisms” was irrelevant to the Panel’s analysis.<sup>35</sup>

28. For the same reasons, Australia also agrees with the European Union that it would have been permissible for the Panel to have assessed whether there was a genuine causal link between the Remaining Subsidies and significant price suppression, significant lost sales, and displacement and impedance of exports in third country markets, such that the effects of the Remaining Subsidies “complemented or supplemented” the effects of the Tax Subsidies with respect to the 100-200 seat single aisle product market and the 300-400 seat wide-body product market.

29. In relation to the second key question before the Appellate Body – whether a panel is required to aggregate the effects of subsidies – Australia notes that previous panels have described their authority to aggregate the effects of subsidies in *permissive* language.<sup>36</sup> Similarly, the Appellate Body has previously described a panel’s authority to consider whether the effect of one group of subsidies “complemented or

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<sup>32</sup> Ibid.

<sup>33</sup> Panel Report, paragraph 7.1824.

<sup>34</sup> Ibid, paragraph 7.1794.

<sup>35</sup> Ibid, paragraph 7.1824.

<sup>36</sup> For example, *US – Subsidies on Upland Cotton* (Panel), paragraph 7.1192.

supplemented” the effects of another group of subsidies in *permissive* language.<sup>37</sup>

This suggests that it is within a panel’s discretion to determine on a case-specific basis whether the effects of different subsidies should be aggregated.

30. However, Australia notes that these previous ‘permissive’ descriptions were made in the context of a panel’s decision *to* aggregate the effects of different subsidies. Given that a panel’s decision to *decline* to aggregate the effects of different subsidies could have significant consequences for a complaining Member’s adverse effects claim, and could lead to a continuation of measures that may ‘complement or supplement’ the adverse effects claimed, Australia would welcome the Appellate Body’s guidance as to whether or not a panel is required to aggregate the effects of subsidies that it finds have a sufficient nexus with the same subsidised product and the same alleged market phenomena.

31. Finally, we would like to note that although Australia’s written submission and this statement do not address every issue raised by the European Union, the United States, and the other Third Participants, this should not be regarded as an indication that Australia considers that the issues it has not addressed are not important. Nor does it indicate agreement or otherwise with any particular argument of the Participants or other Third Participants in these appellate proceedings.

32. Thank you.

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<sup>37</sup> *European Communities – Measures Affecting Trade in Large Civil Aircraft* (Appellate Body), paragraph 1378.