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The Production of Civil Aircraft: A Compromise of Two World Giants

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The European Community and the United States represent the two largest economic trading blocs in the world. Over the past decade, the trading balance between the two parties has been relatively even.¹ One area of trade which threatens this balance is the production and sale of civil aircraft.

Aircraft represent the largest exporting industry in the United States,² and Aircraft production affects nearly 80% of the U.S. economy.³ This sector of the trade relationship between the U.S. and the EC is critical. The amount of capital transferred in a single aircraft sale can have an immediate and profound impact on the entire monthly trade balance between these two trading partners.⁴ Since most of the current world market for civil aircraft is located within the United States and the European Community, international regulation of this trade is both politically and economically sensitive. Any domination of the aircraft market would profoundly upset the current balance of trade between them.

The United States, not particularly concerned with regulation in this area for a long time, has changed its course in large part because its once dominant position in the market has evaporated. Indeed, the United States once held as high as 90% of the world production in this area.⁵

1. U.S. BUREAU OF THE CENSUS, STATISTICAL ABSTRACT OF THE UNITED STATES (1991) (Table No. 1408-09).

2. OFFICE OF TECHNOLOGY ASSESSMENT, U.S. CONGRESS, COMPETING ECONOMICS: AMERICA, EUROPE AND THE PACIFIC RIM 345 (1991). The U.S. trade surplus in transport aircraft (excluding spare parts) was \$35 billion from 1985-1989. While commercial transports represented only .3% of the U.S. gross national product (GNP) in 1989, they accounted for 3.4% of the value of merchandise exports. *Id.* The aerospace industry exported \$39.6 billion worth of goods in 1991. *U.S., EC Sign Agreement Restricting Subsidies to Civil Aircraft Industry*, 9 Int'l Trade Rep. (BNA) No. 30, at 1243 (July 22, 1992).

3. David Cantor, *Aircraft Production and the U.S. Economy*, in HOUSE SUBCOMM. ON TECHNOLOGY AND TRADE, 102D CONG., 2D SESS., AIRBUS INDUSTRIE: AN ECONOMIC AND TRADE PERSPECTIVE 45, 45 (Comm. Print 1992).

4. For example, each time one Boeing 747 airplane is shipped to a major trading partner, the trade balance shifts \$150 million in the U.S.'s favor. Robert Wrubel, *The Last Titan*, FIN. WORLD, Dec. 8, 1992, at 54. See also Robert E. Dallos, *Airbus Soars as U.S. Grumbles*, L.A. TIMES, June 22, 1991, at D1 ("[T]he sale of even one plane can have an impact on monthly trade balance figures.").

5. U.S. DEPARTMENT OF COMMERCE, A COMPETITIVE ANALYSIS OF THE U.S. CIVIL AIRCRAFT INDUSTRY 38 (1986) (Table 10).

Today, U.S. market share is sharply lower principally because of Airbus, which now accounts for at least 30% of all worldwide sales of civil aircraft.

In July, 1992, the European Community and the United States signed a bilateral treaty outlining narrower rules on the trade of large civil aircraft.⁶ This new agreement raises hopes that rules for a level playing field have finally been agreed to in this area. However, there is room for skepticism, since other instruments that attempted many of these same objectives have generally failed to make a strong impact on the practices of the industry.

Will the same result occur with this agreement? Part One of this article identifies the primary complaints pressed by each party over the past decade and the historical justifications for their positions. Traditionally, the U.S. has cried foul at the European Community's direct subsidization of Airbus and the commitment of Airbus' partner governments for funds in research, production, and export assistance. Additionally, the U.S. points to the use of loans, loan guarantees, equity infusions, tax breaks, debt forgiveness, marketing assistance, and bail outs. The European Community has responded to these allegations by identifying the longstanding policy of the U.S. to assist its aerospace industry with large government procurements for aerospace research and development. The EC also notes some examples of U.S. government bail outs, tax concessions, and tariffs.

Part Two examines the legal instruments which apply in this area of trade. Notions of the overall GATT approach to trade are important. The GATT itself has addressed the issue of subsidies with a multilateral agreement on subsidies and a supplemental agreement regulating the production and sale of civil aircraft. Pertinent domestic U.S. and European Community laws are summarized as well.

Part Three introduces the reader to the most recent agreement regarding civil aircraft trade between the parties, and offers supplementary analysis comparing the treaty to former efforts. It also details the need for multilateral agreements, identifies the future competitive threats of other nations, and delineates the hurdles to implementing the latest bilateral treaty to a multilateral forum.

Part Four summarizes the approach the Clinton administration has taken toward the bilateral Agreement. It identifies the U.S. use of legal

6. Agreement Concerning Application of the General Agreement on Tariffs and Trade to Trade in Civil Aircraft, Signed by the European Economic Community and United States July 17, 1992, 9 Int'l Trade Rep. (BNA) No. 30, at 1273 (July 24, 1992) [hereinafter Agreement] (At time of submission for publication, no official source citation was available).

mechanisms contained in the treaty and highlights the early tensions between the two sides on the enforcement of the bilateral Agreement.

I. U.S. AND EC COMPLAINTS REGARDING THE TRADE OF CIVIL AIRCRAFT

A. THE U.S. COMPLAINT

The U.S. has complained that the Airbus Industrie, a European consortium of four companies,⁷ has an unfair advantage in the trade of civil aircraft. Airbus was founded in 1967 as a consortium of the French, British, and German governments. Its goal was to develop and sell a wide-bodied aircraft, with a large seating capacity, for medium range flights. By acting together, the European governments were able to share capital financing and research and development costs, while dispersing the risks associated with a new company.

Initially, the United States did not see this collaboration as a serious threat to its stronghold in the industry. The earlier European collaboration on the supersonic transport (SST) project appeared to be an economic disaster, with no real possibility of profitability. More importantly, the SST project affected a very limited sales market of highly specialized routes. While the new European collaboration concentrated on a broader market base, providing a more quiet and fuel efficient plane, with a large load capacity, for short, popular routes; the U.S. did not take the threat seriously.⁸ Indeed, even the European airlines did not take the project seriously, despite the company's plan to bolster aircraft production in Europe.⁹ Despite this global pessimism, a new global competitor emerged for U.S. manufacturers.

The heart of the present controversy rests with the purpose of the Airbus consortium. Airbus was designed to further political goals rather than create profit.¹⁰ As was shown in the Concorde experience, the EC was willing to commit large sums without an economic return to achieve greater political goals. The survival of Airbus meant positive political re-

7. Today, Airbus Industrie is a consortium of Aerospatiale (37.9%), Deutsche Airbus (now owned by Daimler Benz) (37.9%), British Aerospace (20%), and CASA of Spain (4.2%). It is formed under French law as a Groupement d'Interet Economique (GIE), which allows for such cooperation, along with other favorable organizational and tax standing. OFFICE OF TECHNOLOGY ASSESSMENT, *supra* note 2, at 353.

8. BILL GUNSTON, AIRBUS, 10 (1988).

9. *Id.*

10. As the Office of Technology Assessment notes:

European planners value aircraft manufacture explicitly for the employment it creates. An Airbus official explained that the main reason the collaboration works is that by creating jobs in an export industry, Airbus enables the member countries to capture jobs from other parts of the world . . . With government commitment to full employment, policymakers view the thousands of jobs Airbus creates in England, France, Germany, and other European countries as well worth the costs of the supports provided.

OFFICE OF TECHNOLOGY ASSESSMENT, *supra* note 2, at 352.

turns in such areas as balance of payments, technological spin-off, and employment.¹¹ As a result of these motivations, public money allowed the European manufacturer to stay in business when American companies would have been forced to "cut their losses" and dissolve in a similar situation, giving Europe an unfair advantage.¹²

The U.S. aerospace industry has, therefore, objected to the significant advantage the Europeans have had in selling aircraft, due to the willingness of the Airbus' government sponsors to commit large sums of money for research, production, and export assistance. Direct financial support has taken the form of government contracts for the development of commercial models, loans and loan guarantees covering both development and production costs, guarantees against losses caused by exchange rate fluctuations, equity infusions, tax breaks, debt forgiveness, and bailouts.¹³

This direct support provides several clear advantages over the commercial lending used by U.S. companies to finance their projects. First, government financing allows Airbus to move more rapidly in getting new models to the market quickly, even where the cash flow from previous models is insufficient to convince a commercial lender to provide financing.¹⁴ Timing is essential in this industry. Since initial entry into a new market may deter others from entering, thus establishing a monopoly position.¹⁵ Second, the interest rates that the consortium governments charge for development and production loans are much lower than commercial rates, multiplying the effect of such financing.¹⁶ Third, the consortium partners offer low financing rates to buyers of aircraft, creating

11. KEITH HAYWARD, *INTERNATIONAL COLLABORATION IN CIVIL AEROSPACE*, 162 (1986).

12. *Id.* Other examples of Airbus survival where a U.S. firm would otherwise fail include: (1) Airbus survived its first five years with only ten orders and (2) Airbus built \$1.25 billion worth of unsold planes for inventory during recession. Neither practice could be financed by a U.S. company. U.S. CIVIL AVIATION MFG. INDUS. PANEL, COMM. ON TECHNOLOGY AND INT'L ECON. AND TRADE ISSUES, *THE COMPETITIVE STATUS OF THE U.S. CIVIL AVIATION MANUFACTURING INDUSTRY* 44-5 (1985).

13. OFFICE OF TECHNOLOGY ASSESSMENT, *supra* note 2, at 353.

14. *Id.* at 354.

15. Note that Boeing reaped tremendous rewards from the 747 in large part because no other manufacturer has produced a competing product for the past 20 years. The early launch of the Airbus A320 deterred other manufacturers from directly competing. The launch of the Airbus A300 eight years before Boeing could develop a similar craft is considered a principle reason for Airbus' initial success. *Id.* at 354 & n.66.

16. One writer notes:

A recent study by the U.S. Commerce Department says the companies that make up the Airbus consortium have been subsidized by their respective governments to the tune of \$13 billion since Airbus' founding. If commercial interest rates were applied, the value of such support would be \$25 billion.

Dallos, *supra* note 4, at D1.

artificially low prices.¹⁷

Finally, direct support has not been limited to financing. European governments have also influenced the procurement decisions of their nationalized airlines¹⁸ and have even granted foreign policy concessions in efforts to guarantee continued Airbus sales.¹⁹ Since the aircraft industry is one of traditionally cyclical demand, political influence has allowed Airbus to weather bad economic times when pure market forces may have dictated otherwise.

B. THE EUROPEAN COMMUNITY RESPONSE AND COMPLAINT

To understand the European Community's response to U.S. concerns and its complaint against U.S. practices, one must first acknowledge the differences between American and European market philosophies. The European business culture is radically different in terms of its attitude toward state-subsidization of industry. Unlike the U.S., many European nations have traditionally used subsidies as a key component in their industrial policies.²⁰ Most European subsidization takes the form of direct relief, largely in the form of direct grants and tax concessions.²¹

The European Community argues that the figures used by the U.S.

17. Stephen S. Cohen & John Zysman, *The Mercantilist Challenge to the Liberal International Trade Order*, 1 INT'L TAX & BUS. LAW. 1, 17 (1983). Indeed, financing can create purchases that otherwise would not occur. For example, a 2% advantage on financing terms will outweigh over a 5% advantage in fuel efficiency. *Id.* at 36.

18. Examples of government intervention in procurement decisions include:

1. French government successfully forcing Air France to buy General Electric engines instead of Pratt & Whitney engines for the A310 because of GE's close ties to French engine maker SNECMA,
2. Air France's and Lufthansa's current position as having only Airbus planes where Airbus and U.S. makers compete,
3. British Airways' current fleet uses only Rolls-Royce engines,
4. Key timing of launch orders from European carriers which has allowed the maker to continue production when new models may not otherwise have been launched.

OFFICE OF TECHNOLOGY ASSESSMENT, *supra* note 2, at 354.

19. An excellent example of this interplay occurred when the Australian government announced that a condition of its purchases of Airbusses would be French government backing of increases of access for Australian sheep within the European Community. Cohen & Zysman, *supra* note 17, at 35.

20. In the mid-1980s, total aid to industry amounted to 4.0% of industrial output (GNP) while similar aid the U.S. amounted to a mere 0.5% of industrial output. Glennon J. Harrison, *Subsidies in the European Community*, in HOUSE SUBCOMM. ON TECHNOLOGY AND TRADE, 102D CONG., 2D SESS., AIRBUS INDUSTRIE: AN ECONOMIC AND TRADE PERSPECTIVE 24, 45 (Comm. Print 1992). The manufacturing sector of industry is the primary recipient of such aid, with 41 percent of national government subsidies in the EC going to the manufacturing sector, roughly 8 times the amount of U.S. subsidies to manufacturing. *Id.* at 27.

21. From 1986-88, the U.K. gave 74% of its subsidies in direct grants, tax reductions and loan guarantees; Germany 91%; France 64%. *Id.* at 28 (Table 4).

create an argument of form rather than substance. It claims the U.S.'s long-standing procurement for aerospace research and development has the same adverse effect on competition as the EC's traditional use of direct grants to Airbus. Indeed, while the EC's direct subsidization of Airbus is not a well-kept secret, U.S. practices of state support are more difficult to identify. The EC points to U.S. dependence on government support in research, development, and large military procurement as evidence of *indirect* subsidies in the production of civil aircraft.²² These practices include not only loan bailouts from the government, but also tax concessions on purchases by U.S. airlines, and tariffs.²³ These efforts have given U.S. manufacturers an ability to assume greater risk than they otherwise could. The steady cash flow resulting from these indirect subsidies has given U.S. manufacturers an improved credit rating.²⁴ Indeed, before the 1980s, U.S. industry financed less than a quarter of its research and development costs from private sector sources.²⁵

The U.S. was motivated by the defense needs of cold war and by the need for a rapid mobilization capacity to promote the industry.²⁶ At the same time, the U.S. political climate encouraged the concept of free-market economics, making direct aid to the industry politically sensitive. As a result, direct subsidization from the U.S. government has only occurred when market realities began to threaten the mobilization capacity of the

22. During the negotiation of this latest agreement, the EC claimed that the United States spent over \$23 billion in subsidies to its aircraft manufacturers. *Airbus Industrie Reaction to Remarks by the U.S. Trade Representative*, Business Wire, Apr. 7, 1988, available in LEXIS, Nexis Library, World File. See also *EEC Finds "Evidence" of US Government Support to Domestic Industry*, Transp. Eur. (Eur. Info. Svc.) No. 13 (Dec. 23, 1991).

23. HAYWARD, *supra* note 11, at 159. The European concern over U.S. tax concessions is even more real after the signing of the bilateral agreement. The Agreement does not regulate this area directly. In September 1992, the EC reopened the aircraft subsidies dispute by objecting to US tax concessions to American industry. They claimed that tax law is being "manipulated to support domestic sales to US airlines." Mary Fagan, *Row Simmers Over Aircraft Subsidies*, INDEPENDENT, Sept. 7, 1992, at 18.

24. HAYWARD, *supra* note 11, at 159-60.

25. BARRY BLUESTONE, ET AL., AIRCRAFT INDUSTRY DYNAMICS, 158-59 (1981).

26. General Hap Arnold, Chief of the Army Air Corps at the end of World War II:

[I]n each war there has been time for the mobilization of [] power and the U.S. has been the determining factor in the defense of civilization . . . There will be no opportunity for gradual mobilization . . . It is of the utmost importance that our first line of defense, in the air, must be manned and fully supplied with modern equipment . . . The U.S. must be the world's first power in military aviation.

AIRCRAFT INDUSTRIES ASSOCIATION, AIRCRAFT MANUFACTURING IN THE UNITED STATES, in THE AVIATION ANNUAL OF 1946, (Reginald M. Cleveland & Frank P. Graham eds., 1945) reprinted in HISTORY OF THE AMERICAN AIRCRAFT INDUSTRY, 162, 178 (G.R. Simonson ed., 1968) [hereinafter SIMONSON]. See also OFFICE OF TECHNOLOGY ASSESSMENT, *supra* note 2, at 344 ("The greatest benefits for U.S. commercial aircraft manufacturers have been side effects of the government's commitment to building and maintaining a strong defense industrial and technology base.").

industry.²⁷ Hence, the EC asserts that indirect support of the U.S. civil aircraft industry through such devices as NASA research assistance and military spending has provided the same type of government assistance as the Europeans, but in a different, less identifiable form.

C. NEGOTIATIONS TO RESOLVE COMPLAINTS OF THE EC AND U.S.

Negotiations began in the early 1970s to resolve these complaints,²⁸ but such efforts failed to produce an agreement.²⁹ An increasing deficit in the U.S. balance of payments, a history of failure in negotiations, and expanded European penetration into the U.S. civil aircraft market, pressured the Carter Administration into signing the GATT Agreement on Civil Aircraft³⁰ despite the agreement's adoption of European views on non-tariff barriers.³¹

The need to renegotiate the Aircraft Code surfaced almost immediately after its signing. With many trade barriers removed for the European Community, Airbus cut into the market share of American manufacturers both at home and abroad. Efforts to alleviate growing tension took a more structured tone on October 27, 1987, when both sides agreed to some basic negotiating principles and objectives, including using the GATT as a vehicle to formalize "mutually satisfactory solutions."³² Indeed, these objectives are prominently noted in the declarations of the formal agree-

27. In the past, Europeans have pointed to three specific actions: (1) development of the military's KC135, minimizing the costs of Boeing's initial entry into the civil jet market; (2) in the 1960s, Lockheed's ability to transfer money authorized for military development to its civil aircraft efforts, and its later receipt of Federal loan guarantees; and (3) federal loan guarantees and questionable procurements of additional aircraft approved for McDonnell Douglas when the threat of insolvency began to loom. HAYWARD, *supra* note 11, at 157-58. "[N]either Douglas nor Lockheed had to pay the ultimate price of commercial misjudgment, and, *in extremis*, their survival had depended upon state aid." *Id.* at 158 citing M. Edmonds, *Market Ideology and Corporate Power in the United States*, in *INDUSTRIAL CRISIS*, 81-87 (K. Dyson and S. Wilkes eds., 1983).

It was also this type of public and private intermixing of capital that helped foreign firms such as Rolls Royce argue for direct government assistance to develop new products. See HAYWARD, *supra* note 11, at 158-59.

28. Cohen & Zysman, *supra* note 17, at 37.

29. Indeed, the 1978 "Arrangement on Guidelines for Officially Supported Export Credits" specifically excluded aircraft sales from its scope. *Id.* at 37.

30. Agreement on Trade in Civil Aircraft, 31 U.S.T. 619, T.I.A.S. No. 9620, 1186 U.N.T.S. 170 [hereinafter Aircraft Code].

31. HAYWARD, *supra* note 11, at 175.

32. Specifically, these objectives included: (1) that the current dispute should be resolved through the GATT, (2) a commitment to find "mutually satisfactory solutions in a spirit of mutual understanding . . . [to] promote international competition and facilitate the development of aircraft manufacturing in a fair economic environment, (3) resolve interpretive differences involving Article IV of the [Aircraft Code], and (4) a mandate for resolution of government support in the development of long-range civil aircraft." *U.S., EC Negotiators Given December Deadline to Resolve Civil Aircraft Subsidies Dispute*, Int'l Trade Rep. (BNA) No. 42 at 1312 (Oct. 28, 1987).

ment itself.³³

Still lacking a formal agreement on the 1987 objectives, the United States filed a formal complaint with the GATT Subsidies Committee over German subsidies in February 1991.³⁴ The U.S. made an additional complaint to the Subsidies Committee in May 1991, requesting the elimination of direct government subsidies.³⁵ The United States then heightened tensions by threatening to impose a tax on Airbus imports.³⁶

In June 1991, the European Community asked the GATT if the matter could be resolved through renegotiating the Aircraft Code.³⁷ However, the critical shift in the negotiations came after a GATT panel ruling that German payments as part of exchange rate guarantees to Airbus were illegal.³⁸ It was this striking blow to the European bargaining position, and it accelerated the negotiating process. By the end of March 1992, both parties reached a tentative agreement,³⁹ which was later finalized into the current bilateral accord.

The bilateral Agreement represents the culmination of twelve years (1980-92) of continuous complaints from both European and American aircraft producers to resolve each side's perception of unfair trade practices. Like the Aircraft Code, it too was signed in the dwindling months of an administration pressured to promote American exports in light of a worsening balance of payments deficit and even further European integration in the U.S. market.

II. LEGAL CONTEXT

The Agreement represents a major compromise by both sides after many tense years of negotiations. Now that there is an accord, the question remains whether it can be used as a model for revisions to the Aircraft Code or any other future multilateral agreement, as both sides hope.

To understand the implications of the Agreement, an investigation of instruments which affect current trade in this area is required. This sec-

33. Agreement, *supra* note 6, at 1273.

34. *GATT/Airbus: U.S. Complaint against Germany to be Examined on February 28, 1991*, Eur. Rep. (Eur. Info. Svc.) No. 1656, at 3 (Feb. 27, 1991).

35. *EC Commission Voices Regret at U.S. Move to File New GATT Complaint on Airbus*, 8 Int'l Trade Rep. (BNA) No. 22, at 820 (May 29, 1991).

36. Harvey Elliott, *Fears Grow of U.S. Tariff on Airbus if Aid Persists*, TIMES, May 29, 1991, at B1.

37. *EC Asks GATT that U.S. Airbus Complaint be Settled Under Civil Aircraft Pact*, 8 Int'l Trade Rep. (BNA) No. 25, at 947 (June 19, 1991).

38. *GATT/Airbus: US Scores a Point in Row with EEC*, Transp. Eur. (Eur. Info. Svc.) No. 14 (Jan. 26, 1992); Michael Harrison, *Gatt Rules Against Europe in Airbus Subsidy Row*, INDEPENDENT, Jan. 16, 1992, at 24.

39. *EC and U.S. Reach Accord in Aircraft Subsidy Dispute*, 9 Int'l Trade Rep. (BNA) No. 14 at 575 (Apr. 1, 1992).

tion highlights the policy changes between the General Agreements on Tariffs and Trade (GATT),⁴⁰ Subsidies Code,⁴¹ Aircraft Code,⁴² U.S. trade law, and EC law on state subsidies.

A. THE GATT APPROACH TO TRADE

Most international trade is governed by the rules and arrangements set forth in the General Agreement on Tariffs and Trade (GATT).⁴³ The GATT was founded on the premise that trade would be conducted by private individuals in markets where the unobstructed interplay of supply and demand set prices.⁴⁴ The objective of the GATT, from its inception, was to reduce tariffs and other barriers to trade through agreements among the GATT's trading partners and, at the same time, to insure that all contracting nations would receive most-favored nation status.⁴⁵ The founders believed such unrestricted, non-discriminatory trade would increase market efficiency.⁴⁶

The GATT approach embodies four main assumptions. First, it assumes that trade arrangements constructed from multilateral negotiations are preferable to bilateral or other agreements. It does not anticipate negotiations between individual nations. Second, it assumes that private persons shall conduct trade in an atmosphere of free interaction of supply and demand. Third, it assumes that such free trade shall result in the expansion of all economies. Fourth, it assumes that government intervention distorts the market in a way that delays internal adjustment to international prices.⁴⁷

Despite the GATT's general premise that government intervention is not economically efficient, its regulation of government subsidies was weakly constructed. Indeed, the original GATT agreement had only a reporting requirement for subsidies.⁴⁸ It did not include an outright prohibi-

40. General Agreement on Tariffs and Trade, *opened for signature* Oct. 30, 1947, 61 Stat. A3, T.I.A.S. No. 1700, 55 U.N.T.S. 187 [hereinafter GATT].

41. Agreement on Interpretation and Application of Articles VI, XVI, and XXIII of the General Agreement on Tariffs and Trade, *opened for signature* April 12, 1979, 31 U.S.T. 513, T.I.A.S. No. 9619, 1186 U.N.T.S. 204 [hereinafter Subsidies Code].

42. Aircraft Code, *supra* note 30.

43. GATT, *supra* note 40.

44. Ann M. Denman, *Airbus and Ilk: Thumbing Their Noses at the GATT?*, 29 HARV. INT'L L.J. 111, 111 (1988).

45. "Any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for all other contracting parties." GATT, *supra* note 40, art. I, para. 1.

46. Cohen & Zysman, *supra* note 17, at 3.

47. *Id.*

48. "If any contracting party grants or maintains any subsidy . . . it shall notify the con-

tion of their use.⁴⁹ The original agreement was later amended to restrict and prohibit certain subsidies on exports,⁵⁰ but such provisions apply only to domestic subsidies and only to the nations which accepted the amendment.⁵¹ The term "subsidy" itself is not clearly defined in the GATT.⁵²

The GATT also imposes regulations on "state enterprises." Article XVII defines which organizations may be classified as state enterprises⁵³ and provides standards for such organizations.⁵⁴ However, Article XVII has been largely ineffective in practice. While Article XVII requires that state enterprises notify GATT members of all products that are imported or exported by such organization,⁵⁵ most nations do not provide any notification voluntarily. If a government were to do so, it would, in effect, concede the operation of a state enterprise and thus be subject to special GATT rules for such companies.⁵⁶ Hence, there is a disincentive to voluntarily notify other nations that a state enterprise exists. The practical reality is that governments neither notify other contracting nations of state enterprise practices nor comply with the standards set forth in the GATT.⁵⁷ While European officials have clearly admitted in private that Airbus benefits from state subsidies,⁵⁸ the European Community has re-

tracting parties in writing of the extent and nature of the subsidization . . ." GATT, *supra* note 40, art. XVI, para. 1.

49. Kenneth W. Abbott, *Introduction to the General Agreement on Tariffs and Trade*, 1 Basic Doc. Int'l Econ. L. (CCH) ¶ 3 (1990).

50. GATT, *supra* note 40, art. XVI, para. 2-5.

51. *Id.* at art. XXX.

52. William Lay, Note, *Redefining Actionable "Subsidies" Under U.S. Countervailing Duty Law*, 91 COLUM. L. REV. 1495, 1496 (1991).

53. GATT defines a state enterprise as follows:

Each contracting party undertakes that if it establishes or maintains a state enterprise, wherever located, or grants to any enterprise, formally or in effect, exclusive or special privileges, such enterprise shall . . . act in a manner consistent with the principles of nondiscriminatory treatment prescribed in this Agreement for governmental measures affecting imports or exports by private traders.

GATT, *supra* note 40, art. XVII, para. 1(a).

54. Article XVII of GATT defines the standards of practice for a state enterprise as follows:

[S]uch enterprises shall . . . make . . . purchases or sales solely in accordance with commercial considerations, including price, quality, availability, marketability, transportation and other conditions of purchase or sale, and shall afford the enterprises of other contracting parties adequate opportunity, in accordance with customary business practice, to compete for participation in such purchases or sales.

Id. at art. XVII, para. 1(b).

55. "The contracting parties shall notify the contracting parties of the products which are imported into or exported from their territories by enterprises of the kind described in paragraph 1(a) of this Article" *Id.* at art. XVII, para. 4(a).

56. Such an admonition would be considered self-incrimination. Note, *The Post-Tokyo Round GATT Role in International Trade Dispute Settlement*, 1 INT'L TAX & BUS. LAW. 142, 148 (1983).

57. Denman, *supra* note 44, at 113-15.

58. Cohen & Zysman, *supra* note 17, at 17. See also Dallos, *supra* note 4, at D1

fused to label its relationship with Airbus as a state enterprise.⁵⁹ The United States also refuses to categorize its relationship with the civil aerospace industry as one which includes the granting of special privileges.⁶⁰

Nonetheless, the GATT provides measures for contracting nations to protect themselves against foreign-subsidized products. Article VI states that an importing country may impose a "countervailing duty"⁶¹ if the effect of a subsidy is "to cause or threaten material injury to an established domestic industry."⁶² The imposition of such a duty compensates for the amount of total subsidy which a foreign government has provided to a producer.⁶³

The GATT has been unsuccessful in establishing an effective system of enforcement which does not rely largely on the power of retaliation. Since the GATT was negotiated on the premise that free trade is a natural, universal motivator, it did not envision a need for powerful enforcement mechanisms. Unlike most international agreements, contracting parties are not required to comply with official recommendations or rulings.⁶⁴ The GATT takes a flexible view that its policies are merely desired conduct,⁶⁵ despite the fact that today's modern trade practices require a strict legal standard. The GATT heavily emphasizes the use of consultation as a means of dispute resolution. Nineteen clauses of the GATT agreement require consultations between adverse parties.⁶⁶ Hence, the enforcement provisions of the GATT rely too heavily on flexible suggestions rather than a base of authority to impose recommendations for dispute resolution. As a result, in order to properly resolve subsidy disputes, further agreement between disputants is traditionally required under the GATT.

B. THE GATT SUBSIDIES CODE

Countervailing duties most often replaced consultations as the immediate response to disputes under the original GATT text. Member nations

("[G]overnment financial help was needed to create the company") (quoting spokesman for Airbus).

59. Dallos, *supra* note 4, at D1.

60. See Nancy Dunne, *U.S. Hits Back at Airbus Report*, FIN. TIMES, Apr. 7, 1988, at 4.

61. GATT defines a "countervailing duty" as: "a special duty levied for the purpose of offsetting any bounty or subsidy bestowed directly or indirectly, upon the manufacture, production or exportation of any merchandise." GATT, *supra* note 40, art. VI, para. 2.

62. *Id.* at art. VI.

63. Tariff Act of 1930, 19 U.S.C. § 1671(a)(2) (1992).

64. Shaun A. Ingersoll, Note, *Current Efficacy of the GATT Dispute Settlement Process*, 22 TEX. INT'L L.J. 87, 95 (1986).

65. For example, GATT provides an exception to its nondiscrimination policy where national industries are in trouble and require temporary flexibility. *Id.*

66. *Id.* at 98.

became increasingly concerned with the ease with which others could impose destructive tariffs as a response to disputes. Because of a quirk in the GATT's legal requirements for administering countervailing duty measures, the United States was once able to impose such duties without any showing of injury.⁶⁷ As a result of the fear of retaliation and the shift toward non-tariff concerns in the 1970s,⁶⁸ the GATT Subsidies Code was negotiated as a supplemental agreement in the Tokyo Round of GATT negotiations (1973-1979), outlining in greater detail the proper use of such procedures.⁶⁹

In practice, however, the Subsidies Code did little more than require the United States to show injury before imposing countervailing duties. It lacked clear guidelines for determining which government benefits may be treated as subsidies.⁷⁰ While it provides that benefits "granted with the aim of giving an advantage to certain enterprises" are a possible ground for defining a subsidy,⁷¹ the Subsidies Code does not state that such advantages are *actionable* as subsidies.⁷²

C. THE LAWS OF THE UNITED STATES RELATING TO SUBSIDIES

Despite being constrained by its obligations under the GATT, the United States has produced its own unique set of legislation intended to address the problem of foreign government subsidization. In practice, the U.S. government is selective in its use of countervailing duties.⁷³ It must

67. Under the "grandfather clause" of the Protocol of Provisional Application of the GATT, contracting nations may follow their prior inconsistent domestic legislation in respect to GATT Articles VI and XVI. The United States relied on the grandfather clause to apply countervailing duties without a showing of injury to domestic U.S. industry. As a result of this practice, the Subsidies Code was negotiated. Theodore W. Kassinger, *Introduction to Agreement on Interpretation and Application of Articles VI, LVI and XXIII of the General Agreement on Tariffs and Trade (GATT Subsidies Code)*, 1 Basic Doc. Int'l Econ. L. (CCH) ¶ 79 (1990).

But note the United States still has the power to impose countervailing duties without a showing of injury on non-duty free products from all GATT nations who have not ratified the GATT Subsidies Code. Stephen F. Benz, *Note: Below-Cost Sales and the Buying of Market Share*, 42 STAN. L. REV. 695, 721 (1990).

68. Lay, *supra* note 52, at 1496.

69. The Subsidies Code now requires the following: the simultaneous investigations of subsidization and injury, reasonable notice of investigations and a reasonable opportunity to participate in such investigations, and that investigations must be concluded within one year. Subsidies Code, *supra* note 41, art. 2, para. 4, 5, and 14.

70. *Dual Pricing of Natural Resources: Hearing Before the Subcommittee on International Trade of the Committee on Finance of the United States Senate*, 99th Cong., 2d. Sess. 77-79 (1986) [hereinafter *Hearing on Dual Pricing*] (Statement of Prof. Gary C. Hufbauer) .

71. Subsidies Code, *supra* note 41, art. 11, para. 3.

72. *Id.*

73. See *Hearing on Dual Pricing*, *supra* note 70, at 22 ("[governments do not attempt to counteract] every conceivable Government program under the sun") (testimony of Alan F. Holder, General Counsel, U.S. Trade Representative) .

walk a thin line: attempting to avoid antagonizing its trading partners and provoking retaliation, while at the same time protecting domestic businesses from unfair practices.⁷⁴ Certainly the Airbus subsidy complaint is highly delicate for the United States, since the European Community is the largest trading block in the world and the U.S. has a trade surplus with the Community in the field of civil aviation.⁷⁵

The Subsidies Code was made a part of U.S. law with the enactment of the Trade Agreements Act of 1979.⁷⁶ However, unlike GATT and its codes, U.S. legislation attempts to provide a specific definition for the term "subsidy" as part of the Act.⁷⁷ This Act established a two-step process to determine if a benefit given by a foreign government is an actionable subsidy subject to countervailing duties under U.S. law.⁷⁸ It is

74. Gary N. Horlick, *et al.*, *The Counteravailability of Subsidies: Specificity 38* (Oct. 28, 1985) (unpublished manuscript on file with the *Columbia Law Review*) as cited in Lay, *supra* note 52, at 1498.

75. In 1991, the United States shipped \$7 billion worth of civil aircraft products to the European Community as compared with imports of only \$1.3 billion. William J. Eaton, *U.S., EC Sign Accord to Limit Aircraft Subsidies*, L.A. TIMES, July 18, 1992, at D1.

76. Pub. L. No. 96-39, 93 Stat. 144 (codified in scattered sections of 19 U.S.C.).

77. See 19 U.S.C. § 1677(5) (1992). A list of illustrative domestic subsidies follows the definition:

- (I) The provision of capital, loans, or loan guarantees on terms inconsistent with commercial considerations.
- (II) The provision of goods and services at preferential rates.
- (III) The grant of funds or forgiveness of debt to cover operating losses sustained by a specific industry.
- (IV) The assumption of any costs or expenses of manufacture, production, or distribution.

Id. at § 1677(5)(A) (This is not an exhaustive list).

The definition of a subsidy under U.S. trade law was expanded to include upstream subsidies (indirect aid from governments through supplier agreements at less than market rates) under the Tariff and Trade Act of 1984. Public L. No. 98-573, 98 Stat. 2948 (1984). For a discussion of the ramifications of this addition, see Judith H. Bello & Alan F. Holder, *The Tariff and Trade Act of 1984: Principal Antidumping and Countervailing Duty Provisions*, 19 INT'L LAW. 639 (1985); Paul W. Jameson, *The Administration of the U.S. Counteravailability Duty Laws with Regard to Domestic Subsidies: Where It's Been, Where It Is, Where It May Go*, 12 SYRACUSE J. INT'L L. & COM. 59, 86-96 (1985).

78. 19 U.S.C. §§ 1671-1677k (1992). The first stage determines if the benefit constitutes a "subsidy" under the statutory definition. This is done by the Commerce Department's International Trade Administration. 19 U.S.C. §§ 1671(a)(1), 1677(1), (1992); *id.* at § 2171 notes transfer of power from Secretary of Treasury to Secretary of Commerce.

If a subsidy is determined, the International Trade Commission then looks to whether there is material injury or a threat of material injury. *Id.* at §§ 1671(a)(2). If both a subsidy and a material injury is found, the Commerce Department may seek to impose a countervailing duty. *Id.* at § 1673.

For a detailed description of this process under U.S. Trade law, see Kathleen T. Weaver, *Subsidies and Countervailing Duties Under the Trade Act of 1979*, 5 N.C. J. INT'L L. & COM. REG. 533 (1980); Jameson, *supra* note 77.

through this process that the "specificity test"⁷⁹ is administered. While this test provides the United States a means of regulating the use of countervailing duties, the process has proven inadequate at screening when the United States should administer such duties. Indeed, the GATT panels continue to hold that the U.S. practices violate the intent of the international guidelines to which it must conform.⁸⁰

As a result, the Airbus subsidy dispute succeeded in shifting attention not only to the inadequacies of the GATT Subsidies Code, but also those of the United States Trade Acts. The Subsidies Code proved unable to deal with complex disputes. Its language is too vague. Indeed, it does not outline what actions constitute a "subsidy." Further, it does not provide a clear mandate for action.⁸¹

At the same time, the revisions to the Subsidies Code made upon its adoption by Congress have not advanced U.S. trade interests in this case. The "specificity" test, with the *ad hoc* nature of its application, does not provide a consistent, clear policy on subsidies which can be relied upon by domestic or foreign corporations.⁸² As a result, U.S. law has provoked anger and warnings from the GATT.⁸³ Indeed, throughout the history of U.S. trade policy, the primary policy response to situations where domestic industry has been "jolted" by international competition is to invoke protectionist measures.⁸⁴ The challenge now is to construct a framework whereby the U.S. may find its interests protected without hav-

79. Hearing on Dual Pricing, *supra* note 70, at 22 (statement of Alan F. Holder, General Counsel, U.S. Trade Representative).

The "specificity test" refers to language in the statutory definition of "subsidy." There it states that "subsidy" includes any domestic or export subsidy, "if provided to a *specific* enterprise or industry or group of enterprises or industries." 19 U.S.C. § 1677(5)(A) (italics supplied). The Commerce Department, however, has *ad hoc* power to determine whether the producers receiving benefits constitute a specific group. See Lay, *supra* note 52, at 1498-1500.

Note that the Subsidies Code does not specifically grant the right to label an action a "subsidy" simply because it gives an advantage to certain enterprises. See *supra* notes 69-71 and accompanying text.

80. GATT: *U.S. Bars Cheaper Imports*, WASH. TIMES, March 13, 1992, at C3. For a detailed discussion of the process for determining injury in the Commerce Department and its inadequacies, see Bryan T. Johnson, *A Guide to Antidumping Laws: America's Unfair Trade Practice, Backgrounder*, Ctr. for Econ. Growth (Heritage Found.) No. 906 (1992).

81. See also *supra* notes 73-4 and accompanying text.

82. Indeed, there are conflicting views as to what constitutes material injury under the specificity test. Compare Edward R. Easton & William E. Perry, *The Causation of Material Injury: Changes in the Antidumping and Countervailing Duty Investigations of the International Trade Commission*, 2 UCLA PAC. BASIN. L. J. 35 (1983) (an unofficial look at the ITC's approach at determining material injury and counteravailability) with N. David Palmeter, *Countervailing Subsidized Imports: The International Trade Commission goes Astray*, 2 UCLA PAC. BASIN. L.J. 1 (1983) (an unofficial look at the Commerce Department's view of material injury and counteravailability).

83. Johnson, *supra* note 80.

84. Cohen & Zysman, *supra* note 17, at 39-40.

ing to resort to widespread, institutionalized protectionism.⁸⁵

D. EC POLICY REGARDING STATE AID

The EC attitude toward government support for commercial industry differs greatly from that of the United States. The EEC Treaty⁸⁶ is the primary source of guidance for EC policy in the area of state aid. While the European Court of Justice and the Commission of the European Communities (the "Commission") would probably define the actions of the Airbus consortium as state aid,⁸⁷ the Treaty carves out several exceptions to a general rule against this type of assistance.

First, the Treaty provides that state aid is generally presumed to be "incompatible with the common market" if administered in a form which distorts competition.⁸⁸ While the EC and U.S. certainly disagree on the distortional effect of Airbus subsidies, the intent of the Treaty provision is to focus on the European common market rather than on international trade distortions outside of Europe.

Second, the Treaty permits state aid "to promote the execution of an important project of common European interest . . . [and] aid to facilitate the development of certain economic activities. . . ."⁸⁹ Here, the Treaty carves out an exception to the general rule against state aid. Since Airbus was founded in the common European interest to develop a large civil aircraft industry in the European Community, any attempt to utilize EC law as a means of curbing state aid to the Airbus consortium could be thwarted easily.⁹⁰

85. This same concern was expressed by the former Senator and Vice-President in Dan Quayle, *United States International Competitiveness and Trade Policies for the 1980s*, 5 *Nw. J. INT'L L. & Bus.* 1-2, 36-39 (1983).

86. Treaty Establishing the European Economic Community, Mar. 25, 1957, 298 U.N.T.S. 11 (entered into force Jan. 1, 1958) [hereinafter Treaty].

87. For example, the European Court of Justice has defined state aid in the following ways: (1) "[a] grant from the state for no consideration." Opinion of the Advocate General Reischl in Case 61/79, *Amministrazione delle Fianze Dello Stato v. Denkavit Italiana Srl*, 1980 E.C.R. 1205, 1235, as cited in Andrew Evans & Stephen Martin, *Socially Acceptable Distortion of Competition: Community Policy on State Aid*, 19 *EURO. L. REV.* 79, 81 n.12 (1991); (2) "[a]ssumption by the state of part of the risk which is normally assumed by undertakings." Commission Decision 90/70 of June 28, 1989, concerning aid by France to primary processing steel undertakings O.J. 1990 L47/28 at 35 as cited in Andrew Evans & Stephen Martin, *Socially Acceptable Distortion of Competition: Community Policy on State Aid*, 19 *EURO. L. REV.* 79, 81 n.14 (1991); and (3) "[g]rant of resources or advantages by the state to encourage the attainment of economic or social objectives." Case 61/79, *Amministrazione delle Fianze dello Stato v. Denkavit Italiana Srl*, 1980 E.C.R. 1209, 1228, as cited in Andrew Evans & Stephen Martin, *Socially Acceptable Distortion of Competition: Community Policy on State Aid*, 16 *EURO. L. REV.* 79, 81 n.16 (1991).

88. Treaty, *supra* note 86, at art. 92, para. 1.

89. *Id.* at art. 92, para. 3(b)-(c).

90. Indeed, the Commission relied on this language in its defense of its subsidies to Daimler Benz, the owner of Deutsche Airbus:

Finally, the Commission is given broad discretionary power to determine what financing constitutes illegal state aid under the EEC Treaty.⁹¹ Therefore, if the United States or even a European aircraft maker were to file a complaint under Community law, there is little likelihood of a successful suit since the same political forces funding the Airbus consortium hold powerful positions within the Commission.

Nonetheless, the Europeans are motivated to end subsidization for political rather than legal reasons. The goal of a single internal market has put extra emphasis on the abolition of state aid within the European Community.⁹² Certainly, now that Airbus has established profitability, the practice of soliciting contributions from its sponsoring governments appears inappropriate when a crackdown on other uses of state aid is underway.

E. THE GATT AGREEMENT ON TRADE IN CIVIL AIRCRAFT

Realizing its rapid loss of world market share of civil aircraft in the 1970s, the U.S. insisted upon the inclusion of civil aircraft as part of the Tokyo Round of GATT negotiations. Its efforts were concentrated on abolishing government support for development and export subsidies. At the same time, the EC focused its efforts on gaining even greater access to the U.S. market. Despite U.S. initiation of discussions, the European Community exerted more influence over the final draft of the agreement. The U.S., facing a growing balance of payments deficit and increasing foreign penetration into its markets, was under great pressure to sign any deal which may promote American exports and curb European "excesses."⁹³

Understanding this weakness, the Europeans remained firm. As a result, the language restricting European practices was left extremely vague and almost unenforceable, while language aimed at advancing European concerns is closer to EC objectives.

The Aircraft Code did little to change the regulations on government support. The Aircraft Code expressly relies on the Subsidies Code to out-

In view of the economic and technological importance of the aviation industry to the Community, the Commission considered that the [subsidies to Daimler] would strengthen the overall competitiveness of the sector and thus concretely serve the general interest . . . It therefore considered that state aids qualified for exemption under Article 92(3)(b) (execution of an important project of common European interest).

Commission of the European Communities, *Nineteenth Report on Competition Policy* 157-58 (1990), as cited in Harrison, *supra* note 20, at 35.

91. See e.g., *State Subsidies: An Exercise in Ingenuity*, 138 NEW L.J. 810, 811 (1988).

92. See Commission of the European Communities, *Sixteenth Report on Competition Policy*, 135 (1987) (Community's efforts to complete a single unified internal market by 1992 . . . lend added weight and importance to the enforcement of competition rules, and in particular the rules on State aid") as cited in Evans & Martin, *supra* note 87, at 101.

93. HAYWARD, *supra* note 11, at 175.

line its position on government supports.⁹⁴ But even this provision has little real impact, considering the Aircraft Code also includes language recognizing that government supports are a "special factor" inherent to the industry.⁹⁵ The Aircraft Code requires that pricing need only involve a "reasonable expectation of recoupment of all costs."⁹⁶ How to determine what constitutes a "reasonable" return remains extremely unclear.

The Aircraft Code created new rules regarding aircraft marketing practices, but they were drafted in a manner giving them little practical significance. Rules in the area of marketing are important, since most firms which produce civil aircraft,⁹⁷ as well as a majority of the world's scheduled airlines, are also wholly or partially-owned by their governments.⁹⁸ Therefore, for most carriers and producers outside the U.S., the purchase of aircraft involves both financial *and* political considerations. As a result, government influence quickly becomes a factor in marketing.

While the Aircraft Code forbids government pressure on airlines, aircraft manufacturers, and "other entities," to make purchases of civil aircraft from a particular source,⁹⁹ its provisions are couched in language so vague such restrictions are essentially unenforceable. Here again, the drafters of the Aircraft Code use a "reasonable" standard:

Signatories shall not require airlines, aircraft manufacturers, or other entities engaged in the purchase of civil aircraft, nor exert *unreasonable pressure* on them, to procure civil aircraft from any particular source which would create discrimination against suppliers from any Signatory [italics supplied].¹⁰⁰

The resulting agreement thus contains a huge loophole destroying much of its original spirit. Indeed, the Aircraft Code merely restates much of the GATT standards already in place relating to state trading and marketing.¹⁰¹

94. Aircraft Code, *supra* note 30, at art. 6, para. 6.1 ("Signatories note that the provisions of the [Subsidies Code] apply to trade in civil aircraft.").

95. *Id.* at art. 6, para. 1.

96. *Id.* at art. 6, para. 2.

97. U.S. DEPARTMENT OF COMMERCE, *supra* note 5, at 74.

98. *Id.* at 75.

99. Aircraft Code, *supra* note 30, at art. 4, para.2. See also *id.* at art. 4, para. 4 ("Signatories agree to avoid attaching inducements of any kind to the sale or purchase of civil aircraft . . .").

100. *Id.* at art. 4, para. 2

101. The Aircraft Code provides:

Signatories agree that the purchase of products covered by this Agreement should be made only on a competitive price, quality, and delivery basis . . . [A] signatory may, however, require that its qualified firms be provided with access to business opportunities on a competitive basis and on terms no less favourable than those available to the qualified firms of other Signatories.

Id. at art. 4, para. 3.

This is substantially similar to the provisions for state trading in the main body of GATT:

[State trading] enterprises shall, having due regard to the other provisions of the [GATT], make . . . purchases or sales solely in accordance with commercial considera-

The Aircraft Code provides no restriction on the use of government export credits, a major interest of the U.S. in light of the failure to include aircraft in the 1978 Arrangement on Guidelines for Officially Supported Export Credits.¹⁰² As a result, the Export-Import Bank ("Exim") has become more heavily relied upon to minimize unfair practices, producing both an additional cost and a philosophical compromise from a strict private enterprise philosophy.¹⁰³

The European Community, on the other hand, was more successful in negotiating terms that would facilitate its goal of opening markets. The Aircraft Code provides clear language eliminating customs duties on aircraft products, parts, and repairs;¹⁰⁴ reiterates the commitment to the provisions of the GATT Agreement on Technical Barriers to Trade;¹⁰⁵ and eliminates both quantitative restrictions and licensing requirements on imports and exports.¹⁰⁶ In these ways, the EC managed to enhance its objectives while the U.S. was forced to accept less imposing language to address its concerns. As a result, the U.S. manifested its frustration with the initiation of complaints about European support practices throughout the 1980s.

III. ANALYSIS OF THE BILATERAL AGREEMENT AND ITS IMPLICATIONS

Like the Carter Administration, which signed the last major agreement involving civil aircraft trade, the Bush Administration faced similar economic and political pressures to reach an accord. The U.S. balance of payments deficit was even higher in 1992. So too was European penetration into the U.S. and world aerospace markets. These were the driving factors for the Carter Administration to sign the Aircraft Code, and these same pressures drove the Bush Administration to sign the Agreement.¹⁰⁷

tions including price, quality, availability, marketability, transportation and other conditions . . . and shall afford the enterprises of other contracting parties adequate opportunity, in accordance with customary business practice, to compete for participation in such purchases or sales.

GATT, *supra* note 40, art. XVII, para. 1(b).

102. *See also supra* note 29.

103. HAYWARD, *supra* note 11, at 175.

104. Aircraft Code, *supra* note 30, art. 2, para. 1.

105. *Id.* at art. 3, para. 1.

106. *Id.* at art. 5, para. 1-2.

107. The Bush Administration specifically wanted the accord to limit development subsidies, prohibit production subsidies, and expand such rules multilaterally. *President's 1992 Trade Policy Agenda*, 9 Int'l Trade Rep. (BNA) No. 10, at 422 (Mar. 4, 1992) (Full text).

A. *THE TERMS OF THE AGREEMENT BETWEEN THE UNITED STATES AND THE EUROPEAN COMMUNITY SIGNED JULY 17, 1992*

The Agreement between the United States and the European Community contains several major advancements towards creating a level playing field for both sides. First, the Agreement provides for a ban on all future production subsidies and a limit on development subsidies at 33% of total cost. Second, it reinforces current language to further prohibit government assistance in marketing. Third, it increases reporting requirements, creating greater transparency in the marketplace.¹⁰⁸ Finally, it limits indirect government aid to 3% of annual industrywide turnover and 4% of the turnover for each individual manufacturer.

1. *NEW RULES ON DIRECT SUBSIDIES*

The Agreement bars all future production subsidies¹⁰⁹ and limits current development subsidies to 33% of the total development costs on new aircraft.¹¹⁰ The U.S. had originally hoped to resolve the dispute by a total ban on all subsidies.¹¹¹ This objective can be traced back to the Carter Administration's goals in negotiating the Aircraft Code in 1979. The failure of the Aircraft Code to place an outright ban on subsidies left continuing tension between the two parties.

These provisions represent some gains for the United States on an initial bilateral basis, since it will curb some of the disputed trading practices. Yet at the same time, the limits on subsidies points to the weaknesses in the current multilateral framework. As noted earlier, GATT does not contain an outright ban on subsidies.¹¹² Indeed, it does not even define what qualifies as an actionable subsidy.¹¹³ This flaw has not been corrected in the Agreement, which still does not define a "subsidy" or when an action constitutes "government support." Nor does the Agreement establish a new framework for dispute resolution.¹¹⁴ Consequently, there is no showing that this new Agreement will eliminate these problems associated with the current GATT framework.

However, by at least banning future production subsidies, the United

108. "Transparency" in this context means greater public awareness of the government's actions. Denman, *supra* note 44, at 115.

109. Agreement, *supra* note 6, at art. 3, para. 1.

110. *Id.* at art. 4, para. 1-3.

111. Dallos, *supra* note 4 ("Neither the U.S. government nor the U.S. industry is prepared to live with the current situation in which privately financed companies compete against government-subsidized entities.") (quoting U.S. Transportation Secretary Samuel K. Skinner).

112. See *supra* notes 49-52, 70-72.

113. Lay, *supra* note 52, at 1497.

114. The dispute mechanism for the Agreement shall be the general GATT provision as agreed to in the Uruguay Round. Agreement, *supra* note 6, art. 12, para. 1.

States gained an additional legal tool to combat any European claims that government production supports do not hinder free trade. In addition, the compromise to limit developmental support to 33% of total costs demonstrates a strong reduction from current practices of supporting 75%-100% of all such costs.¹¹⁵ Also as part of the concessions on development cost subsidies, the European Community has agreed to force Airbus to repay cash advances at levels of interest closer to market rates than was previously practiced.¹¹⁶ This limitation will greatly reduce Airbus' advantage in being able to accept lower-than-market rates of return in its orders.¹¹⁷ Its elimination shall have an immediate impact, since financing considerations were a primary part of Airbus' strategy to gain market share.¹¹⁸

Surprisingly, Congress has been most critical of the direct subsidy regulatory provisions of the bilateral Agreement. It has treated the new ceiling on such spending as a "legitimization" of European subsidies at the expense of American industry.¹¹⁹ Despite the satisfaction of both the Bush Administration and European Community with the Agreement, Congress has been hostile to the accord. Both the House of Representatives and the Senate have passed non-binding resolutions calling on the United States not to "condone or legitimize" subsidies that cause injury to U.S. companies.¹²⁰ Their expectations of the Agreement have run counter to political reality. Resolutions passed in Congress criticize the Agreement: (1) for allowing subsidies to continue, rather than imposing an outright ban, and (2) for not requiring Airbus to repay the full value of past subsidies. While Congressional approval was not required for the execution of the Agreement, Congressional consent will be required for any future multilateralization of the Agreement.¹²¹

However, the election year context of these Congressional efforts makes these actions a less credible threat to any future multilateral agreement. As Ann Denman predicted in 1988, tough talk about trade law and strong, unrealistic remedies are commonplace in election year

115. Eaton, *supra* note 75. See also Dallos, *supra* note 4 ("On the average, 74% of the cost to develop new aircraft has been provided Airbus governments.").

116. Eaton, *supra* note 75.

117. A recent study by the U.S. Commerce Department says the companies claims: [T]he Airbus consortium have been subsidized by their respective governments to the tune of \$13 billion since Airbus' founding. If commercial interest rates were applied, the value of such support would be \$25 billion. Dallos, *supra* note 4.

118. Cohen & Zysman, *supra* note 17, at 17. Indeed, financing can create purchases that otherwise would not occur. For example, a 2% advantage on financing terms will outweigh over a 5% advantage in fuel efficiency. *Id.* at 36.

119. 138 CONG. REC. S 4848 (1992); 139 CONG. REC. S 2005 (1993).

120. H.R. 417 102d Cong., 2d Sess. (1992); S. 281, 102d Cong., 2d Sess. (1992).

121. 1988 Omnibus Trade and Competitiveness Act, 19 U.S.C. §§ 2901-2906.

"hype."¹²² Undertones of protectionism seem to swell in the presidential campaigns as well.¹²³ Hence, while on their face these objections seem terribly damaging to the goals of the Agreement, criticism of the Agreement should lessen in the United States as election year politics fade.

2. RULES ON SALES AND MARKETING OF AIRCRAFT

The Agreement bars state efforts in sales and marketing.¹²⁴ Historically, this was a concern of the United States. European governments did not hide the interplay between government action and aircraft sales. Airbus sales have been discussed at a number of meetings between high level European officials and other nations, producing agreement for Airbus purchases as part of broad economic, political and cultural packages.¹²⁵ Indeed, part of Airbus' market strategy has been to invoke political pressure from its sponsoring governments and use state influence in markets outside Europe and the United States.¹²⁶ The fact that a majority of the world's airlines outside the United States continue to be state-run amplifies the ability of state governments to influence the civil aircraft market.

The Agreement builds on the Aircraft Code's efforts in this area.¹²⁷

122. Specifically, Denman made the following comment:

Efforts [to amend trade laws and provide sanctions against violators of GATT rules on state enterprises] are made as part of election year 'hype' when, responding to a rising tide of protectionist sentiment, legislators tend to propose powerful remedies without first carefully defining the problems posed by state trading.

Denman, *supra* note 44, at 111.

123. For example, note the protectionist undertones of Patrick Buchanan's campaign during the time when the terms of the Agreement were being finalized. See Gloria Berger, *Standing Pat? Civil War on the Right*, U.S. NEWS & WORLD REP., Mar. 16, 1992, at 31; William Pfaff, *Will Isolationism Cause U.S. to Eschew World Cooperation?*, CHI. TRIB., Mar. 15, 1992, at 3.

Also note the comments in the final presidential debate of October 18, 1992: "We won't be making airplanes in this country 10 years from now if we let deals like this go through." Clinton, *Buyouts Have Wrecked the U.S. Airline Industry*, Reuters, Oct. 19, 1992 (AM Cycle) (Comments of Ross Perot, Independent Candidate for President, referring specifically to European ownership of U.S. airlines).

"Even Boeing is losing market share — because we let the Europeans spend \$25 to \$40 billion on Airbus without an appropriate competitive response." *Id.* (Comments of Bill Clinton, Democratic Candidate for President).

124. Agreement, *supra* note 6, at anx. 1.

125. An excellent example of this interplay occurred when the Australian government announced that a condition of its purchases of Airbus' aircraft would be French government backing of increases of access for Australian sheep within the European Community. Cohen & Zysman, *supra* note 17, at 35. Airbus salesmen have also been said to threaten cuts in European imports of tapioca, Thailand's second largest export, if an aircraft order was switched to Boeing. Michael Harrison, *Book Review: Jumbos Scrambling for the Public Trough*, INDEPENDENT, Feb. 25, 1993, at 23 (reviewing IAN MCINTYRE, *JUMBOS SCRAMBLING FOR THE PUBLIC TROUGH*).

126. *Id.* at 18.

127. Article 4 of the Aircraft Code was given the following narrow interpretation by the US/EC Agreement:

As noted above, the Aircraft Code created a restriction on "unreasonable" government pressure tactics in marketing.¹²⁸ This latest Agreement specifically defines what constitutes "unreasonable government pressure" and gives examples.¹²⁹

The Agreement prohibits the use of offset concession demands as a prerequisite for the sale of aircraft.¹³⁰ This is a significant change from the Aircraft Code that expressly allowed such pressure tactics.¹³¹ Offset concession demands were commonplace in the industry as a means to gain technology and jobs for the purchasing nation in exchange for the capital to develop aircraft. Ironically, this was a key tactic the United States used during the infancy of its aircraft industry to establish itself.¹³² Later, the Europeans used this same tactic to solidify adequate technology transfer from the U.S.¹³³ In the 1980s and early 1990s the Pacific rim nations, along with other significant buyers of aircraft, have attempted to use their strong capital position as a means to bring the technology and jobs created from offset concessions to their developing civil aircraft industries. Therefore, while the EC and the United States may no longer demand offset concessions to develop their own industry, the real challenge will arise when the parties try to multilateralize the Agreement and simultaneously place this restriction on those nations with emerging aerospace industries who currently demand concessions.

All participants of signatories in the domestic political decision making process shall not take any action, including but not limited to political representations, pressure or inducements to other governments or foreign airlines

Agreement, *supra* note 6, an. 1. Cf. Aircraft Code, *supra* note 30, art. 4, para. 2, 4.

128. See *supra* notes 114-15 and accompanying text.

129. The Agreement provides:

'Unreasonable pressure' is any action favoring products or suppliers, or which influences procurement decisions in a manner which creates discrimination against suppliers from any other signatory [examples then follow].

Agreement, *supra* note 6, an. 1, art. 4.2.

130. Specifically, the Agreement states: "a signatory may not require that a vendor must provide offset, specific types or volumes of business opportunities or other types of industrial compensation." *Id.* at an. 1, art. 4.3.

131. The Aircraft Code provides:

In conjunction with the approval or awarding of procurement contracts for products covered by this Agreement a Signatory may, however, require that its qualified firms be provided with access to business opportunities on a competitive basis and on terms no less favourable than those available to the qualified firms of other Signatories.

Aircraft Code, *supra* note 30, art. 4, para. 3. This language was specifically reinterpreted in the Agreement to mean merely that a signatory may require that manufacturers not discriminate against the signatory's qualified firms. Agreement, *supra* note 6, an. 1, art. 4.3.

132. United States was a net importer of aircraft technology in the early years of aviation. This helped the American industry close this early technological gap. BLUESTONE, *supra* note 25, at 18.

133. See U.S. DEPARTMENT OF COMMERCE, *supra* note 5, at 78.

3. NEW RULES OF DISCLOSURE: TRANSPARENCY

The Agreement also provides for greater "transparency" of state support. This has been a longtime concern of the United States.¹³⁴ Airbus benefits from unique rules of incorporation under French law. These rules state that Airbus is unable to retain any of its earnings. Thus it is not required to report financial results and is not liable to pay taxes on profits.¹³⁵ In addition, Airbus owns no production facilities. Rather, production work is done under contract to Airbus by the partners. Each contract for production is negotiated separately. The partners do not know the terms of each production subcontract.¹³⁶ As a result of this peculiar system, even Airbus does not know the costs to the individual members.¹³⁷ This makes it all but impossible to determine profitability, since neither profit nor loss from these subcontracting arrangements are disclosed. Further, the Airbus consortium does not publish the amount of profit or loss distributed to its member companies.¹³⁸

As a result of these highly secretive and unorthodox accounting techniques, the United States has been unable to determine the exact amount of direct support member nations have given. It is impossible to tell whether the subcontracting agreements do, in fact, reflect market conditions, as required by the GATT Aircraft Code.

In many respects the Agreement goes farther than earlier efforts to compel the disclosure of some of the manufacturers' financial information. The Agreement contains specific, mandatory notification and reporting requirements, unlike the general GATT provisions.¹³⁹ It requires notification of the amount of government support, planned repayment schedules of such support, annual disbursements and other highly specific data.¹⁴⁰

However, the complexity of Airbus' accounting structure has proved a very real obstacle to the enforcement of the transparency requirements set forth in the bilateral agreement. The publication of detailed accounts for Airbus, which the United States has argued is required by the transparency provisions, was expressly overruled by the ministers of the four

134. Note that this objective was codified into the Omnibus Trade and Competitiveness Act, 19 U.S.C. § 2901(b)(2)(C)(3) (1992).

135. OFFICE OF TECHNOLOGY ASSESSMENT, *supra* note 2, at 353. Every 15 days, Airbus either distributes funds to its members or requests more funds if needed. The members are fully and separately liable for all Airbus activities. *Id.*

136. *Id.*

137. *Id.*

138. *Id.*

139. There is no need to determine if a state enterprise or actionable subsidy is involved. Agreement, *supra* note 6, art. 8.

140. *Id.* at art. 8.

consortium partners.¹⁴¹ While officials claim this noncompliance is simply due to an inability to disentangle Airbus interests from those of the manufacturers,¹⁴² their action appears in direct violation of treaty language.¹⁴³ It therefore appears the next round of disputes may center on enforcement and verification of the Agreement.

4. ENFORCEMENT

While the transparency requirements are highly specific so as to avoid any interpretive arguments between the parties, the overall enforcement mechanisms of the Agreement mirrors the broad, traditional GATT language. As noted earlier, GATT utilizes a flexible approach to dispute resolution.¹⁴⁴ Like the GATT, the Agreement provides for an exception to its provisions in cases where a key manufacturer's financial viability is threatened.¹⁴⁵ It also requires consultation as its main dispute resolution device.¹⁴⁶ Hence, the current Agreement does little to improve on the dispute resolution procedures of the GATT. Instead, it provides that the parties shall propose to incorporate any improvements in dispute settlement procedures agreed to in the Uruguay Round in revisions to the Aircraft Code.¹⁴⁷

5. NEW RULES ON INDIRECT SUBSIDIES

Finally, the Agreement limits indirect government supports to 3% on the value of annual industrywide sales and 4% of the value of each company's annual sales.¹⁴⁸ This provision is a major U.S. concession, since large military spending and NASA research traditionally assist U.S. aircraft producers, while there is less such assistance in Europe.¹⁴⁹ No

141. Simon Beavis, *Airbus Books Stay Shut, Say Ministers*, GUARDIAN, Sept. 9, 1992, at 11.

142. Michael Heseltine, then head of the U.K. Board of Trade claimed, "We have not seen a way which we could publish accounts in a detailed way." *Id.*

143. The actions of the ministers appears to directly violate the Agreement, which states:

The Parties will encourage firms engaged in the manufacture of large civil aircraft to increase the public disclosure of disaggregated financial results of their civil aircraft operations and the adoption of lines of business financial reporting. These disaggregated financial results would at a minimum be expected to include information on sources and uses of funds including specific information on revenue, operating income, net assets, capital investment and government equity infusions.

Agreement, *supra* note 6, art. 8, para. 11.

144. See *supra* note 65 and accompanying text.

145. Agreement, *supra* note 6, art. 9, para. 1. Compare with *supra*, note 66 and accompanying text.

146. Agreement, *supra* note 6, art. 11, para. 1-3. Compare *supra*, note 67 and accompanying text.

147. Agreement, *supra* note 6, art. 12, para. 1.

148. *Id.* at art. 5, para. 1-3.

149. Note that the European efforts at government sponsored civil aeronautical research and development, while supplying research facilities like NASA, have limited beneficial effect, since

such limitation existed under the Aircraft Code.

In reality, however, the foregoing provision will have little effect. The military and NASA have dramatically reduced their spending in areas directly applicable to civil aircraft development since the 1960s.¹⁵⁰ The theory of indirect subsidization was more applicable during America's dominance thirty years ago than today.¹⁵¹ Nonetheless, it continues to provide the EC with political justification for some subsidies, since the U.S. is entitled to some limited subsidization with this provision.¹⁵²

6. THE MULTILATERAL FUNCTION OF THE EC-U.S. AGREEMENT

The current Agreement was negotiated bilaterally, allowing for great concentration on the concerns of the EC and the U.S., the two dominant makers of civil aircraft. Nonetheless, the underlying goal of the accord is to impose the terms of their bilateral compromise onto a multinational playing field. The Agreement provides that both parties shall "make their utmost efforts to ensure that these or similar disciplines are incorporated into the [GATT Aircraft Code]."¹⁵³ Indeed, both parties have taken initial steps to include this bilateral Agreement as a framework for establishing a multilateral accord.¹⁵⁴ Further, the GATT civil aircraft committee has agreed to renegotiate the GATT Aircraft Code as part of the Uruguay Round.¹⁵⁵ The recognized importance of this interest is symbolized by Article 12.3 of the bilateral agreement, which states: "[i]f multilateralization has not yet been achieved in one year, the Parties shall review the question of continued application of this bilateral Agreement."¹⁵⁶ In this

work is often inefficiently duplicated by Germany's Deutsche Forschungsund Versuchsanstalt für Luft- und Raumfahrt (now DLR), Britain's Royal Aircraft Establishment (RAE), and France's Office National d'Etude et de Recherches Aérospatiales (ONERA). OFFICE OF TECHNOLOGY ASSESSMENT, *supra* note 2, at 358.

150. See U.S. CIVIL AVIATION MFG. INDUS. PANEL, COMM. ON TECHNOLOGY AND INT'L ECON. AND TRADE ISSUES, *supra* note 12, at 135-39. By 1983, aeronautical research made up only 5% of NASA's total research and development budget. *Id.*

151. In 1963, civilian aircraft sales represented less than 3% of the dollar sales for the entire aircraft industry. SIMONSON, *supra* note 26, at 227. By 1989, Boeing's military sales represented only 23.4% of revenues; McDonnell Douglas had 55.5% of its revenues from military aircraft and related sales. OFFICE OF TECHNOLOGY ASSESSMENT, *supra* note 2, at 357 (Table 8-5).

152. See *U.S. and EC Sign US/EC Civil Aircraft Agreement and Suggest Renegotiations of GATT Agreement*, EUROPEAN COMMUNITY NEWS (EC Office of Press and Public Affairs, Washington, D.C.), July 20, 1992, ("The Commission considers that the results concerning direct and indirect support are reasonably equivalent.").

153. Agreement, *supra* note 6, art. 12, para. 2.

154. See Frances Williams, *GATT Offered Airliner Subsidy Model*, FIN. TIMES, July 17, 1992, at 5.

155. *GATT States to Renegotiate Civil Aircraft Code*, Reuters (Reuters) (July 16, 1992) (BC Cycle).

156. Agreement, *supra* note 6, art. 12, para. 3.

sense, the driving purpose of the Agreement was to create a bilateral accord for multilateral adoption.

*B. UNIQUE ECONOMICS OF CIVIL AIRCRAFT PRODUCTION NECESSITATE
MULTILATERAL RULES*

For the United States, future expansion of civil aircraft demand rests in foreign markets. Since the 1970s, growth in the U.S. air travel market has been the slowest of all major world regions.¹⁵⁷ Today's U.S. civil aviation market has matured to such an extent that any rise in domestic demand is simply a function of a cyclical need to re-equip aging fleets. The Asian sector is by far the fastest growing aircraft market, since the need for modern transport links has risen dramatically with the area's tremendous economic growth.¹⁵⁸

Communist China and former communist nations may also become larger markets for civil aircraft as costs to develop other modes of modern transportation are higher and completion of construction slower.¹⁵⁹ In all of these markets, however, U.S. manufacturers must face competition from Airbus, as well as Russia,¹⁶⁰ their traditional supplier.¹⁶¹ Hence,

157. See U.S. CIVIL AVIATION MFG. INDUS. PANEL, COMM. ON TECHNOLOGY AND INT'L ECON. AND TRADE ISSUES, *supra* note 12, at 55 (The U.S. has had about 5% annual growth whereas other regions average about 9%).

158. Airbus estimates a constant growth of 7% for the region over the next 20 years, which in turn means a demand for 2,800 additional aircraft. Karl Wilson, *China: Battle for Skies Heats Up*, S. CHINA MORNING POST (Reuter Textline) (Oct. 25, 1992).

159. A 1980 World Bank report notes that air transportation is more important to developing nations than developed countries. Development costs are cheaper and construction time faster than road or rail networks. Charles Barton, *China's Growing Airlines and Aviation Industry*, in JOINT ECONOMIC COMMITTEE, 102D CONG., 1ST SESS., CHINA'S ECONOMIC DILEMMAS IN THE 1990S: THE PROBLEMS OF REFORM, MODERNIZATION, AND INTERDEPENDENCE 469, 472 (S. Print 1990).

160. The Russians have aggressively moved to enter the world civil aircraft market. Aviastar, the leading Russian transport plane producer intends to become the third largest civil aircraft maker, after Boeing and Airbus. The Russian government has allowed up to 50% of the company to be owned by Western investors. Low wage costs, coupled with a relatively modern plants already in place, support the Russian claim that its costs to produce aircraft are 20-25% lower than Western rivals. Peter Gregson, *Russian Aircraft Maker Bids to Break into Global Market*, Reuter Library Report, (Reuters) (Oct. 6, 1992) (BC Cycle).

Realizing this advantage, 18 U.S. firms contributed to Aviastar's first civil jetliner to be introduced on the world market. The new Russian challenge, the 311 seat Ilyushin IL-96M, has already been rolled out to the public and is expected to enter service in 1995. Leyla Boulton and Paul Betts, *Co-operation Lifts Russian Aero-industry — The Fruits of International Links*, FIN. TIMES, Mar. 30, 1993, at 10.

161. For example, Chinese civilian transport needs are expected to demand an additional 500 aircraft in the near future. Its civilian aerospace demand is the highest growth rate in the world. Wilson, *supra* note 156. While China has greatly expanded its domestic production capacity through foreign offset concessions, its infrastructure was built by Russia in the 1950s, and continues to have a fleet partially composed of Soviet-built aircraft. See Barton, *supra* note 159,

while the United States remains the largest civil aircraft market, its makers must look to other areas of the world for the best opportunities to sell new planes.

The Asian nations, generally rich with capital, have demanded offset concessions as a precondition to civil aircraft purchases.¹⁶² As a result, the U.S. producers are under tremendous pressure to accept such conditions. The loss of military orders from the end of the Cold War, coupled with huge development costs,¹⁶³ make U.S. makers dependent on such financing.¹⁶⁴ The recent increase in Exim bank financing,¹⁶⁵ while helpful, has not effectively lessened the need to look internationally for financing of new aircraft development.¹⁶⁶

Large costs have not only increased financing pressures, but questions are now being raised as to the economic feasibility of large civil aircraft development and production without government assistance. The U.S. aerospace industry's return on sales and assets is significantly below the average of the total manufacturing base in the country.¹⁶⁷ These high initial costs and the unpredictable nature of future demand make the development of new aircraft a tremendously high risk venture.¹⁶⁸ One

at 469, 473-74. Russia has established barter arrangements in China, leasing former Aeroflot aircraft. Wilson, *supra* note 158.

162. Japan, for example, has taken advantage of offset agreements, giving it a 15% share of production in the 767, and supplied various component parts for the 737, 747, 757, DC-10, and the L-1011. U.S. DEPARTMENT OF COMMERCE, *supra* note 5, at 71-72. If the United States continues to pressure Japan to assume more of the burden of its defense, surely the civil aircraft industry in that nation will expand further as a result of greater government research and involvement. See Cohen & Zysman, *supra* note 17, at 40-41.

163. For example, the Boeing 777, its latest model, is estimated to cost over \$5 billion in development, more than three times the \$1.2 billion required to develop the 747. OFFICE OF TECHNOLOGY ASSESSMENT, *supra* note 2, at 343 (Table 8-2).

164. One industry insider told a House Foreign Affairs Subcommittee on Economic Policy and Trade: "No major commercial aerospace program today can be launched without some form of international collaboration—the costs and risks are too high." *Aircraft Executives Urge Government "Cooperation"*, Int'l Trade Daily (BNA), Aug. 10, 1992.

165. Exim's loan authority has dramatically increased from \$3.8 billion in 1983 and 1984. That figure represented almost the same amount of financing the Bank had supported in the previous 20 years. U.S. DEPARTMENT OF COMMERCE, *supra* note 5, at 94. Today, Exim is anticipated to require \$14.5 billion in 1993. *Civil Aircraft Needs Continued Coverage Under Subsidies Code, U.S. Industry Says*, 9 Int'l Trade Rep. (BNA) Aug. 12, 1992.

However, some in the aircraft industry fear increases in Exim financing may soon level off. USA: *Exim Cuts and Runs — New Aircraft Financing to be Limited*, AIRLINE BUSINESS (Reuter Textline), Mar. 1, 1993.

166. Even Boeing, which has traditionally been described as a "go-it-alone" company, has now publicly invited more global collaboration. It recently established agreements with three Japanese aerospace companies for its super-jumbo project. Paul Betts, *Boeing to Open Itself to Wider Global Collaboration*, FIN. TIMES, Sept. 2, 1992, at 18.

167. U.S. CIVIL AVIATION MFG. INDUS. PANEL, COMM. ON TECHNOLOGY AND INT'L ECON. AND TRADE ISSUES, *supra* note 12; at 66-67.

168. This reality has led some to conclude that "launching a new large transport is equivalent

analyst claimed that since 1982, less than 10% of all commercial jets developed have been profitable ventures.¹⁶⁹ Recovery of the initial capital requirements of launching a new aircraft typically requires 10 to 15 years.¹⁷⁰ This history, coupled with increased financing demands, and a tougher battle for ever-diminishing market share makes an unregulated world market a threat to the entire industry. The implication of greater competitiveness in the world marketplace could be devastating for all producers.¹⁷¹

If more competition ensues, makers may be less willing to enter certain markets for fear that its potential market share is too small to sustain profitability. Thus subsidies will, more than ever, tilt the balance of power in the field of civil aviation. If such unfair competitive advantages continue in other parts of the world, the U.S. will have to increase spending on the Exim bank even further to protect the industry from unfair financing.¹⁷² Otherwise, its only option is to place protective tariffs on foreign products, which would cripple an industry increasingly dependent on export sales. Hence, it is in the interest of both the United States and Europe to multilateralize the current agreement to establish a level playing field, not only amongst themselves, but to ward off any unfair competition from other emerging aerospace nations.

to betting the company on a high risk project for a rate of return that could be realized from investment alternatives with much lower risks." U.S. DEPARTMENT OF COMMERCE, *supra* note 5, at 58.

The launch of both the 747 and the DC-10 represented development costs over three times greater than the entire capitalization of their respective companies. OFFICE OF TECHNOLOGY ASSESSMENT, *supra* note 2, at 343.

169. Specifically, the study found that only two of twenty-two commercial aircraft developed had been profitable, the Boeing 707 and 727. John Newhouse, *A Reporter at Large. A Sporty Game III: Big, Bigger, Jumbo*, NEW YORKER, June 28, 1982, at 58. See also *Aerospace Survey*, ECONOMIST, Aug. 30, 1980, at 5-22 (it found only three profitable commercial jets, the Boeing 707, 727, and the McDonnell Douglas DC-8). By 1991, only four planes were considered profitable, with a fifth model close to profitability. OFFICE OF TECHNOLOGY ASSESSMENT, *supra* note 2, at 342 & n.6.

170. U.S. CIVIL AVIATION MFG. INDUS. PANEL, COMM. ON TECHNOLOGY AND INT'L ECON. AND TRADE ISSUES, *supra* note 12, at 58. See also U.S. DEPARTMENT OF COMMERCE, *supra* note 5, at 24 ("A successful aircraft project, [] is unlikely to achieve the breakeven point . . . at best, until 12 years or so after the project is initiated.').

171. The presence of Airbus alone is estimated to have forced Boeing to lower its pricing of comparable aircraft by 40%. Richard Baldwin & Paul Krugman, *Industrial Policy in Wide-Bodied Jet Aircraft*, in TRADE POLICY ISSUES AND EMPIRICAL ANALYSIS 45, 68 (Richard E. Baldwin, ed., 1988). The results of the empirical study hint that the world market cannot support more than two makers producing aircraft that are close substitutes in demand, and perhaps could only support one without government intervention. *Id.* at 71.

172. Exim's loan authority has dramatically increased from \$3.8 billion in 1983 and 1984. That figure represented almost the same amount of financing the Bank had supported in the previous 20 years. U.S. DEPARTMENT OF COMMERCE, *supra* note 5, at 94. Today, Exim is anticipated to require \$14.5 billion in 1993. *Civil Aircraft Needs Continued Coverage Under Subsidies Code*, U.S. Industry Says, 9 Int'l Trade Rep. (BNA) No. 33, at 1386 (Aug. 12, 1992).

IV. CLINTON'S UNCERTAIN APPROACH TO THE AIRBUS DISPUTE

The Clinton Administration has led many to believe the bilateral Agreement may quickly be unravelling. On February 25, 1993, the United States formally requested "consultations" with the European Community.¹⁷³ Technically, these consultations are to take place biannually under the terms of the Agreement,¹⁷⁴ but due to "technical reasons", the two sides had not yet met.¹⁷⁵ The administration has been criticized by Brussels for displaying a "good-cop, bad cop"¹⁷⁶ strategy on trade issues.

For example, in defending its position that consultations were needed, the White House replied, "there have been some discrepancies over the amount of subsidies that have gone to Airbus and how you count the direct and indirect subsidies, and a lot of people make a very strong case that some of the subsidies may, in some way, be improper."¹⁷⁷ These comments came just two days after the EC External Economic Affairs Commissioner, Sir Leon Brittan, issued a statement acknowledging he had received "assurances [that] the administration does not intend to reopen the Airbus agreement."¹⁷⁸ Those assurances were prompted by President Clinton's remarks the previous day that "we're going to try to change the rules of the game."¹⁷⁹

Regardless of whether the intent of such maneuvering was to renew the trade controversy, clearly U.S. allegations of EC impropriety were the catalyst to recent EC allegations of U.S. impropriety. Specifically, the EC alleges possible U.S. violations of caps on indirect subsidies.¹⁸⁰

Additionally, the EC notes that while it has already sent a proposal to the GATT for transforming the bilateral agreement into a revised multilat-

173. *United States asks EC Commission for Consultations on Airbus Pact*, Int'l Trade Rep. (BNA) Mar. 3, 1993.

174. Agreement, *supra* note 6, art. 11, para. 1.

175. *United States asks EC Commission for Consultations on Airbus Pact*, Int'l Trade Rep. (BNA) Mar. 3, 1993.

176. See Tom Buerkle, *EC Summons U.S. to Clarify its Position in Trade Feud, Washington Approach 'Good Cop, Bad Cop' is Decried by Brussels*, INT'L HERALD TRIB. (Mar. 18, 1993); Lyndsay Griffiths, *Jekyll-and-Hyde U.S. Trade Policy has Allies Worried*, Reuters Asia-Pacific Bus. Rep. (Reuters) Mar. 8, 1993.

177. *United States Asks EC Commission for Consultations on Airbus Pact*, Int'l Trade Rep. (BNA) March 3, 1993 (quoting remarks made by White House Communications Director George Stephanopoulos on Feb. 25, 1993).

178. *Id.* (quoting Feb. 23, 1993 statement of EC External Affairs Commissioner, Sir. Leon Brittan).

179. *United States Asks EC Commission for Consultations on Airbus Pact*, Int'l Trade Daily (BNA) Mar. 1, 1993 (quoting the Feb. 22, 1993 remarks of President Clinton).

180. Specifically, Sir Leon Brittan said that "'very possibly the U.S. may be exceeding the authorized level of indirect subsidies.'" *EC Will Seek Clarifications from U.S. on Airbus During Meeting Later this Month*, Int'l Trade Daily (BNA) Mar. 18, 1993.

eral code, the U.S. has failed to send a proposal or comment on the EC draft.¹⁸¹ Despite this record, the Clinton Administration continues to make public statements in support of a multilateral agreement.¹⁸²

Realizing the great potential for a trade war in this area, both sides have left some room for the other to maneuver, while at the same time continuing to profess compliance with the bilateral agreement. The consultations were preceded by tough talk from both sides. The EC threatened to issue a formal complaint with the GATT regarding the tax concessions given to U.S. export trading companies in civil aerospace¹⁸³ as well as challenging the U.S. to consent to international arbitration on the issue.¹⁸⁴ The U.S. heightened tensions with the introduction of two bills in Congress. The Civil Aircraft Trade Enforcement Act of 1993,¹⁸⁵ if passed, will formally initiate a countervailing duty investigation regarding Airbus' production of civil aircraft. This is certainly contrary to the industry's wishes, since it could jeopardize American joint ventures and customers in Europe.¹⁸⁶ Additionally, the Aeronautical Technology Consortium Act of 1993 was introduced.¹⁸⁷ If passed, this act would provide more direct financial assistance to aircraft manufacturing companies, as well as greater governmental coordination and financial assistance in the research and development of civil aircraft. In effect, these two bills set the stage for renunciation of the bilateral agreement and a large and expensive subsidies battle.

Realizing the increasing potential of a trade war and renunciation of the Agreement, the two sides toned down their rhetoric during the formal consultation period and, at the time of this writing, both sides appear to be

181. *Id.*

182. Specifically, Mickey Kantor, the U.S. Trade Representative, said he wants "further improvement of rules in government support to aircraft through multilateral negotiations in the GATT aircraft code." *Kantor Sees Problems Ahead with Europe, Japan, China*, Reuter European Community Report (Reuters, Ltd.) Mar. 7, 1993 (BC cycle). See also *EC Official Says Aircraft Talks Should Lead to a Less Contentious Period*, Int'l Trade Daily (BNA) Apr. 2, 1993 (U.S. official stating "both sides 'are looking to implement the agreement and to multilateralize [sic] it.'").

183. *EC Expects to Initiate Complaint against U.S. Aircraft Manufacturers*, WORLD AIRLINE NEWS (Phillips Bus. Info., Inc.) Mar. 29, 1993.

184. Boris Johnson, *Brittan's New Trade Threat to America*, DAILY TELEGRAPH, Mar. 18, 1993, at 13.

185. S. 418, 103d Cong. 1st Sess. (1993).

186. Paul Maidment, *Does Airbus Cheat? Does Boeing*, NEWSWEEK, Mar. 8, 1993, at 44.

187. S. 419, 103d Cong., 1st Sess. (1993).

The Clinton Administration has sent mixed signals as to whether it fully supports such increased direct subsidization as proposed by this bill. Compare Jeff Cole, *U.S. May Try to Stop Airbus From Using 'Walkaway' Leases*, WALL ST. J. A3, Mar. 22, 1993, at A8 ("Vice-President Al Gore has said he considers the creation of a research consortium aiding aerospace companies to be a top priority.") with *Clinton urged to veto subsidy bills*, FIN. TIMES, Apr. 2, 1993, at 8 ("[the Administration will] inform Congress where it believed legislation was contrary to other trade commitments.").

willing to recognize an informal "cooling off" period.¹⁸⁸ For its part, the Clinton Administration acknowledged doubts about the proposed legislation, promising to eliminate language in the legislation contrary to existing trade commitments.¹⁸⁹ Additionally, the Administration has provided reassurance that it has no plans to withdraw from the Agreement.¹⁹⁰ The EC has backed off as well, stating the consultations should "lead to a less contentious period."¹⁹¹ The issue may heat up again in the summer of 1993, since under the terms of the Agreement, neither party can request to withdraw from the treaty until one year has expired.¹⁹² Even if a party decides to withdraw, the Agreement remains valid for an additional year after an expression of such intent.¹⁹³

V. CONCLUSION

The bilateral agreement's potential multilateral implications for the United States, the European Community, and the world trade of aircraft are enormous. Effective multilateralization of the accord would have a positive effect on U.S. trading interests.

First, U.S. civil aircraft makers have used the export market as a means to expand demand, overcome any downturns in the domestic market, and improve their capital position to develop new technology. If restraints on international subsidies are not put in place, foreign buyers may choose to finance the development of their own civil aircraft industry rather than looking to the United States to purchase aircraft.

Second, the emergence of new producers threatens the ability of existing U.S. makers to maintain profitability, since a high percentage of market share is needed to offset the large development costs inherent to the industry. It is essential that the Agreement be expanded internationally. Entry of new, heavily subsidized makers on the world market, immune to the financial risks inherent to the industry, could force further consolidation of the world's aircraft makers. If multilateralized, the provi-

188. See e.g., Sarah Lambert, *America and Europe Call Truce in Trade War*, INDEPENDENT, Mar. 30, 1993, at 23; *EC Official Says Aircraft Talks Should 'Lead to a Less Contentious Period'*, Int'l Trade Daily (BNA) Apr. 2, 1993; *EC: Consultations on Aid to Civil Aeronautics Confirm Willingness by both EC and U.S. to Abide by 1992 Accord*, AGENCE EUROPE (Reuter Textline) (Apr. 3, 1993).

189. *Clinton Urged to Veto Subsidy Bills*, FIN. TIMES, Apr. 2, 1993, at 8.

190. *EC: Consultations on Aid to Civil Aeronautics Confirm Willingness by both EC and U.S. to abide by 1992 Accord*, AGENCE EUROPE (Reuter Textline) April 3, 1993 ("it is now clear [after the consultations] that the Clinton Administration does not intend putting the accord into question.").

191. *EC Official Says Aircraft Talks Should 'Lead to a Less Contentious Period'*, Int'l Trade Daily (BNA) (Apr. 2, 1993).

192. Agreement, *supra* note 6, art 13, para. 3.

193. *Id.*

sions of the treaty would protect against this competition, by providing a legal tool to prevent heavily subsidized new makers of competitive aircraft from entering the world market.

Finally, the Agreement would continue to provide a legal tool to insure an end to perceived unfair trade practices of the European Community in this area.

Similar interests of the European Community would also be furthered by multilateralization of the bilateral agreement. They too are threatened by emerging, unregulated competitors. At the same time, the Agreement would continue to provide a policing mechanism for the EC to oversee indirect government financing in the U.S.

Recognizing a common interest in maintaining their combined stronghold on the international civil aircraft market,¹⁹⁴ both the U.S. and the EC have actively encouraged greater involvement of the emerging aerospace nations with the Agreement.¹⁹⁵ The survival of the U.S. and the EC aircraft industries surely depends on each maker maintaining stable market share. New entrants in the world market mean not only lower profits for both industries, but may mean the potential destruction of an essential industry to both Europe and the United States.

Continued unregulated, subsidized competition could foreclose the opportunity for any one maker to profitably sell aircraft without government supports. Without international safeguards, the threat of an international subsidies war looms large.

EPILOGUE

The threat of an international subsidies war has increased dramatically since the completion of the above article. The failure to include a civil aircraft provision to the Uruguay Round of GATT negotiations¹⁹⁶ casts a shadow of uncertainty as to what legal standards will apply to the

194. The United States and the European Community delivered 95% or better of the world civilian aircraft from 1978-1989. GENERAL ACCT. OFF., HIGH-TECHNOLOGY COMPETITIVENESS: TRENDS IN U.S. AND FOREIGN PERFORMANCE, 53 (1992).

195. For example, in July 1992 representatives from the US, EC, Japan and 10 other countries met along with representatives from the Japanese Ministry of International Trade and Industry (MITI) in the hopes of creating international guidelines regarding government subsidization of civilian aircraft development. *Meeting to Discuss Aircraft Subsidy Rules About to Begin*, REPORT FROM JAPAN (Yomiuri News Service) (July 10, 1992).

South Korea, despite only a small aerospace industry, was invited by the United States to take part as an observer in the multilateral negotiations associated with the Agreement since it has an active policy of government subsidies. *South Korea: Efforts to Enter Aircraft Industry Encounter Difficulties*, KOREA ECONOMIC DAILY, (Reuter Textline), Sept. 26, 1992.

196. *EC Commissioner Cites Successes in Uruguay Round Negotiations*, Int'l Trade Daily (BNA) (Dec. 17, 1993).

industry in the future. As noted above,¹⁹⁷ the express purpose of the Agreement was to facilitate a multilateral set of rules in the Uruguay Round of GATT negotiations. The failure to multilateralize a new agreement on civil aircraft means that the bilateral Agreement still represents the legal instrument with the most specific language to combat claims of improper subsidies in the United States and the European Community. Further, it remains an important model for future multilateralization efforts. Despite the recent political setback, efforts to multilateralize the Agreement should continue, since legal concessions granted to the Europeans as part of the Uruguay Round will expire at the end of 1994 should no new aircraft code emerge.¹⁹⁸

In the meantime, however, the actions of both the United States and the European Community represent an open affront to current legal instruments. The European Parliament, acknowledging the economic pressures for international cooperation and integration, has called for a central industrial strategy for the Europe's aircraft manufacturing sector, including a call for direct subsidies.¹⁹⁹ At the same time, member states such as France and Germany have now called for increased *indirect* subsidies.²⁰⁰ These political moves imply potential violations of the Agreement's ban on future production subsidies and caps on indirect subsidies.²⁰¹

The United States, under the Clinton administration, has furthered its early tactic of sending mixed signals regarding its intention to uphold the Agreement. On the one hand, the administration immediately sought refuge in the language of the Agreement as an adequate safeguard shortly after the failure of the Uruguay Round of the GATT to adopt a new aircraft code.²⁰² On the other hand, the President of the United States personally undertook the role of aircraft salesman by calling King Fahd of Saudi Ara-

197. See *supra*, note 156 and accompanying text.

198. The EC successfully negotiated two footnotes exempting subsidies for large civil aircraft from the newly negotiated GATT Subsidies Code. First, the agreement upholds the legality of development loans which are not repaid because of slow sales. Second, the general rule that a maker has the burden of proof to show a subsidy is fair if the subsidy accounts for more than 5% of the product's value will not apply to aircraft makers. *Post - GATT Talks Face Deadline for 'Tailor Made' Aviation Code*, AVIATION EUROPE (McGraw-Hill, Inc.) (Dec. 23, 1993).

199. *European Parliament Calls for Strategy to Help Aircraft Sector Manufacturers*, Int'l Trade Daily (BNA) (Dec. 16, 1993).

200. *French manufacturers Urge Indirect Subsidies*, Int'l Trade Daily (BNA) (Jan. 5, 1994); *DASA proposes 'crisis' plan*, Flight International (Reed Bus. Pub.) (Jan. 26, 1994). Cf. *Airbus Industrie Calls for Indirect Aid System in Europe*, Les Echos (Reuter Textline) (Jan. 28, 1994); *Europe Should Follow U.S. Example in Financing Aircraft Development*, Int'l Trade Daily (BNA) (Jan. 31, 1994).

201. See *supra*, notes 109, 148-52 and accompanying text.

202. *U.S. Pledges Strict Monitoring of Bilateral Airbus Agreement*, AFX News (AFX-Extel News, Ltd.) (Jan. 7, 1994).

bia and encouraging him to buy American-made aircraft for the state-run airline, soon after rolling back Saudi military debts, and then by the President himself announcing the completion of the aircraft deal.²⁰³ Additionally, the United States allowed Kazakhstan its first purchase of Western civil aircraft "immediately after signing of a commercial agreement".²⁰⁴ These incidents demonstrated a blatant affront to Article IV of the Aircraft Code and the Annex of the Agreement, prohibiting the use of government pressure to induce purchase agreements.²⁰⁵ Because of these actions, the Aircraft Code and the Agreement have taken on great importance as legal tools for European retaliation.²⁰⁶

Both sides continue to recognize the importance of multilateralizing the Agreement despite their respective shortfalls in upholding the spirit of the Agreement.²⁰⁷ The civil aircraft industry is facing the toughest economic climate in its history.²⁰⁸ As the financing and development pressures increase, so too does the need for international rules on subsidies in civil aircraft. Without a legal framework to control these pressures, the United States and the European Community run the continued risk of wild government involvement in the industry.

203. *Airbus Asks if U.S. 'Inducements' Over Saudi Plane Order Broke Rules*, GUARDIAN, Feb. 18, 1994, at 17. Political influence regarding the Saudi aircraft purchase can be traced at least as far back as May, 1994, when the undersecretary for international trade acknowledged the direct involvement of the Secretary of Commerce lobbying Saudi officials for the sale. *Competitiveness of the Aerospace Industry and S. 419: Hearing before the Committee on Commerce, Science and Transportation of the United States Senate*, 103d Cong., 1st Sess., 26 (1993).

204. *Airbus Chief Hits at "Contracts Between States" in Saudi Plane Deal*, Agence France Presse (Agence France Presse) (Feb. 22, 1994).

205. See *supra*, notes 99-101, 130-131 and accompanying text.

206. E.g., *Airbus Could Appeal to GATT on Boeing Contract in Saudi Arabia*, Euro. Rep. (Euro. Info. Svc.) (Feb. 19, 1994); *Airbus Suggests U.S.-Saudi Deal on Airplane Buy May Violate GATT*, Int'l Trade Daily, (BNA) (Feb. 22, 1994).

207. *French Partner in Airbus Sees Future Disputes if Talks Fail*, Int'l Trade Daily (BNA) (Jan. 6, 1994); *U.S. Pledges Strict Monitoring of Bilateral Airbus Agreement*, AFX News (AFX-Extel News, Ltd.) (Jan. 7, 1994).

208. *Struggling to Get Back in the Air - Manufacturing in Civil Aviation*, ENGINEER (Reuter Textline) (Jan. 20, 1994).

