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The WTO *EC - Aircraft* Panel and Appellate Body Reports on Subsidies to Airbus

By Simon Lester



Introduction

The WTO dispute in *EC—Aircraft* (DS316)[1] has been both lengthy (six years from the first consultations request to the circulation of the Appellate Body report) and complex (in terms of both legal and factual issues). This *Insight* provides a brief overview of the issues involved in the panel and appellate

proceedings.

Factual Background

In this dispute, the United States challenged the legality of alleged subsidies by the European Union and certain member States to the various Airbus companies under the WTO Agreement on Subsidies and Countervailing Measures ("SCM Agreement"). The U.S. complaint alleged "more than 300 separate instances of subsidization, over a period of almost forty years, by the European Communities and four of its member States, France, Germany, Spain and the United Kingdom, with respect to large civil aircraft ('LCA') developed, produced and sold by the company known today as Airbus SAS." [2] The Panel grouped these measures into five general categories:

- "Launch Aid" / Member State Financing ("LA/MSF"): Provision by France, Germany, Spain, and the United Kingdom of financing to the Airbus companies for large civil aircraft design and development. The United States alleged that this financing provides benefits to the recipient companies, such as below-market interest rates and a repayment obligation that arises only if sales are successful.
- *Design and Development Financing Loans*: Provision by the European Communities and the member States of financing through the European Investment Bank ("EIB") to the Airbus companies for large civil aircraft design,

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development, and other purposes.

- *Infrastructure and Related Grants*: Provision by the European Communities and the member States of financial contributions to develop, expand, and upgrade facilities and other infrastructure for the Airbus companies.
- *Corporate Restructuring Measures (Debt Forgiveness, Equity, and Grants)*: Assumption and forgiveness by the European Communities and the member States of debt resulting from Launch Aid and other financing for large civil aircraft development and production; and provision by the European Communities and the member States of equity infusions and grants, including through government-owned and government-controlled banks.
- *Research and Development*: Provision by the European Communities and the member States of financial contributions for aeronautics-related research, development, and demonstration undertaken by Airbus, whether alone or with others, or in any other way to the benefit of Airbus.

The product at issue is large civil aircraft (“LCA”) (as distinguished from smaller (regional) aircraft and military aircraft). LCA are generally described as large (weighing over 15,000 kilograms) “tube and wing” aircraft, with turbofan engines carried under low-set wings, designed for subsonic flight. LCA are designed for transporting hundred or more passengers and/or a proportionate amount of cargo.

In terms of the companies in the industry, LCA are presently produced only by Boeing (a U.S. company) and Airbus (a European company), which both sell a range of LCA models world-wide. Both companies engage in continued development of LCA, which requires significant up-front investments over a period of three to five years before any revenues are obtained.

As the Panel explained, before 2001, no single legal entity produced Airbus LCA. Airbus LCA were produced by a consortium of French, German, Spanish, and (from 1979) United Kingdom aerospace companies (the Airbus partners), operating in a form of partnership arrangement through the French entity Airbus GIE. In 2000, the Airbus partners consolidated their LCA-related activities under the European Aeronautic Defence and Space Company, EADS N.V. (EADS): each of the French, German, and Spanish Airbus partners placed its Airbus-related design, engineering, manufacturing, and production assets and activities into legal entities that would become wholly owned subsidiaries of the newly formed EADS, in return for shares in EADS representing the agreed values of the Airbus partners’ corresponding contributions. In 2001, EADS and Airbus’ British partner BAE Systems placed their Airbus-related assets and operations and their membership rights in Airbus GIE under the common control of a newly-created holding company, Airbus SAS. Finally, in 2006, EADS purchased BAE Systems’ twenty percent interest in Airbus SAS, and Airbus SAS became a wholly-owned subsidiary of EADS.[3]

The Claims

The U.S. claims fell into two categories:

- Claims that the challenged *LA/MSF* measures are *prohibited export subsidies* within the meaning of SCM Agreement Article 3.1(a);[4] and
- Claims that each challenged measure is a specific subsidy within the meaning of SCM Agreement Articles 1 and 2, and that the European Communities and the four member States, through the use of these subsidies, caused *adverse*

Boeing

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effects to U.S. interests under the SCM Agreement. The adverse effects claims involved allegations of both “injury” under Article 5(a) and serious prejudice under Articles 5(c) and Article 6.3.[5]

The Panel's Rulings

Adverse effects claims: The SCM Agreement only applies to “specific subsidies,” so the initial issues confronting the Panel were: (1) Is there a subsidy (a “financial contribution” by government or a public body that confers a “benefit”)? And (2), if so, is it “specific” (as opposed to generally available)?

With regard to “financial contribution,” the Panel focused on issues of *direct and potential direct transfers of funds* under Article 1.1(a)(1)(i) and *provision of goods and services “other than general infrastructure”* under Article 1.1(a)(1)(iii). Past cases have established that a “benefit” exists if government financial contributions are provided on terms more favorable than those available on the market[6]—and the Panel here considered whether that was true in this instance.

Article 2 provides that subsidies are “specific” if, *inter alia*, they go to “an enterprise or industry or group of enterprises or industries.” Here, the Panel focused on *de jure* specificity under Article 2.1(a), *de facto* specificity under Article 2.1(c), and regional specificity under Article 2.2.

For those subsidies found to be specific,[7] the Panel then considered whether the United States had demonstrated the existence of “adverse effects” as defined by SCM Articles 5 and 6, examining in particular the following “serious prejudice” issues:

- Article 6.3(a) - Displacement and Impedance in the EC Market;
- Article 6.3(b) - Displacement and Impedance in Third Country Markets;
- Article 6.3(c) - Price Undercutting;
- Article 6.3(c) - Price Depression;
- Article 6.3(c) - Price Suppression; and
- Article 6.3(c) - Lost Sales.

The Panel considered first whether serious prejudice exists; and then, separately, whether this serious prejudice has been caused by the subsidies. Ultimately, the Panel found that the subsidies caused the following types of serious prejudice: Displacement in the EC Market; Displacement in Third Country Markets; and Lost Sales.[8] The Panel rejected claims under Article 5(a) related to injury and threat of injury made as part of an additional U.S. “adverse effects” claim.[9]

Export subsidies: The Panel found that some instances of LA/MSF constituted export subsidies, whereas others did not.[10] In the context of reaching this conclusion, the Panel set out what it considered to be the correct interpretation of the *de facto* export contingency legal standard. In this regard, it said that “a subsidy may be found to be contingent *in fact* upon *anticipated* export performance, and therefore prohibited under Article 3.1(a), when there is evidence demonstrating the existence of three distinct elements: (i) the granting of a subsidy; (ii) that is tied to; (iii) anticipated exportation or export earnings.” The Panel noted that “[a]t the heart of this legal standard is the second element, which reflects the notion of contingency set out in Article 3.1(a).” The meaning of “contingent” in Article 3.1(a) is “conditional” or “dependent for its existence upon,” and thus in order to qualify as a prohibited export subsidy, the grant of the subsidy “must be *conditional* or *dependent*

upon actual or anticipated export performance.” In this regard, the Panel explained that under this standard, “a subsidy must be granted *because* of actual or anticipated export performance.”^[11]

The Appellate Body's Rulings

The EU filed a notice of appeal^[12] alleging various errors in relation to the Panel's findings of violation, as well as on some systemic issues. In addition, the United States filed a notice of other appeal,^[13] alleging errors related to certain claims that had been rejected.

On appeal, the Appellate Body reversed some of the Panel's findings and upheld others. In some instances where it reversed the Panel's findings, it was able to complete the legal analysis and make a finding of its own. In others, it was not.

Adverse Effects: The Appellate Body modified and reversed several of the Panel's findings on adverse effects, but it upheld the broad thrust of these findings: a large number of the EU subsidies at issue, including LA/MSF, had caused adverse effects, in the form of “serious prejudice,” to U.S. interests. In particular, this serious prejudice here was the “displacement” and “lost sales” experienced by Boeing in various markets.^[14]

Export Subsidies: The Appellate Body reversed the Panel's legal interpretation on *de facto* export contingency. Rather than focusing on whether a subsidy is granted “*because of*” actual or anticipated export performance, the Appellate Body said the standard should involve looking at whether the subsidy creates an incentive to export as compared to selling domestically. As the Appellate Body stated:

Where the evidence shows, all other things being equal, that the granting of the subsidy provides an incentive to skew anticipated sales towards exports, in comparison with the historical performance of the recipient or the hypothetical performance of a profit-maximizing firm in the absence of the subsidy, this would be an indication that the granting of the subsidy is in fact tied to anticipated exportation within the meaning of Article 3.1(a) and footnote 4 of the SCM Agreement.^[15]

Having reversed the Panel's legal interpretation, the Appellate Body was unable to complete the analysis to determine whether any of the particular LA/MSF subsidies at issue constitute an export subsidy.^[16]

As a result, the legal status of these subsidies is uncertain. There is simply no finding on whether any such measures are export subsidies, and such a finding could only be made if a new proceeding were brought.

In addition to these findings, the Panel and Appellate Body also considered a number of important issues of systemic interest, including the following: the proper consideration of the “subsidized product” and the product markets; the issue of “extinguishing” subsidies through sale of the subsidized company or similar events; the role of non-WTO legal instruments in interpreting WTO rules; how to evaluate subsidies granted many years before a dispute; and the appropriate method of appealing issues involving application of the law to the facts.

Implementation

A great deal of uncertainty remains as to how these rulings will be implemented and the impact this will have on future EU subsidies to Airbus. In this regard, one key overarching issue was whether “Launch Aid” could be challenged as a “program,” beyond the individual instances of financing that had been undertaken for specific Airbus planes. The Panel had found that the United States did not prove that such a “program” existed.^[17] The United States appealed this finding. On appeal, the Appellate Body found that the panel request (which defines the scope of the claims in a WTO dispute) did not properly identify Launch Aid as a measure subject to challenge—and so the U.S. challenge to Launch Aid as a program was outside the scope of this dispute.^[18] Arguably, this result is an important setback for the United States in terms of achieving fundamental changes to future Launch Aid, as it may make enforcement of these rulings in relation to new Launch Aid financing more difficult.

In addition, there is the more general question of how compliance with these rulings will be achieved. The rulings do not find that Launch Aid is *per se* illegal under the SCM Agreement. Rather, they simply find that the way these particular instances of Launch Aid were carried out violated the rules. The practical question becomes, how can the EU modify future Launch Aid so as to comply with the rules? In all likelihood, the parties will have strong disagreements as to what is required, and this will provide the next battleground for the dispute (along with the related complaint against alleged subsidies to Boeing, *United States—Measures Affecting Trade in Large Civil Aircraft (Second Complaint)* (DS353), which is currently in the appeal stage).

About the Author:

Simon Lester, a former Legal Affairs Officer at the Appellate Body Secretariat of the World Trade Organization, has taught courses on international trade law at American University's Washington College of Law and the University of Michigan Law School. He is co-founder of WorldTradeLaw.net.

Endnotes:

[1] *European Communities and Certain Member States—Measures Affecting Trade in Large Civil Aircraft*.

[2] Panel Report, *European Communities and Certain Member States—Measures Affecting Trade in Large Civil Aircraft*, ¶ 7.1, WT/DS316/ (June 30, 2010) [hereinafter Panel Report, *EC—Aircraft*].

[3] *Id.* ¶¶ 2.1-5, 7.1, 7.183, 7.619-623, 7.1716-1728; Appellate Body Report, *European Communities and Certain Member States—Measures Affecting Trade in Large Civil Aircraft*, ¶¶ 573-632, WT/DS316/AB/ (May 18, 2011) [hereinafter Appellate Body Report, *EC—Aircraft*].

[4] Panel Report, *EC—Aircraft*, ¶ 3.1(a).

[5] *Id.* ¶ 3.1(b).

[6] Appellate Body Report, *Canada—Measures Affecting the Export of Civilian Aircraft*, ¶ 157, WT/DS70/AB/R (Aug. 2, 1999).

[7] The EIB financing was the only category of measures not found to be specific subsidies.

[8] Panel Report, *EC—Aircraft*, ¶ 7.2025.

[9] *Id.* ¶ 7.2186.

[10] *Id.* ¶ 7.689.

[11] *Id.* ¶ 7.648.

[12] Revision to the Notification of an Appeal by the European Union, *European Communities and Certain Member States—Measures Affecting Trade in Large Civil Aircraft*, WT/DS316/12/Rev.1 (Aug. 17, 2010).

[13] Notification of an Other Appeal by the United States, *European Communities and Certain Member States—Measures Affecting Trade in Large Civil Aircraft*, WT/DS316/13 (Aug. 20, 2010).

[14] Appellate Body Report, *EC—Aircraft*, ¶¶ 1105-1413.

[15] *Id.* ¶ 1047; and, more generally, ¶¶ 1040-1055.

[16] *Id.* ¶¶ 1085-1101.

[17] Panel Report, *EC—Aircraft*, ¶¶ 7.576-580.

[18] Appellate Body Report, *EC—Aircraft*, ¶¶ 778-796.