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UNITED STATES - CONDITIONAL TAX INCENTIVES FOR LARGE CIVIL AIRCRAFT

Report of the Appellate Body
WT/DS487/AB/R and Add.1

Adopted by the Dispute Settlement Body on 22 September 2017

United States, *Appellant/Appellee*
European Union, *Other Appellant/Appellee*
Australia, *Third Participant*
Brazil, *Third Participant*
Canada, *Third Participant*
China, *Third Participant*
Japan, *Third Participant*
Korea, *Third Participant*
Russia, *Third Participant*

Appellate Body Division:
Graham, Presiding Member
Servansing, Member
Van den Bossche, Member

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ABBREVIATIONS USED IN THIS REPORT

Abbreviation	Description
aerospace tax measures	The B&O aerospace tax rate and a series of other tax credits or exemptions relating to product development activities, property and leasehold taxes, and sales and use taxes
B&O	business and occupation
B&O aerospace tax rate	B&O tax rate that applies to business activities concerning the manufacture and sale of commercial airplanes
BCI	business confidential information
DSB	Dispute Settlement Body
DSU	Understanding on Rules and Procedures Governing the Settlement of Disputes
ESSB 5952	Engrossed Substitute Senate Bill 5952, Chapter 2, Laws of 2013 3rd Special Session, 2014 Wash. Sess. Laws 2, codified in the *Revised Code of Washington* (Panel Exhibit EU-3)
First Siting Provision	ESSB 5952 (Panel Exhibit EU-3), Section 2
GATT 1994	General Agreement on Tariffs and Trade 1994
Panel Report	Panel Report, *United States – Conditional Tax Incentives for Large Civil Aircraft*, WT/DS487/R
SCM Agreement	Agreement on Subsidies and Countervailing Measures
Second Siting Provision	ESSB 5952 (Panel Exhibit EU-3), Sections 5-6(11)(e)(ii)
Washington	state of Washington
Working Procedures	Working Procedures for Appellate Review, WT/AB/WP/6, 16 August 2010
WTO	World Trade Organization

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CASES CITED IN THIS REPORT

Short Title	Full Case Title and Citation
Canada – Aircraft	Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, adopted 20 August 1999, DSR 1999:III, p. 1377
Canada – Aircraft (Article 21.5 – Brazil)	Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft – Recourse by Brazil to Article 21.5 of the DSU*, WT/DS70/AB/RW, adopted 4 August 2000, DSR 2000:IX, p. 4299
Canada – Autos	Appellate Body Report, *Canada – Certain Measures Affecting the Automotive Industry*, WT/DS139/AB/R, WT/DS142/AB/R, adopted 19 June 2000, DSR 2000:VI, p. 2985
EC and certain member States – Large Civil Aircraft	Appellate Body Report, *European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft*, WT/DS316/AB/R, adopted 1 June 2011, DSR 2011:I, p. 7
EC and certain member States – Large Civil Aircraft (Article 21.5 – US)	*European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft – Recourse to Article 21.5 of the DSU by the United States*, WT/DS316/RW and Add.1, circulated to WTO Members 22 September 2016 [Panel Report currently under appeal]
US – Anti-Dumping Measures on Oil Country Tubular Goods	Appellate Body Report, *United States – Anti-Dumping Measures on Oil Country Tubular Goods (OCTG) from Mexico*, WT/DS282/AB/R, adopted 28 November 2005, DSR 2005:XX, p. 10127
US – Carbon Steel (India)	Appellate Body Report, *United States – Countervailing Measures on Certain Hot-Rolled Carbon Steel Flat Products from India*, WT/DS436/AB/R, adopted 19 December 2014, DSR 2014:V, p. 1727
US – Continued Zeroing	Appellate Body Report, *United States – Continued Existence and Application of Zeroing Methodology*, WT/DS350/AB/R, adopted 19 February 2009, DSR 2009:III, p. 1291

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Short Title	Full Case Title and Citation
US – Superfund	GATT Panel Report, *United States – Taxes on Petroleum and Certain Imported Substances*, L/6175, adopted 17 June 1987, BISD 34S, p. 136
US – Tax Incentives	Panel Report, *United States – Conditional Tax Incentives for Large Civil Aircraft*, WT/DS487/R and Add.1, circulated to WTO Members 28 November 2016

1. INTRODUCTION

1.1 The United States and the European Union each appeals certain issues of law and legal interpretations developed in the Panel Report, *United States – Conditional Tax Incentives for Large Civil Aircraft*[1] (Panel Report). The Panel was established on 23 February 2015 to consider a complaint by the European Union[2] with respect to measures taken by the United States concerning certain tax incentives for large civil aircraft.

1.2 Before the Panel, the European Union challenged certain tax-related measures provided by the state of Washington (Washington), as amended by Washington Engrossed Substitute Senate Bill 5952[3] (ESSB 5952), specifically: (i) a reduction in the business and occupation (B&O) tax rate that applies to business activities concerning the manufacture and sale of commercial airplanes (B&O aerospace tax rate); and (ii) a series of other tax credits or exemptions relating to product development activities, property and leasehold taxes, and sales and use taxes – collectively, the "aerospace tax measures".[4] The European Union claimed that these tax incentives are prohibited under Articles 3.1(b) and 3.2 of the Agreement on Subsidies and Countervailing Measures (SCM Agreement) as subsidies contingent upon the use of domestic over imported goods.[5]

1.3 The European Union identified two "siting" provisions in ESSB 5952 that govern the availability of the challenged tax incentives.[6] The First Siting Provision pertains to all of the aerospace tax measures and states that the tax

[1] WT/DS487/R, 28 November 2016.
[2] Request for the Establishment of a Panel by the European Union of 12 February 2015, WT/DS487/2.
[3] Engrossed Substitute Senate Bill 5952, Chapter 2, Laws of 2013 3rd Special Session, 2014 Wash. Sess. Laws 2, codified in the *Revised Code of Washington* (ESSB 5952) (Panel Exhibit EU-3). (Panel Report, paras. 2.1 and 7.15)
[4] Panel Report, section 7.3.1.
[5] Panel Report, paras. 7.1 and 7.3.
[6] Panel Report, section 7.3.2.

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incentives will take effect "upon the siting of a significant commercial airplane manufacturing program" in Washington.[7] Both parties agreed that the First Siting Provision has been fulfilled in respect of Boeing's 777X aircraft program, and that the challenged tax incentives are therefore in effect.[8] The Second Siting Provision concerns the continued availability of the B&O aerospace tax rate only, and provides that the reduced tax rate will no longer apply if there is a determination by the Washington Department of Revenue "that any final assembly or wing assembly of any version or variant of a commercial airplane that is the basis of a siting of a significant commercial airplane manufacturing program" under the First Siting Provision has been sited outside of Washington.[9]

1.4 In the Panel Report, circulated to Members of the World Trade Organization (WTO) on 28 November 2016, the Panel found that each of the aerospace tax measures at issue constitutes a subsidy within the meaning of Article 1 of the SCM Agreement.[10] The Panel also found that, although the European Union had not demonstrated that any of the aerospace tax measures are *de jure* contingent upon the use of domestic over imported goods with respect to the First or Second Siting Provisions in ESSB 5952, whether considered jointly or separately[11], the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under Boeing's 777X aircraft program is a subsidy *de facto* contingent upon the use of domestic over imported goods within the meaning of Article 3.1(b) of the SCM Agreement.[12] Accordingly, the Panel also found that the United States had acted inconsistently with Article 3.2 of the SCM Agreement.[13]

1.5 On 5 December 2016, the Appellate Body received a letter from the European Union referring to an imminent appeal in this dispute, to the ongoing appeal in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* (DS316), and to the anticipated appeal in *US – Large Civil Aircraft (2nd complaint) (Article 21.5 – EC)* (DS353). Referring to Rules 16(1) and 16(2) of the Working Procedures for Appellate Review[14] (Working Procedures) and Article 9 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), the European Union requested that the schedules for these three appeals be harmonized to the greatest extent possible and that the hearings be sufficiently proximate in time, so that a particular matter would not be effectively disposed of in one appeal before the related matter is heard in one of the other appeals. The Chair of the Appellate Body invited the other party in these disputes, the United States, and the third parties to submit comments by 9

7 Panel Report, para. 7.28 (quoting ESSB 5952 (Panel Exhibit EU-3), Section 2).
8 Panel Report, paras. 7.31 and 7.33.
9 Panel Report, para. 7.32 (quoting ESSB 5952 (Panel Exhibit EU-3), Sections 5-6(11)(e)(ii)), and para. 7.33.
10 Panel Report, paras. 7.165 and 8.1.a.
11 Panel Report, paras. 7.297, 7.311, 7.317, and 8.1.b.
12 Panel Report, paras. 7.369 and 8.1.c.
13 Panel Report, para. 8.2.
14 WT/AB/WP/6, 16 August 2010.

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December 2016. The United States argued that the European Union's request was not supported by the DSU or the Working Procedures, and would result in delays in the proceedings, but that it remained open to proposals to set deadlines for submissions and dates for oral hearings in a way that would allow the participants and third participants in each dispute to advocate effectively their positions on appeal, and for the Appellate Body to consider fully the issues raised.[15] The participants and third parties were invited to submit additional comments by 16 December 2016. The European Union reiterated its request that any oral hearings in these appeals be sufficiently proximate in time, but noted that it was content to leave it to the Appellate Body to determine what that would mean in practice.[16] By letter dated 22 December 2016, the Appellate Body indicated that it would bear in mind the European Union's request, as well as the comments received, during the appellate proceedings in these three disputes.

1.6 On 16 December 2016, the United States notified the Dispute Settlement Body (DSB), pursuant to Articles 16.4 and 17 of the DSU, of its intention to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, and filed a Notice of Appeal[17] pursuant to Rule 20 of the Working Procedures.

1.7 Also on 16 December 2016, the Appellate Body received a joint letter from the European Union and the United States requesting the Division hearing this appeal to adopt additional procedures to protect business confidential information (BCI) in these appellate proceedings. In their letter, the European Union and the United States argued that BCI procedures are needed in these proceedings to avoid the undue risk of detrimental disclosure of particularly sensitive confidential information provided by the United States to the Panel, and proposed that the additional procedures adopted by the Appellate Body in the ongoing appeal in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* (DS316), with adjustments to remove references to highly sensitive business information, form the basis for any procedural ruling on confidentiality in these appellate proceedings.

1.8 On the same day, the Chair of the Appellate Body sent a letter to the participants and third parties indicating that the Division hearing this appeal had decided to suspend the deadlines that would otherwise apply under the Working Procedures for the filing of submissions and other documents in this appeal. On behalf of the Division, the Chair of the Appellate Body invited the third parties to comment in writing on the joint request by the European Union and the United States by 20 December 2016. Australia submitted written comments, indicating that it did not object to the joint request, provided that the proposed procedures were not implemented in a manner that unduly restricted the ability of third participants to gain reasonable access to information, or to engage in

[15] Comments were also received from Canada, China, and Japan.
[16] Comments were also received from the United States and Australia.
[17] WT/DS487/6.

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meaningful participation in the proceedings. Taking into account the arguments made by the participants and the comments by Australia, the Chair of the Appellate Body, on behalf of the Division hearing this appeal, issued a Procedural Ruling on 22 December 2016 adopting additional procedures to protect the confidentiality of BCI in these appellate proceedings.[18] On the same day, the Division provided the participants and third parties with a Working Schedule for Appeal, setting out the dates for the filing of written submissions.

1.9 On 5 January 2017, the Chair of the Appellate Body received a communication from the United States requesting that the Division modify the deadline for the filing of the United States' appellant's submission. Relying on Rule 16(2) of the Working Procedures, the United States maintained that exceptional circumstances in these proceedings justified an extension of the deadline from 10 January to 17 January 2017. On the same day, the Chair of the Appellate Body, on behalf of the Division hearing this appeal, invited the European Union and the third parties to comment in writing on the United States' request. The European Union indicated that it did not, in principle, oppose the United States' request, but observed that the United States had had more than five months since receipt of the final Panel Report to prepare its appellant's submission, and that the time periods in this dispute were subject to the expedited treatment required by Article 4.12 of the SCM Agreement. No comments were received from the third parties.

1.10 On 6 January 2017, the Chair of the Appellate Body, on behalf of the Division hearing this appeal, issued a Procedural Ruling[19] in which the Division observed that: (i) under normal circumstances – i.e. where the schedule had not been revised to allow for additional procedures to protect BCI – the United States would have already prepared and filed its appellant's submission on 16 December 2016; (ii) at the time of the request for additional procedures to protect BCI, the United States had not requested more time to prepare the contents of its appellant's submission; (iii) the scheduling of the deadlines for the United States' submissions in this appeal and in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* would not impede its ability to finalize the submissions; (iv) there had already been a delay in the deadline due to the WTO's end-of-year closure; and (v) the United States itself had indicated that its appellant's submission would not be exceptionally lengthy. For these reasons, the Division declined the United States' request, and affirmed the deadline for the filing of its appellant's submission for 10 January 2017.

1.11 On 17 January 2017, the European Union notified the DSB, pursuant to Articles 16.4 and 17 of the DSU and Article 4.8 of the SCM Agreement, of its intention to appeal certain issues of law covered in the Panel Report and certain

[18] The Procedural Ruling of 22 December 2016 is contained in Annex D-1 of the Addendum to this Report, WT/DS487/AB/R/Add.1.

[19] The Procedural Ruling of 6 January 2017 is contained in Annex D-2 of the Addendum to this Report, WT/DS487/AB/R/Add.1.

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