COLUMN:

AIRBUS (DS316) / BOEING (DS353) AND RULES ON SUBSIDIES

1. PURPOSE OF THIS COLUMN

Backgrounds and summaries for the disputes involving Airbus (DS316) / Boeing (DS353) are discussed in the main text of this Chapter 7. In the last year or two, noteworthy decisions were made by the Panels, the Appellate Body, and the arbitrators in both of these cases regarding the Agreement on Subsidies and Countervailing Measures (ASCM), and in particular regarding the "yellow" subsidies (i.e., subsidies against which counteraction can be taken). Major points in these decisions are introduced in this column as they may be instructive when exploring trends in the interpretation and application of the ASCM and considering the outlook for rules related to subsidies.

2. RECOGNITION OF "SERIOUS PREJUDICE"

The issues at hand in both cases focus on the giving of production support subsidies (such as research and development (R&D) subsidies and launch aid (subsidies provided upon launching a business)) to manufacturers (namely, Airbus and Boeing). To establish that "serious prejudice" results from these subsidies, it is required to demonstrate that these subsidies cause competing firm(s) to lose sales, cause an impedance on exports to third countries, or cause other similar effects as a result of the production of a subsidized product (e.g., a new production facility would not have been completed "but for" subsidization, and the market share of the new subsidized product that is produced in the new facility has increased). Further, a mere allegation that the lost sales or the impedance on exports or imports was caused in the past is not considered sufficient, and it is necessary to establish that the effect still continues and is ongoing (see paragraph 5.346, and others, in the compliance Appellate Body report on the Boeing case adopted in March 2019).

Accordingly, in the arbitration award against countermeasures in the Airbus case issued in October 2019, the arbitrator made a decision in line with the aforementioned report by estimating the scale of the "serious prejudice" to be the aggregate (after adjustment for inflation) of the annualized value (from 2011 to 2013) of Boeing's lost sales due to the launch aid provided to Airbus (Article 6.3(c) of the ASCM) or the impedance on exports/imports to third countries (Article 6.3(a) and (b) of the ASCM), and established that aggregate as the maximum permissible level for countermeasures imposed on Airbus. As a result, an enormous amount of countermeasures, totaling US$7,496,620,000, was awarded based on the degree and nature of the adverse effects determined to exist as at 2013.

3. SCOPE OF SUBSIDIES REQUIRING CORRECTIONS

No performance of WTO obligations is considered required in terms of any "yellow" subsidies (Article 7.8 of the ASCM) that have either already expired or come to the end of their life (see the compliance Appellate Body report on the Airbus case adopted in May 2018).

With that being the case, determining whether the subsidy has expired or ended is a crucial criterion to heed; however, the meanings of the words "expire" and "end" in this context are slightly different from those ordinarily ascribed to them. The compliance Appellate Body on the Airbus case (in May 2018) stated that "a subsidy that has ceased to exist" "cannot be required to [be] withdraw[n]," and it is as if what is being required is the realization of a situation similar to one where the subsidy had never existed. On this point, the compliance Second Panel report on the Airbus case (in December 2019) stated that "the repayment of a loan on subsidized terms merely confirms that a subsidy has been fully provided" and it cannot be said that the life of a subsidy has come to an end, because the circumstance should be considered "in the same way that the transfer of a … cash grant confirms the recipient has received the full subsidy" (see paragraph 7.202 in the compliance Second Panel report on the

Airbus case). In other words, the life of a subsidy comes to an end either (i) when both the financial contribution and the benefit have been removed or (ii) when only the benefit is removed (id. para. 7.202). So long as the recipient is continuing to enjoy the use of the subsidy for its originally intended purposes, the "life" of a subsidy continues to exist unless the recipient repays at least the remaining value of the benefit associated with the original financial contribution (on a prospective basis) (id. para. 7.203).

In the case of a subsidy provided in the form of a loan, the issue becomes whether the recipient of the loan is able to continue enjoying the use of the benefit of the subsidy for its originally intended purposes. For instance, if an asset is purchased with a loan on subsidized terms, the "benefit" remains for the useful life of the asset. In a sense, the subsidy continues to exist even after the loan has been fully repaid on subsidized terms and thus neither expires nor comes to an end unless the remaining value of that subsidy is at the very least returned (*id.* para. 7.203).

4. WITHDRAWAL OF A SUBSIDY AS A REMEDIAL MEASURE

If the yellow subsidy has neither expired nor come to an end, it is up to the implementing member country whether to withdraw the subsidy or remove the "serious prejudice" as a remedial action to address a breach of the ASCM and bring it into compliance (Article 7.8 of the ASCM). However, as there have been no precedent cases on the removal of "serious prejudice," and assuming that the "serious prejudice" should be calculated based on lost sales or other factors as described above, then it appears that production activity would need to be reduced to the level of activity prevailing before it was subsidized, as if "dialing back the clock," and it is practically impossible to take such a remedial action. So, the implementing member country, on most occasions, aims to withdraw the subsidy.

In terms of achieving "withdrawal" of a subsidy provided in the form of a loan, the implementing member country can do so by amending or renewing the loan arrangement, such as the interest rate of return, by aligning it with a market benchmark to ensure the arrangement does not fall within the terms of the subsidy (see paragraph 7.125, and others, in the second compliance panel report on the Airbus case). The test thereof is, to picture the situation a commercial lender would have been in at the time of the renewal had the commercial lender agreed to lend on market terms from the very beginning, and judging whether the borrower was actually placed in the same situation at the time of the renewal (*id.* para. 7.158). For example, in order to bring a subsidized loan provided for a 10-year period at an average cost of 5% interest per annum (instead of the market rate of 7%) into compliance by withdrawal after 5 years, the terms and conditions of loan need to be aligned with a market benchmark in year five by increasing the rate of interest to apply over the remaining five years to 7% (this would mean that aligning with the market rate for a comparable five-year loan in year five would not be sufficient) (id. para. 7.150).

5. PROBLEMS AND ISSUES

It is difficult to ascertain a consistent line of interpretation when reading through "2." through "4." above in its entirety. First of all, if a subsidized loan is ongoing, then it is simply a matter of aligning the loan arrangement to the market-based interest rate from then on (and there is no need to return the already enjoyed low-rate loans and business profits therefrom) (see 4 above). In contrast, however, if the issuance of a loan or a repayment thereof has already been ended, then these facts themselves do not constitute the expiry or the end of the subsidized loan, and thus it would be required to return the remaining value of the business interests (such as a production facility) enjoyed through the use of the subsidized loan (see 3 above). This would seem to generate an imbalance in some cases.

Further, there is no clear explanation as to what the "remaining value" is that needs to be returned. It could be interpreted that it refers to the book value after amortization of the subsidized production facility. However, not all of the subsidy is always exhausted in facility construction. There may also be a situation where loans from financial institutions in the private sector and funds on hand are used as well. How the "remaining value" would be calculated in such a situation is not expressly stated.

In addition, if it is determined that the implementing member country has failed to come into compliance due to the fact that the "remaining value" of the subsidized facility remains (as the European Union failed to do in the Airbus case), then the extent of the "serious prejudice" by the subsidy is, in principle, irrelevant to the extent of the "remaining value" of the subsidy. The amount would be far greater than that because the calculation would be based on the integrated value of factors such as the lost sales of competitor(s) and the impedance on exports or imports due to the provided subsidy (see 2 above). Even if the effort for compliance is insufficient, however, should it not be perceived that the extent of the incurred "serious prejudice" had naturally been affected if the "remaining value" of the subsidy is reduced?

It probably is the case that conceptual terms, such as "life of the subsidy," "expire," and "remaining value," that are not the exact wordings used in the ASCM were coined through the efforts to settle the disputes; however, the propriety of opening discussions on new interpretations for these concepts is questionable, and we should keep a close eye on future developments.