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## **1 ARTICLE 7**

### **1.1 Text of Article 7**

#### **Article 7**

##### *Remedies*

7.1 Except as provided in Article 13 of the Agreement on Agriculture, whenever a Member has reason to believe that any subsidy referred to in Article 1, granted or maintained by another Member, results in injury to its domestic industry, nullification or impairment or serious prejudice, such Member may request consultations with such other Member.

7.2 A request for consultations under paragraph 1 shall include a statement of available evidence with regard to (a) the existence and nature of the subsidy in question, and (b) the injury caused to the domestic industry, or the nullification or impairment, or serious prejudice<sup>19</sup> caused to the interests of the Member requesting consultations.

*(footnote original)*<sup>19</sup> In the event that the request relates to a subsidy deemed to result in serious prejudice in terms of paragraph 1 of Article 6, the available evidence of serious prejudice may be limited to the available evidence as to whether the conditions of paragraph 1 of Article 6 have been met or not.

7.3 Upon request for consultations under paragraph 1, the Member believed to be granting or maintaining the subsidy practice in question shall enter into such consultations as quickly as possible. The purpose of the consultations shall be to clarify the facts of the situation and to arrive at a mutually agreed solution.

7.4 If consultations do not result in a mutually agreed solution within 60 days<sup>20</sup>, any Member party to such consultations may refer the matter to the DSB for the establishment of a panel, unless the DSB decides by consensus not to establish a panel. The composition of the panel and its terms of reference shall be established within 15 days from the date when it is established.

*(footnote original)*<sup>20</sup> Any time-periods mentioned in this Article may be extended by mutual agreement.

7.5 The panel shall review the matter and shall submit its final report to the parties to the dispute. The report shall be circulated to all Members within 120 days of the date of the composition and establishment of the panel's terms of reference.

7.6 Within 30 days of the issuance of the panel's report to all Members, the report shall be adopted by the DSB<sup>21</sup> unless one of the parties to the dispute formally notifies the DSB of its decision to appeal or the DSB decides by consensus not to adopt the report.

*(footnote original)*<sup>21</sup> If a meeting of the DSB is not scheduled during this period, such a meeting shall be held for this purpose.

7.7 Where a panel report is appealed, the Appellate Body shall issue its decision within 60 days from the date when the party to the dispute formally notifies its intention to appeal. When the Appellate Body considers that it cannot provide its report within 60 days, it shall inform the DSB in writing of the reasons for the delay together with an estimate of the period within which it will submit its report. In no case shall the proceedings exceed 90 days. The appellate report shall be adopted by the DSB and unconditionally accepted by the parties to the dispute unless the DSB decides by consensus not to adopt the appellate report within 20 days following its issuance to the Members.<sup>22</sup>

*(footnote original)*<sup>22</sup> If a meeting of the DSB is not scheduled during this period, such a meeting shall be held for this purpose.

7.8 Where a panel report or an Appellate Body report is adopted in which it is determined that any subsidy has resulted in adverse effects to the interests of another Member within the meaning of Article 5, the Member granting or maintaining such subsidy shall take appropriate steps to remove the adverse effects or shall withdraw the subsidy.

7.9 In the event the Member has not taken appropriate steps to remove the adverse effects of the subsidy or withdraw the subsidy within six months from the date when the DSB adopts the panel report or the Appellate Body report, and in the absence of agreement on compensation, the DSB shall grant authorization to the complaining Member to take countermeasures, commensurate with the degree and nature of the adverse effects determined to exist, unless the DSB decides by consensus to reject the request.

7.10 In the event that a party to the dispute requests arbitration under paragraph 6 of Article 22 of the DSU, the arbitrator shall determine whether the countermeasures are commensurate with the degree and nature of the adverse effects determined to exist.

## 1.2 Article 7.8

### 1.2.1 General

1. The Panel in *Indonesia – Autos* referred in its conclusions and recommendations to the remedy in Article 7.8 as follows:

"With respect to the conclusion of serious prejudice to the interests of the European Communities, Article 7.8 of the SCM Agreement provides that, '[w]here a panel report or an Appellate Body report is adopted in which it is determined that any subsidy has resulted in adverse effects to the interests of another Member within the meaning of Article 5, the Member granting or maintaining the subsidy shall take appropriate steps to remove the adverse effects or shall withdraw the subsidy.'"<sup>1</sup>

2. In the context of a claim regarding the scope of Article 21.5 of the DSU, the Panel in *US – Upland Cotton (Article 21.5 – Brazil)* addressed the issue of whether it is only the adverse effects resulting from the subsidies at issue in the original proceeding that need to be removed, or whether the Article 7.8 obligation also requires the removal of (additional) adverse effects resulting from the continued provision of the same subsidies:

"Under Article 7.8 of the *SCM Agreement* the United States was obligated, with respect to the subsidies subject to the 'present' serious prejudice finding of the original panel, to 'take appropriate steps to remove the adverse effects or ... withdraw the subsidy'.

It is clear from the context that the adverse effects that must be removed are the adverse effects of the subsidy that has been determined to have resulted in adverse effects. Since the original panel made a finding of present serious prejudice in respect of subsidies provided during MY 1999-2002, the question arises whether the obligation to take appropriate steps to remove the adverse effects only applies to payments of subsidies made in those years.

It is not in dispute that the United States presently provides marketing loan and counter-cyclical payments on the same legal basis and subject to the same conditions and criteria as the marketing loan payments and counter-cyclical payments that were subject to the panel's finding of 'present' serious prejudice. In a situation where the subsidy in question has been found to be a prohibited one, the continued use of the subsidy under the same conditions and criteria is inconsistent with a Member's obligation to 'withdraw' the subsidy under Article 4.7 of the *SCM Agreement*. Thus, the concept of 'withdrawal' must in any event be interpreted to mean that a Member must cease to act in a WTO-inconsistent manner with respect to that subsidy. If a failure to cease conduct inconsistent with a Member's obligations under Article 3 of the *SCM Agreement* is inconsistent with the obligation to withdraw the subsidy in Article 4.7 of the *SCM Agreement*, we see no logical reason why the same concept should not also apply to the obligation that arises under Article 7.8 of the *SCM Agreement* to withdraw the subsidy or to take appropriate steps to remove the adverse effects of a subsidy that has been determined to result in adverse effects. In our view, the remedy under Article 7.8 must be viewed in its relationship to the obligation in Article 5 not to cause through the use of any subsidy referred to in Articles 1.1 and 1.2 of the *SCM Agreement* adverse effects to the interests of other Members. It must serve to restore conformity with the Member's obligation to avoid causing adverse effects through the use of any subsidy. As a consequence, a Member does not take appropriate steps to remove adverse effects of a subsidy if it continues to provide payments under the same conditions and criteria as the original subsidy in a manner that causes adverse effects. The interpretation advocated by the United States, whereby the obligation under Article 7.8 of the *SCM Agreement* is limited to the removal of the adverse effects caused by subsidies granted in a particular period of time, implies that it would not be possible to review in an Article 21.5 proceeding whether a Member causes adverse effects by continuing to grant subsidies under the same conditions and criteria as the subsidies found to have caused adverse effects.

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<sup>1</sup> Panel Report, *Indonesia – Autos*, para. 15.3.

Such an interpretation fails to take into account the relationship between Article 7.8 and Article 5 of the *SCM Agreement* and thus fails to interpret Article 7.8 in its proper context."<sup>2</sup>

3. The Appellate Body was in broad agreement with the Panel's approach to Article 7.8 of the SCM Agreement:

"Pursuant to Article 7.8, the implementing Member has two options to come into compliance. The implementing Member: (i) shall take appropriate steps to remove the adverse effects; or (ii) shall withdraw the subsidy. The use of the terms 'shall take' and 'shall withdraw' indicate that compliance with Article 7.8 of the *SCM Agreement* will usually involve some action by the respondent Member. This affirmative action would be directed at effecting the withdrawal of the subsidy or the removal of its adverse effects. A Member would normally not be able to abstain from taking any action on the assumption that the subsidy will expire or that the adverse effects of the subsidy will dissipate on their own.

The question then becomes: With respect to which subsidies must the implementing Member take such action? Such action would certainly be expected with respect to subsidies granted in the past and which may have formed the basis of a panel's determination of present serious prejudice and adverse effects. However, we do not see the obligation in Article 7.8 as being limited to subsidies granted in the past. Article 7.8 expressly refers to a Member 'granting or maintaining such subsidy'. The verb 'maintain' suggests, to us, that the obligation set forth in Article 7.8 is of a continuous nature, extending beyond subsidies granted in the past. This means that, in the case of recurring annual payments, the obligation in Article 7.8 would extend to payments 'maintained' by the respondent Member beyond the time period examined by the panel for purposes of determining the existence of serious prejudice, as long as those payments continue to have adverse effects. Otherwise, the adverse effects of subsequent payments would simply replace the adverse effects that the implementing Member was under an obligation to remove. Such a reading of Article 7.8 would not give meaning and effect to the term 'maintain', which is distinct from the term 'grant', and has also been included in that Article. Indeed, it would render the term 'maintain' redundant. In addition, it would fail to give meaning and effect to the obligation to 'take appropriate steps to remove the adverse effects' in Article 7.8, and to the requirement under Article 21.5 to 'comply' with the DSB's recommendations and rulings, including the requirement to take the remedial action foreseen in Article 7.8 as a consequence of a finding of adverse effects.

Our interpretation of Article 7.8 is consistent with the context provided by Article 4.7 of the *SCM Agreement*, which applies in cases involving prohibited subsidies. In *US – FSC (Article 21.5 – EC II)*, the Appellate Body stated that, 'if, in an Article 21.5 proceeding, a panel finds that the measure taken to comply with the Article 4.7 recommendation made in the original proceedings does not achieve *full* withdrawal of the prohibited subsidy—either because it leaves the entirety or part of the original prohibited subsidy in place, or because it replaces that subsidy with another subsidy prohibited under the *SCM Agreement*—the implementing Member continues to be under the obligation to achieve full withdrawal of the subsidy'. Similarly, a Member would not comply with the obligation in Article 7.8 to withdraw the subsidy if it leaves an actionable subsidy in place, either entirely or partially, or replaces that subsidy with another actionable subsidy. We recognize that, unlike Article 4.7, Article 7.8 gives Members the option of removing the adverse effects as an alternative to withdrawing the subsidy. The availability of this option is arguably a consequence of the fact that actionable subsidies are not prohibited *per se*; rather, they are actionable to the extent they cause adverse effects. Nevertheless, the option of removing the adverse effects cannot be read as allowing a Member to continue to cause adverse effects by maintaining the subsidies that were found to have resulted in adverse effects. As observed earlier, if the contrary proposition were accepted, the adverse effects of subsequent subsidies, especially in the case of recurrent subsidies, would simply replace the adverse effects that the implementing Member was required to

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<sup>2</sup> Panel Report, *US – Upland Cotton (Article 21.5 – Brazil)*, paras. 9.77–9.79.

remove, making the obligation in Article 7.8 to 'take appropriate steps to remove the adverse effects' meaningless."<sup>3</sup>

4. In *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 21.5 – EU)*, the Panel disagreed with the European Union's interpretation of the phrase "to take appropriate steps to remove the adverse effects" which was that this phrase entails an obligation to ensure adverse effects are removed from the specific transaction that formed the basis of the adverse effects findings in the original proceeding. The Panel explained:

"First, the European Union's argument involves an assumption that the phrase 'take appropriate steps to remove the adverse effects' in Article 7.8 must be interpreted to mean that a Member found to be granting or maintaining an actionable subsidy is obligated to ensure that the particular adverse effects found to exist in respect of the specific transactions during the original reference period cease to exist in respect of those same transactions. We doubt whether such an interpretation of 'remove the adverse effects' is meaningful in a practical sense. It is not clear, for example, how it is possible in practice for a Member to take steps to ensure that significant price suppression found in relation to specific transactions during the original reference period does not continue in respect of those same transactions in the post-implementation period or that a significant lost sale found in the original reference period in respect of a specific transaction does not continue to constitute a lost sale in respect of that transaction in the post-implementation period.

Second, the idea that 'to take appropriate steps to remove the adverse effects' entails an obligation to ensure that adverse effects must be 'removed' from the specific transactions that formed the basis for the adverse effects findings in the original proceeding is also difficult to reconcile with the prospective interpretation of Article 7.8. ... In our view, to interpret 'to take appropriate steps to remove the adverse effects' to mean 'ensuring that no adverse effects arise in the new reference period', is very different from interpreting this phrase to mean that a Member is obligated 'to remove the adverse effects associated with each of {the} sales' that were found to be lost sales in the original proceeding."<sup>4</sup>

5. The Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* considered the scope of Article 7.8 by stressing the effects-based nature of disciplines under Article 5 of the SCM Agreement and noting the role of Article 7.8 in bringing an implementing Member into conformity with its rights and obligations. The Panel concluded that "a subsidy found to have caused adverse effects in an original proceeding *need not always* continue to exist during the implementation period in order for an implementing Member to have a compliance obligation with respect to that subsidy under the terms of Article 7.8 of the SCM Agreement."<sup>5</sup> The Panel explained:

"It follows from the *effects-based* nature of the disciplines in Article 5 and the role that Article 7.8 is intended to play in bringing an implementing Member into conformity with its obligations under the SCM Agreement, that there may well be particular factual circumstances when the obligation to 'take appropriate steps to remove the adverse effects' or 'withdraw the subsidy' will apply to subsidies found to have caused adverse effects in an original proceeding, *irrespective of whether those subsidies continue to exist* in the implementation period. In other words, because the remedies provided for under Article 7.8 are intended to bring an implementing Member into conformity with its obligations under Article 5, the fact that it is possible under these disciplines to find that a subsidy no longer being granted or maintained causes adverse effects, necessarily implies that the mere fact that a subsidy granted in the past no longer exists cannot *alone* exclude it from the scope of an implementing Member's Article 7.8 compliance obligations."<sup>6</sup>

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<sup>3</sup> Appellate Body Report, *US – Upland Cotton (Article 21.5 – Brazil)*, paras. 236–238.

<sup>4</sup> Panel Report, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 21.5 – EU)*, paras. 9.312–9.313.

<sup>5</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.822.

<sup>6</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.822.

6. In *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, the Panel provided guidance on the appropriate counterfactual to assess whether a Member has complied under Article 7.8 of the SCM Agreement by taking appropriate steps to remove the adverse effects after it has been determined that the Member failed to achieve compliance under Article 7.8 of the SCM Agreement by withdrawing the subsidy. The Panel rejected the counterfactual suggested by the European Union, which "entails comparing the actual market situation ... with the market situation that would have existed if the challenged subsidies had been withdrawn at the end of the implementation period."<sup>7</sup>

7. The Panel noted that "the European Union's proposed counterfactual ignores all prior effects of the non-withdrawn subsidy, which may well be important to understanding its present-day effects" and "fails to identify whether the provision of a non-withdrawn subsidy that continues to exist in the post-implementation period has present day effects."<sup>8</sup> Moreover, the Panel pointed out that the respondent's different hypothetical withdrawal options may involve "different, *possibly competing*, scenarios" and "a complainant might well conceive of other possible withdrawal options that would have a different counterfactual market effect."<sup>9</sup>

8. Therefore, the Panel found that the appropriate counterfactual to apply is one under which the subsidies in question were never granted to Airbus, referred to as "the absence of" these subsidies.<sup>10</sup>

### **1.2.2 Implication under Article 7.8 of the "expiry" of subsidy for determination of "withdrawal"**

9. The Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* found that the "expiry" of a subsidy does not necessarily amount to withdrawing that subsidy within the meaning of Article 7.8 of the SCM Agreement:

"[I]t cannot be concluded on the *sole* basis of the 'expiry' of the relevant ... subsidies that the European Union and certain member States have *ipso facto* complied with the obligation to 'withdraw the subsidy' with respect to those measures. Rather, in the light of the effects-based nature of the subsidy disciplines of Article 5, the extent to which these *passive* 'expiry' events may be found to amount to the 'withdrawal' of subsidies for the purpose of Article 7.8 will depend upon the extent to which they bring the European Union and certain member States into conformity with Article 5 of the SCM Agreement."<sup>11</sup>

10. The European Union in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* contended that the "expiry", "extinction" and/or "extraction" events always amount to "withdrawal" of subsidies.<sup>12</sup> In support of this interpretation, the European Union presented three arguments. First, the European Union argued that "the obligation to 'withdraw the subsidy' in both Articles 4.7 and 7.8 of the SCM Agreement must be given the same meaning and that, therefore, the former possibility for achieving compliance with Article 4.7 must also be available to an implementing Member faced with a compliance obligation under Article 7.8."<sup>13</sup> The Panel disagreed:

"[T]he fact that the 'removal' or 'taking away' of a subsidy, in the sense of bringing the 'life' of a subsidy to an end, may suffice to bring an implementing Member into compliance with Article 4.7 does not undermine our interpretation of what is needed to 'withdraw the subsidy' for the purpose of Article 7.8. This is because the availability of this particular compliance option under Article 4.7 results from the fact that the prohibition in Articles 3.1(a) and 3.2 is based on the mere *existence* of a particular type of subsidy, *irrespective of its trade effects*. ... [I]n the light of the purpose of Article 7.8 and the effects-based disciplines of Article 5, it is only logical, in our view,

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<sup>7</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.263.

<sup>8</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.265.

<sup>9</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.267.

<sup>10</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.268.

<sup>11</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.1078.

<sup>12</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.1079.

<sup>13</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.1086.

to find that the 'removal' or 'taking away' of a subsidy, in the sense of bringing the 'life' of a subsidy to an end, may not always *ipso facto* suffice to bring an implementing Member into compliance with its obligation to 'withdraw the subsidy' for the purpose of Article 7.8 of the SCM Agreement.

...

[W]e understand Article 3.7 of the DSU to be a more general expression of the compliance objective that is articulated in Articles 4.7 and 7.8 for the purpose of Parts II and III of the SCM Agreement. It follows, therefore, that as is the case with the obligation to 'withdraw the subsidy' under Articles 4.7 and 7.8, the 'withdrawal' of measures that is referred to in Article 3.7 of the DSU should be understood in the light of the nature of the particular obligation(s) with respect to which an implementing Member must achieve conformity in any given dispute. Where pursuant to any such obligation a continued infringement of a covered agreement can only be established on the basis of the *existence* of a particular type of measure, the mere 'removal' or 'taking away' of that measure, in the sense of its termination, will be sufficient to conclude that the measure has been 'withdrawn', thereby bringing the relevant Member into conformity with the covered agreements. On the other hand, where the relevant obligation imposes a prohibition or discipline that is based on the existence of certain *trade effects*, as opposed to the existence of a measure, the mere 'removal' or 'taking away' of the relevant measure, in the sense of its termination, may not bring an end to the undesired trade effects. In this latter situation, the mere 'removal' or 'taking away' of a measure would be insufficient to establish that the 'withdrawal' of measures envisaged in Article 3.7 has been achieved.

Thus, the reason why the 'removal' or 'taking away' of a subsidy, in the sense of bringing the 'life' of a subsidy to an end, may have a different impact on the extent to which an implementing Member has complied with Article 4.7 compared with Article 7.8 is not because of any fundamental difference in the intellectual framework used to interpret the respective obligations to 'withdraw the subsidy'. Rather, the difference is due to the diverse nature of the obligations that give rise to the respective compliance obligation – the former being based on the *mere existence* of a prohibited subsidy, whereas the latter being focused on the *trade effects* of a subsidy, *irrespective of its continued existence*.<sup>14</sup>

11. Second, the European Union in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* argued that the Appellate Body's statements in *US – Upland Cotton (Article 21.5 – Brazil)* must be understood "within the specific temporal context of the lives of the subsidies at issue in a particular dispute."<sup>15</sup> The European Union emphasized that the LA/MSF measures in this proceeding were provided over 42 years ago and the subsidies had "accrued and diminished" over time, which affect the way by which compliance is assessed with the requirements of Article 7.8.<sup>16</sup> The Panel also rejected this argument:

"Contrary to what appears to be the European Union's position, we do not understand the ... Appellate Body statements to support the proposition that the mere expiry of a subsidy at the end of its expected life *before the end of an implementation period* will *always* suffice to establish that an implementing Member has 'withdrawn' the subsidy for the purpose of Article 7.8. Rather, as already noted, the logical implication of the Appellate Body's statement is that it will only be in circumstances that are not 'usual' or 'normal' that allowing a subsidy to expire passively over the ordinary course of its expected life will be sufficient to establish compliance.

While it is true that the Appellate Body has declared that a subsidy has a 'finite life', which 'accrues and diminishes over time', and which 'comes to an end', the Appellate Body has never equated the end of the life of a subsidy with the cessation of its effects. On the contrary, the Appellate Body has explicitly found that the effects of a

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<sup>14</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, paras. 6.1086 and 6.1088-6.1089.

<sup>15</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.1092.

<sup>16</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.1092.

subsidy may well persist beyond its expected life, and that ultimately, the extent to which this may be the case will be a fact-specific matter. Although the age of a subsidy will be an important factor to consider when making this assessment, it will not *alone* be determinative. Thus, the simple fact that the anticipated life of a subsidy may have expired before the end of the implementation period does not preclude that the subsidy may be continuing to cause adverse effects in the post-implementation period. Ultimately, therefore, we cannot accept the European Union's reliance on the Appellate Body's statements to support its contention that the passive 'expiry' events it relies upon mean that it has complied with the obligation to 'withdraw the subsidy' because, as already noted, equating these events with the 'withdrawal' of subsidies for the purpose of Article 7.8 would render any findings of adverse effects made against such expired subsidies in original proceedings purely declaratory, and to this extent render the effects-based disciplines of Article 5 of the SCM Agreement *inutile*."

12. Finally, the Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* rejected the European Union's third argument that an interpretation of Article 7.8 in which an implementing Member must achieve conformity with Article 5 of the SCM Agreement would read out the compliance option in Article 7.8 to "take appropriate steps to remove the adverse effects", contrary to the principle of effective treaty interpretation.<sup>17</sup> In the Panel's view, Article 7.8, by its express terms, provides an implementing Member with "potentially two *different* pathways to achieve the *same compliance objective*".<sup>18</sup> The Panel explained, that the first option to "withdraw the subsidy"—which may be achieved by bringing the "life" of the subsidy to an end or by modifying the terms of the subsidy in a way that eliminates the prohibited export performance condition— focuses on the implementing Member's efforts on the subsidy found to have caused adverse effects. Thereby, the Member found to have caused such adverse effects has the option to come into conformity with Article 5 of the SCM Agreement by "withdrawing" that subsidy. By contrast, because the second option in Article 7.8 to "take appropriate steps to remove the adverse effects" does not explicitly refer to the "subsidy", an implementing Member under this approach would come into conformity with its compliance obligations under Article 5 "without taking any specific action *in relation to the subsidy* found to cause adverse effects, but rather through other more effects-based or market-focused solutions".<sup>19</sup> In the Panel's view, "the very existence of this possibility suggests that the drafters of the SCM Agreement had in mind that the option to 'withdraw the subsidy' might not always be a desirable course of action for an implementing Member".<sup>20</sup> Under either approach, the range of compliance options will vary and depend on the facts of the particular case.<sup>21</sup> In sum, the Panel stated:

"It follows from the above analysis that finding that the two compliance options provided for in Article 7.8 must be interpreted in a way that brings an implementing Member into conformity with its obligations under Article 5 of the SCM Agreement does not render the option to 'withdraw the subsidy' *inutile*. While the efforts of an implementing Member taking up the option to 'withdraw', 'remove' or 'take away' the subsidy, will be focused on the *subsidy itself*; an implementing Member wanting to 'take appropriate steps to remove the adverse effects' may pursue a different course action that is *unrelated to the subsidy* measure itself. An implementing Member will, of course, be free to choose between any possible alternative means of pursuing these two compliance options. However, as the Appellate Body has emphasized, whatever approach an implementing Member finally decides upon must be 'sufficient to bring that Member into compliance with its WTO obligations'. "<sup>22</sup>

13. The Appellate Body in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* considered whether the Panel erred in its interpretation of Article 7.8. The Appellate Body noted that the use of the word "or" in the text of this provision suggests that a Member may implement DSB recommendations and rulings under Part III of the SCM Agreement by choosing either of the alternative pathways to achieving compliance. It also considered that the use of the words "granting or maintaining" of a subsidy found to have caused adverse effects reflects an

<sup>17</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.1095.

<sup>18</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.1096.

<sup>19</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.1099.

<sup>20</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.1099.

<sup>21</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, paras. 6.1097 and 6.1099.

<sup>22</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.1100.



obligation to cease any such conduct. Therefore, the Appellate Body found it difficult to see how a Member could be said to be granting or maintaining a subsidy giving rise to a compliance obligation if that subsidy has expired and therefore no longer exists. The Appellate Body pointed out:

"Article 7.8 consists of two clauses. The introductory clause refers to circumstances where a subsidy is found, in an adopted panel or Appellate Body report, to have 'resulted in adverse effects to the interests of another Member'. The second clause then specifies that, in such a situation, 'the Member granting or maintaining such subsidy' may come into compliance with its obligations under the SCM Agreement in one of two alternative ways: (i) it may either 'take appropriate steps to remove the adverse effects'; or (ii) it may 'withdraw the subsidy'. The use of the word 'or' in the context of the second clause of Article 7.8 suggests that the Member concerned may implement the recommendations and rulings of the DSB under Part III of the SCM Agreement by choosing either of these alternative pathways to achieving compliance.

...

Article 7.8 of the SCM Agreement expressly refers to the 'granting or maintaining' of a subsidy found to have caused adverse effects to the interests of another Member. As we see it, these terms indicate that Article 7.8 reflects an obligation to cease any conduct amounting to the 'granting or maintaining' of subsidies that cause adverse effects. This is true regardless of whether the words 'granting or maintaining' in Article 7.8 are understood in the present continuous tense, or as present participles qualifying the term 'Member'. Indeed, Article 7.8 sets out an obligation 'of a continuous nature, extending beyond subsidies granted in the past. Moreover, the object of the action of 'granting or maintaining' is the 'subsidy' that causes adverse effects. In the light of this language in Article 7.8, we find it difficult to see how a Member could be said to be 'granting or maintaining' a subsidy giving rise to a compliance obligation if that subsidy has expired and therefore no longer exists."<sup>23</sup>

11. In *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, the Appellate Body expressed concern with the Panel's understanding that "withdrawal" requires, in each case, that the implementing Member remove the adverse effects of any past subsidies, regardless of whether such subsidies had expired. The Appellate Body looked at the ordinary meaning of the word "withdraw" and found that it concerns the taking away of that subsidy, and thus means that a Member "granting or maintaining" a subsidy should cease such conduct. The Appellate Body noted that the Panel's reasoning in this regard was that it should be possible to find that an implementing Member has withdrawn – i.e. "taken away" – a subsidy found to cause adverse effects when "the terms or conditions of that subsidy have been modified" in a way that ensures it no longer causes adverse effects."<sup>24</sup> However, the Appellate Body noted that it was not clear how an implementing Member could modify the terms and conditions of subsidies that no longer exist.<sup>25</sup> Moreover, while the pathway identified by the Panel – i.e. modification of the terms or conditions of a subsidy in a way that ensures it no longer causes adverse effects – may provide one way for an implementing Member to come into compliance with its obligations under Article 7.8, the Appellate Body noted that it did "not see how it would effectively differ from the other compliance option provided for under this provision: the option of taking appropriate steps to remove the adverse effects."<sup>26</sup>

12. The Appellate Body in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* noted the Panel's reliance on the context and object and purpose of Article 7.8. It also underlined that Article 7.8 is situated within a broader range of provisions applicable to disputes regarding actionable subsidies that have been found to be inconsistent with Articles 5 and 6 of the SCM Agreement. According to the Appellate Body, however, while Article 5 and Article 7.8 of the SCM Agreement concern two related but distinct inquiries, the Panel's analysis of Article 5 appears

<sup>23</sup> Appellate Body Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, paras. 5.362 and 5.364.

<sup>24</sup> (footnote original) Panel Report, para. 6.1098. (italics original; underlining added).

<sup>25</sup> Appellate Body Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 5.364.

<sup>26</sup> Appellate Body Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 5.366.

to have blurred the distinction between these two provisions. the Appellate Body clarified that while a past subsidy that no longer exists may be found to cause or have caused adverse effects that continue to be present during the reference period, the source of the inconsistency under Article 5 is nonetheless the subsidy that causes adverse effects. In turn, the option to withdraw the subsidy under Article 7.8 contemplates action in relation to the subsidy found to have caused adverse effects and to the extent that the underlying subsidy has ceased to exist, there is no additional requirement to remove any lingering effects that may flow from the subsidy. The Appellate Body disagreed with the Panel that it follows from the so-called "effects based nature" of Article 5 that an implementing Member would have a compliance obligation under Article 7.8 regardless of whether the subsidy continues to exist:

"As we see it, Article 5 and Article 7.8 of the SCM Agreement concern two related but distinct inquiries: while the former seeks to establish the existence of adverse effects and the causal link between any subsidy and the adverse effects found to exist, the latter specifies the compliance actions to be taken by a Member granting or maintaining a subsidy found to have caused or to cause adverse effects. The Panel's analysis of Article 5 appears to blur the distinction between these two provisions and, as the European Union suggests, to 'collapse {} the substantive obligations under Article 5 and the implementation obligations under Article 7.8'. We note in particular that, in its analysis of the compliance obligations that an implementing Member has under Article 7.8, the Panel relied heavily on what it characterized as the 'effects-based nature' of Article 5 of the SCM Agreement. The Panel referred in particular to the following passage of the Appellate Body report in *EC and certain member States – Large Civil Aircraft*:

Article 5 of the SCM Agreement imposes an obligation on Members not to cause adverse effects to the interests of other Members through the use of any subsidy as defined in Article 1. *We disagree with the proposition that this obligation does not arise in respect of subsidies that have come to an end by the time of the reference period. In fact, we do not exclude that, under certain circumstances, a past subsidy that no longer exists may be found to cause or have caused adverse effects that continue to be present during the reference period.*

This passage recognizes that a subsidy and its effects need not be contemporaneous. Contrary to what the Panel appears to have assumed, it does not follow from this that the effect of a subsidy can be detached from the subsidy itself such that these effects could be subject to a separate compliance obligation under Article 7.8. When a subsidy has expired such that it is no longer in existence, we cannot see how a compliance obligation could still apply to lingering effect of such a past subsidy. Rather, what is relevant for Article 5, as well as for Article 7.8, is the *causing* of adverse effects through the use of the subsidy. While a past subsidy that no longer exists may 'be found to cause or have caused adverse effects that continue to be present during the reference period', the *source* of the inconsistency under Article 5 is nonetheless the *subsidy* that causes adverse effects. The option to 'withdraw the subsidy' under Article 7.8 contemplates action in relation to the subsidy found to have caused adverse effects. To the extent that the underlying subsidy has ceased to exist, there is no additional requirement, under Article 7.8, to remove any lingering effects that may flow from that subsidy. We therefore disagree with the Panel that it follows from the so-called 'effects-based nature' of the discipline of Article 5 that an implementing Member would have a compliance obligation under Article 7.8 regardless of whether the subsidy continues to exist."<sup>27</sup>

13. The Appellate Body in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* found support for its interpretation of Article 7.8 in Part II of the SCM Agreement covering prohibited subsidies, as well as the rules that apply to the imposition of countervailing duties in Part V. The Appellate Body also looked at context provided by other covered agreements and noted that Article 7.8 is one of the special or additional rules and procedures on dispute settlement contained in the covered agreements that are identified in Article 1.2 and Appendix 2 of the DSU,

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<sup>27</sup> Appellate Body Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, paras. 5.370 - 5.371.

and it was concerned with the Panel's decision to resort to context provided by the DSU without properly considering the contextual relevance of those provisions in other parts of the SCM Agreement:

"Our reading of Article 7.8 also finds support in the relevant provisions under Part II of the SCM Agreement, entitled 'Prohibited Subsidies', comprising Articles 3 and 4. Article 3.1 provides that subsidies contingent upon export performance (Article 3.1(a)) or upon the use of domestic over imported goods (Article 3.1(b)) 'shall be prohibited'. Article 3.2 further provides that '{a} Member shall neither grant nor maintain subsidies referred to' in Article 3.1. Article 4, like Article 7 of the SCM Agreement, is entitled 'Remedies', and sets out the rules for dispute settlement involving prohibited subsidies referred to in Article 3. Article 4.7 provides that, '{i}f the measure in question is found to be a prohibited subsidy, the panel shall recommend that the subsidizing Member withdraw the subsidy without delay'. Article 4.7 does not require removal of the effects of such subsidies. Rather, withdrawal under Article 4.7 seeks to eliminate the source of the inconsistency, namely, the condition that is prohibited under Article 3.1(a) or 3.1(b). Similarly, Article 7.8 addresses the source of the infringement found to exist, and requires cessation of conduct consisting of the granting or maintaining of subsidies that cause adverse effects. It would be incongruous, in our view, if elimination of the source of the inconsistency were sufficient to comply with an implementing Member's obligations in the context of Article 4.7, but not in the context of Article 7.8.

It is also useful in this regard to consider the rules that apply to the imposition of countervailing duties under Part V of the SCM Agreement. While serious prejudice can only be addressed through countermeasures imposed under Part III, subsidies that cause injury to the domestic industry can be addressed *either* through countermeasures imposed under Part III *or* through countervailing duties under Part V.

With regard to the imposition of countervailing duties, Article 19.1 of the SCM Agreement stipulates that countervailing duties may be imposed on subsidized imports 'unless the subsidy or subsidies are withdrawn.' Hence, under Part V of the SCM Agreement, remedial action is contemplated with respect to subsidies that cause injury to the domestic industry. As we see it, the same is true in the context of Part III of the SCM Agreement, where the inconsistency to be remedied relates to *subsidies* that constitute a genuine and substantial cause of adverse effects during the implementation period. Thus, the inconsistency does not relate to only the effects, as the Panel seems to have suggested, but rather to the *action of using subsidies* in a way that causes adverse effects.

Looking beyond the SCM Agreement to context provided by other covered agreements, we note that Article 7.8 of the SCM Agreement is one of the 'special or additional rules and procedures on dispute settlement contained in the covered agreements' that are identified in Article 1.2 and Appendix 2 of the DSU, which prevail over the general DSU rules and procedures to the extent that they '*cannot* be read as *complementing* each other'. In this regard, we are concerned with the Panel's decision to resort to context provided by various provisions of the DSU without considering properly the contextual relevance of provisions in other parts of the SCM Agreement. This is especially so because, as a 'special or additional rule {}' on dispute settlement in the SCM Agreement, Article 7.8 must be properly understood in the particular context of disputes involving subsidies."<sup>28</sup>

14. The Appellate Body concluded that while expired subsidies can give rise to adverse effects, there is no requirement under Article 7.8 to remove these effects. The obligation to take appropriate steps to remove the adverse effects or withdraw the subsidy concerns the subsidies that continue to be granted or maintained by the implementing Member at the end of the implementation period. An implementing Member cannot be required to withdraw a subsidy that has ceased to exist. The Appellate Body also noted that it saw no basis, under Article 7.8 of the

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<sup>28</sup> Appellate Body Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, paras. 5.376 – 5.379.

SCM Agreement, "to require that an implementing Member 'take appropriate steps to remove the adverse effects' of subsidies that no longer exist."<sup>29</sup>

### 1.2.3 Implication under Article 7.8 of the modification of the terms of a subsidy

15. In *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, the European Union argued that a "substantial modification" of the terms of a subsidized loan gives rise to a new financial contribution, which requires a new benefit assessment against a contemporaneous market benchmark.<sup>30</sup> The Panel recalled the Appellate Body's observations in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* and stated that "the question ... to be resolved, in the light of the European Union's submissions, is whether the [\*\*\*] amendment has aligned the terms of the A350XWB LA/MSF loan agreement with a market benchmark."<sup>31</sup> The Panel added:

"In the light of the prospective nature of WTO remedies, we understand that the alignment of an existing subsidized loan with a market benchmark need not result in the repayment of past subsidies provided under that loan, but rather, it must achieve non-subsidization with respect to the future operation of the loan."<sup>32</sup>

16. The Panel rejected the European Union's reliance on *Japan – DRAMS (Korea)* because that dispute addressed different legal and factual matters. The Panel explained that, in contrast to the German A350XWB agreement, the loans at issue in *Japan – DRAMS (Korea)* had not been characterized as a subsidy within the meaning of Article 1.1 of the SCM Agreement.<sup>33</sup> The Panel pointed out that the legal question in *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)* was the following:

"[W]hether the [\*\*\*] amendment should be understood to have created a *new* German A350XWB loan contract that must be considered *separately and independently* from the pre-existing *subsidized* A350XWB loan, when it comes to determining whether the subsidy provided under the pre-existing A350XWB loan contract has been withdrawn for the purpose of Article 7.8 of the SCM Agreement."<sup>34</sup>

17. The Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)* further considered that "the [\*\*\*] amendment to the German A350XWB LA/MSF agreement altered the rights of the German government and Airbus, but it did not bring into existence a *new* loan agreement."<sup>35</sup> The Panel therefore found that:

"[T]he original German A350XWB LA/MSF agreement continues to exist in a modified form, reflecting the revised repayment terms agreed through the [\*\*\*] amendment. In our view, this implies that, contrary to the European Union's contention, the appropriate benchmark against which to measure whether the [\*\*\*] amendment aligned the terms of the German A350XWB LA/MSF agreement with the market, is *not* a loan on the same or similar terms issued by a market lender *for the first time at the same moment as the amendment*."<sup>36</sup>

18. In this regard, the Panel stated that:

"[W]here funding under a subsidized loan agreement has already been disbursed and remains outstanding, an amendment to that loan to bring it into alignment with a market benchmark on a prospective basis would need to ensure that, all other things being equal, the revised repayment terms capture the overall cash-flow the market

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<sup>29</sup> Appellate Body Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 5.383.

<sup>30</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.129.

<sup>31</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.140.

<sup>32</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.140.

<sup>33</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.145.

<sup>34</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.143.

<sup>35</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.147.

<sup>36</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.147.

lender would have expected to achieve, *at the time the recipient originally entered into the government loan contract*, for the remaining duration of the particular loan."<sup>37</sup>

19. According to the Panel, such an approach "would ensure that the 'withdrawal' of a subsidy will depend upon a Member's own actions and decisions, as opposed to exogenous factors such as the general cost of finance in an economy."<sup>38</sup>

20. The Panel found that the same reasoning applies "*mutatis mutandis* in relation to the European Union's reliance on *Japan – DRAMS (Korea)* to support its submissions concerning the [\*\*\*] amendments to the A380 LA/MSF agreements."<sup>39</sup>

#### **1.2.4 Implication under Article 7.8 of the full repayment of a loan on its subsidized terms**

21. The Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)* disagreed with the European Union's contention that the repayment of the LA/MSF agreements removed the financial contribution provided to Airbus and thus brought the life of the subsidy to an end. The Panel pointed out that, contrary to the European Union's assertion, the first compliance panel in the same dispute did not discuss whether the removal of one of the constituent elements of a subsidy means that the subsidy no longer exists, but stated that "the repayment of a loan on its own subsidized terms might *not* amount to the 'removal' of a financial contribution."<sup>40</sup> The Panel considered that:

"[T]he full repayment of the *principal* disbursed under a subsidized loan can be best equated with the *provision* of a financial contribution in the form of a one-off cash grant (equivalent to the total savings resulting from below-market interest rates), *not the 'removal' of a subsidy*. In our view, to argue otherwise would mean that Members would have different compliance obligations under Article 7.8 of the SCM Agreement in relation to the withdrawal of subsidies affording recipients *the same amount of benefit*, simply because of the form of the financial contribution chosen to confer that benefit."<sup>41</sup>

22. The Panel concluded that "the repayment of a loan on subsidized terms should *not* be understood to bring the life of a subsidy to an end".<sup>42</sup> The Panel pointed out that the repayment of principal and interest under a subsidized loan is an inherent feature of this type of financial contribution, and that the performance of this essential requirement cannot define "both the provision *and* the withdrawal of a subsidy" for the purpose of Article 7.8 of the SCM Agreement.<sup>43</sup>

23. Referring to the Appellate Body statement in *EC and certain member States – Large Civil Aircraft* concerning the terms of Article 1 of the SCM Agreement, the Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)* found that "the life of a subsidized loan may come to an end in either of two situations: when the financial contribution and the benefit have been removed; or when only the benefit is removed."<sup>44</sup>

24. The Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)* further clarified that although "a Member has no compliance obligation under Article 7.8 with respect to expired subsidies", the repayment of a loan on subsidized terms does not necessarily mean that the subsidy has expired and it does not "remove", "return" or "withdraw" the subsidized loan.<sup>45</sup> For both a grant and a subsidized loan, "the life of the subsidy will depend upon the extent to which the recipient is continuing to use the subsidy for its originally intended purposes (in the European Union's example, the useful life of the purchased assets) without having repaid at least the

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<sup>37</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.149.

<sup>38</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.151.

<sup>39</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.217.

<sup>40</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.188.

<sup>41</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.196.

<sup>42</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.197.

<sup>43</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.198.

<sup>44</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.202.

<sup>45</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.203.

remaining value of the benefit associated with the original financial contribution on a prospective basis."<sup>46</sup>

### **1.2.5 Implication under Article 7.8 of the amortization of the benefit through the passage of time**

25. In *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, in discussing the withdrawal of a subsidy through the amortization of benefit, the Panel rejected the European Union's argument that the life of a subsidized loan may be determined on the basis of the expected repayment period. To the contrary, the Panel stated that "the life of the subsidy will depend upon the extent to which the recipient is continuing to use the financial contribution for its originally intended purpose without having repaid at least the remaining value of the benefit on a prospective basis."<sup>47</sup>

26. Furthermore, the Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)* noted that the Spanish A380 LA/MSF agreement had been amended twice, which constituted "intervening events", modifying the *ex ante* expectations.<sup>48</sup> The Panel thus found that "even by the European Union's own 'loan life' standard, the life of the Spanish A380 LA/MSF subsidy has not come to an end because the [\*\*\*] amendment extended the repayment terms beyond the contracting parties' *ex ante* expectations."<sup>49</sup>

### **1.2.6 Article 7.8 as a special or additional rule and procedure**

27. The Appellate Body in *US – Upland Cotton (Article 21.5 – Brazil)* noted that Article 7.8 of the SCM Agreement is one of the "special or additional rules and procedures on dispute settlement contained in the covered agreements" within Annex II of the DSU, which prevail over the general DSU rules and procedures to the extent of a conflict between them.<sup>50</sup>

28. In addition, the Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* elaborated on Article 7.8 of the SCM Agreement as a "special or additional rule and procedure" on dispute settlement:

"Article 7.8 specifies what an implementing Member must do following the adoption of a panel and/or Appellate Body report in which it is determined that any subsidy has caused adverse effects within the meaning of Article 5 of the SCM Agreement. In particular, Article 7.8 prescribes that any 'Member granting or maintaining such subsidy shall take appropriate steps to remove the adverse effects or shall withdraw the subsidy'. It follows that in order to determine whether an implementing Member has complied with the recommendations and rulings adopted by the DSB in cases involving actionable subsidies, one of the questions that an Article 21.5 panel will have to evaluate is whether the Member concerned has acted in conformity with the requirement to 'take appropriate steps to remove the adverse effects' or 'withdraw the subsidy'."<sup>51</sup>

29. However, the Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* cautioned that the fact Article 7.8 of the SCM Agreement is a "special or additional rule and procedure" within the meaning of DSU Annex II does not mean that Article 7.8 "must be applied in isolation to the rules of the DSU". Rather, "a first important part of the context of Article 7.8 are the rules of the DSU governing when and how WTO compliance obligations are incurred and discharged."<sup>52</sup>

30. The Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* highlighted various provisions of the DSU – such as Articles 19.1 (obligation to bring WTO-

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<sup>46</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.203.

<sup>47</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.239.

<sup>48</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.243.

<sup>49</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – EU)*, para. 7.244.

<sup>50</sup> Appellate Body Report, *US – Upland Cotton*, para. 235; see also Appellate Body Reports, *Guatemala – Cement I*, fn 55; *US – FSC*, para. 159.

<sup>51</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.2.

<sup>52</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.804.

inconsistent measure into conformity), 21.1 (prompt compliance with the recommendations and rulings of the Dispute Settlement Body), 21.5 (process by which disputing parties resolve disagreement with the existence or consistency of measures taken to comply), 3.2 (preservation of Members' rights and obligations under the covered agreements), 3.4 (satisfactory settlement of the matter), and 3.7 (mutually acceptable solutions) – as relevant context to the interpretation of Article 7.8.<sup>53</sup> On that basis, the Panel concluded that "one of the fundamental objectives of Article 7.8 of the SCM Agreement must be to bring an implementing Member found to have caused adverse effects to the interests of another Member back into conformity with its obligations under Article 5 of the SCM Agreement."<sup>54</sup> The Panel found additional support for this approach in WTO case law.<sup>55</sup>

### **1.2.7 Relationship with other provisions of the SCM Agreement**

#### **1.2.7.1 Article 4.7**

31. In the context of its finding that the phrase "withdraw the subsidy" under Article 4.7 referred to retrospective remedies (repayment), the Panel in *Australia – Automotive Leather II (Article 21.5 – US)* considered Article 7.8 and the phrase "shall take appropriate steps to remove the adverse effects or shall withdraw the subsidy" therein.

### **1.3 Article 7.9 and 7.10**

#### **1.3.1 Meaning of "countermeasures ... commensurate with the degree and nature of the adverse effects determined to exist"**

##### **1.3.1.1 "countermeasures"**

32. The Arbitrator in *US – Upland Cotton (Article 22.6 – US II)* developed a detailed interpretation of the expression "countermeasures ... commensurate with the degree and nature of the adverse effects determined to exist". With respect to the term "countermeasures", the Arbitrator stated that:

"We note at the outset that the term 'countermeasures' is used to designate retaliatory measures in the WTO Agreement only in the *SCM Agreement*. This contrasts with the terms of Article 22 of the DSU, which refers to the 'suspension of concessions or other obligations'. However, it is not argued by either party in these proceedings that the term 'countermeasures' would designate, in the *SCM Agreement*, anything other than a temporary suspension of certain obligations, and this is what we understand this term to refer to.

The prefix 'counter-' can be defined as meaning 'against, in return'. The Oxford English Dictionary further cites the term 'counter-measure' as an illustration of a situation in which this prefix is used to indicate something that is '[d]one, directed, or acting against, in opposition to, as a rejoinder or reply to another thing of the same kind already made or in existence'. Another dictionary defines the term 'countermeasure' as an 'action or device designed to negate or offset another'.

...

We are not convinced that the use of the term 'countermeasures' necessarily connotes, in and of itself, an intention to refer to retaliatory action that 'goes beyond the mere rebalancing of trade interests', as Brazil suggests. As noted above, the term indicates that the action is taken in response to another, in order to 'counter' it. This does not necessarily connote, in our view, an intention to 'go beyond' a rebalancing of trade interests. Indeed, we are not convinced that the dictionary meanings of the term, in and of themselves, provide any compelling guidance as to the exact *level* of

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<sup>53</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, paras. 6.805-6.812.

<sup>54</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.813.

<sup>55</sup> Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, paras. 6.814-6.819.



countermeasures that may be permissible under Article 7.9 of the *SCM Agreement*. We also note that the term 'countermeasures' is similarly used in Article 4.10 of the *SCM Agreement*, where the permissible level of countermeasures is defined differently, in terms of 'appropriateness'.

...

We note that the term 'countermeasures' is the general term used by the ILC in the context of its Articles on State Responsibility to designate temporary measures that injured States may take in response to breaches of obligations under international law. This has been noted by arbitrators in the context of interpreting Article 4.10 of the *SCM Agreement*.

We agree that this term, as understood in public international law, may usefully inform our understanding of the same term as used in the *SCM Agreement*. Indeed, we find that the term 'countermeasures', in the *SCM Agreement*, describes measures that are in the nature of countermeasures as defined in the ILC's Articles on State Responsibility.

At this stage of our analysis, we therefore find that the term 'countermeasures' essentially characterizes the *nature* of the measures to be authorized, i.e. temporary measures that would otherwise be contrary to obligations under the relevant WTO Agreement(s) and that are taken in response to a breach of an obligation under the *SCM Agreement*. This is also consistent with the meaning of this term in public international law as reflected in the ILC Articles on State Responsibility."<sup>56</sup>

#### **1.3.1.2 "commensurate with the degree and nature"**

33. In the context of providing a detailed interpretation of the expression "countermeasures ... commensurate with the degree and nature of the adverse effects determined to exist", the Arbitrator in *US – Upland Cotton (Article 22.6 – US II)* considered the term "commensurate":

"Dictionary definitions of this term include: 'equal in measure or extent: coextensive' and 'corresponding in size, extent, amount, or degree: proportionate', 'of equal extent, coextensive'.

In light of these elements, we agree that the term 'commensurate' essentially connotes a 'correspondence' between two elements. In the context of Article 7.9, the 'correspondence' is between the countermeasures and the 'degree and nature of the adverse effects determined to exist'.

...

We agree that the term 'commensurate' does not suggest that exact or precise equality is required, between the two elements to be compared, i.e. in this case, the proposed countermeasures and the 'degree and nature of the adverse effects determined to exist'. To that extent, we agree that the term 'commensurate' connotes a less precise degree of equivalence than exact numerical correspondence. Nonetheless, the term 'commensurate' does indicate, in our view, a relationship of *correspondence* and proportionality between the two elements, and not merely a relationship of 'adequacy' or 'harmony' as suggested by Brazil. We do not exclude that this correspondence may be qualitative as well as quantitative. The exact nature of the correspondence at issue will further be informed by the identification of what exactly the proposed countermeasures are required to be 'commensurate' with. This is defined through the terms 'the degree and nature of the adverse effects determined to exist'."<sup>57</sup>

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<sup>56</sup> Decision by the Arbitrator, *US – Upland Cotton (Article 22.6 – US II)*, paras. 4.24-4.32.

<sup>57</sup> Decision by the Arbitrator, *US – Upland Cotton (Article 22.6 – US II)*, paras. 4.36-4.39.



34. The Arbitrator in *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)* further clarified that the "commensurateness" standard may not require exact equivalence between the level of the proposed countermeasures and the adverse effects found to exist.<sup>58</sup>

35. Regarding the terms "degree and nature", the Arbitrator in *US – Upland Cotton (Article 22.6 – US II)* stated that:

"We agree that the reference to both the 'degree' and the 'nature' of the adverse effects determined to exist suggests that the correspondence that is required to exist, between the proposed countermeasures and the 'degree and nature of the adverse effects', may encompass both quantitative and qualitative elements. The 'degree' of the effects could be understood as a quantitative element, whereas the reference to the 'nature' of the adverse effects seems to point to something more qualitative.

...

We agree that the reference to the 'nature' of the adverse effects may be understood to refer to the different 'types' of adverse effects that are foreseen in Articles 5 and 6, and that this therefore invites a consideration of the specific type of 'adverse effects' that have been determined to exist as a result of the specific measure in relation to which countermeasures are being requested. These effects could manifest themselves in a variety of ways, each reflecting a specific type of trade distortion.

...

... In assessing the 'commensurateness' of the proposed countermeasures to the 'degree and nature' of the adverse effects determined to exist, we are entitled to take into account fully the 'degree and nature' of these adverse effects as they present themselves in the case at hand, but we are not permitted to do more than that. In other words, the 'degree and nature' of the adverse effects determined to exist in the case at hand constitute the entirety of what we may and must consider in assessing the 'commensurateness' of the proposed countermeasures in that case."<sup>59</sup>

36. The Arbitrator in *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)* noted that, in accordance with its mandate under Article 7.10 of the SCM Agreement, the maximum level of annual suspension to be applied by the complainant (i.e. the 2015 annualized value) must be "commensurate" with the annualized value of adverse effects determined to exist. The Arbitrator therefore examined whether the level of countermeasures proposed by the complainant was "commensurate" with the 2015 annualized value of adverse effects.<sup>60</sup>

37. The Arbitrator recalled that it had calculated the 2015 annualized value to be USD 3,993,212,564, but that the complainant had calculated it as USD 8,581,019,068. The Arbitrator thus examined whether the complainant's value of USD 8,581,019,068 could be considered "commensurate" with the 2015 annualized value calculated by the Arbitrator.<sup>61</sup>

38. The Arbitrator considered that the phrase "commensurate with" within the meaning of Article 7.10 connotes a correspondence of a "less precise degree of equivalence than exact numerical correspondence" between the "adverse effects determined to exist" and "countermeasures" proposed. Nevertheless, the Arbitrator noted that the complainant did not request that it be allowed to take countermeasures in the form of a maximum level of annual suspension higher than the annualized value of adverse effects. The Arbitrator also considered that any adjustment from its valuation of USD 3,993,212,564 to the complainant's valuation of USD 8,581,019,068 would be too significant to represent a permissible degree of discrepancy:

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<sup>58</sup> Decision by the Arbitrator, *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)*, para. 6.508.

<sup>59</sup> Decision by the Arbitrator, *US – Upland Cotton (Article 22.6 – US II)*, paras. 4.41-4.47. See also Decision by the Arbitrator, *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)*, para. 6.45.

<sup>60</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, paras. 6.313 and 6.322.

<sup>61</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.322.

"The phrase 'commensurate with' within the meaning of Article 7.10 of the SCM Agreement connotes a correspondence of a 'less precise degree of equivalence than exact numerical correspondence' between the 'adverse effects determined to exist' and 'countermeasures' proposed.<sup>62</sup> The European Union, however, does not request that it be allowed to take countermeasures in the form of a maximum level of Annual Suspension higher than the annualized value of adverse effects (nor do we perceive any justification for doing so in the circumstances of this proceeding). We further note that our calculated 2015 Annualized Value of adverse effects (i.e. USD 3,993,212,564) is significantly lower than the European Union's proposed 2015 Annual Suspension Value (i.e. USD 8,581,019,068), a value that we have determined in this Decision was derived from an at-times flawed methodology. Even assuming that, as a general matter, the commensurateness standard could permit some limited degree of discrepancy between the proposed level of countermeasures and the value of the adverse effects determined to exist, an adjustment from USD 3,993,212,564 to USD 8,581,019,068 would in our view exceed, by far, any permissible degree of discrepancy. We are accordingly unable to accept USD 8,581,019,068 as the 'commensurate' 2015 Annualized Value."<sup>63</sup>

### **1.3.1.3 "the adverse effects determined to exist"**

39. The Arbitrator in *US – Upland Cotton (Article 22.6 – US II)* considered that "the adverse effects determined to exist" refers to the findings on adverse effects made by the Panel/Appellate Body in the underlying proceedings:

"Brazil observes that the term 'adverse effects determined to exist' sends the treaty interpreter back to the precise findings on adverse effects made by the panels and the Appellate Body as these constitute the 'adverse effects determined to exist'. We agree.

The expression 'adverse effects determined to exist' refers us to the specific 'adverse effects' within the meaning of Articles 5 and 6 of the *SCM Agreement* that form the basis of the underlying findings in the case at hand.

We note in this respect that Article 5 of the *SCM Agreement* identifies three categories of 'adverse effects to the interests of other Members', that 'no Member should cause, through the use of any subsidy referred to in paragraphs 1 and 2 of Article 1'. These are:

- (a) injury to the domestic industry of another Member;
- (b) nullification or impairment of benefits accruing directly or indirectly to other Members under GATT 1994 in particular the benefits of concessions bound under Article II of GATT 1994;
- (c) serious prejudice to the interests of another Member.'

Article 7.1 further provides the possibility for any WTO Member to request consultations with another Member, whenever it has reason to believe that 'any subsidy referred to in Article 1, granted or maintained by another Member, results in injury to its domestic industry, nullification or impairment or serious prejudice'.

In principle, therefore, the 'adverse effects determined to exist' in the underlying proceedings ultimately leading to a request for countermeasures under Article 7.9 of the *SCM Agreement* may be in the form of injury to the domestic industry of a

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<sup>62</sup> Decision by the Arbitrator, *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)*, para. 5.4 (citing Decision by the Arbitrator, *US – Upland Cotton (Article 22.6 – US II)*, paras. 4.35-4.39). See also section 6.4.5.1 above.

<sup>63</sup> See Decision by the Arbitrator, *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)*, paras. 6.505-6.509 (resolving the same issue similarly).

Member, nullification or impairment, or serious prejudice to the interests of another Member." <sup>64</sup>

40. In *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), the parties disagreed as to whether the adverse effects caused by the pre-2007 aeronautics R&D subsidies in the reference period in the original proceeding (i.e. 2004-2006 R&D Adverse Effects) could have been assigned a value for purposes of applying countermeasures. Specifically, the parties disagreed as to whether the 2004-2006 R&D adverse effects had satisfied the "trigger condition" encompassed in the following phrase at the beginning of Article 7.9 of the SCM Agreement: "[i]n the event the Member has not taken appropriate steps to remove the adverse effects of the subsidy or withdraw the subsidy within six months from the date when the DSB adopts the panel report or the Appellate Body report ...". Should the 2004-2006 R&D adverse effects satisfy this "trigger condition", these adverse effects would fall within the scope of the phrase "the adverse effects determined to exist" in Article 7.10 of the SCM Agreement and could then be assigned value for the purposes of applying countermeasures.<sup>65</sup>

41. The Arbitrator noted that, at the end of the compliance proceedings in this dispute, the DSB had not been presented with any findings that the pre-2007 aeronautics R&D subsidies had caused adverse effects *in the post-implementation period*. Additionally, according to the Arbitrator, the DSB had not been presented with any findings that the respondent had brought these subsidies into compliance with the DSB's recommendations and rulings from the original proceedings. Specifically, the Arbitrator stated the following in this regard:

"The Arbitrator recalls that, at the end of the compliance proceedings, the Appellate Body reversed the compliance panel's findings that the European Union had failed to establish that the pre-2007 aeronautics R&D subsidies still caused adverse effects after the end of the implementation period. However, the Appellate Body was unable to complete the analysis as to whether there remained acceleration effects of the pre-2007 aeronautics R&D subsidies in the post-implementation period. Thus, at this time, there are no findings adopted by the DSB as to whether the pre-2007 aeronautics R&D subsidies cause adverse effects in the post-implementation period. Relatedly, there are also no DSB-adopted findings as to whether the United States brought the pre-2007 aeronautics R&D subsidies into compliance with the recommendations and rulings of the DSB issued as a result of the original proceeding by the end of the implementation period."<sup>66</sup>

42. The complainant had also clarified that its position was not that the 2004-2006 R&D adverse effects continued to exist in the post-implementation period. Rather, the complainant considered that the Arbitrator should value the 2004-2006 R&D adverse effects even in the absence of an affirmative finding of non-compliance in the post-implementation period.<sup>67</sup>

43. After evaluating the parties' arguments and making the observations above, the Arbitrator addressed whether Article 7.9 imposes a condition requiring that "the adverse effects determined to exist" in the meaning of Article 7.10 must be those caused *in the post-implementation period* by a subsidy that fails to comply with the DSB's recommendations and rulings following the original proceedings. Specifically, the Arbitrator set out to determine the following:

"[W]hether Article 7.9 creates a condition that 'the adverse effects determined to exist' within the meaning of Article 7.10 must be those caused in the post-implementation period by a subsidy with respect to which an original respondent has failed to comply with previously issued recommendations and rulings of the DSB. Understanding the relationship between Article 7.9 and Article 7.10 is critical for determining what, if any, scope the Arbitrator has within its mandate to value the 2004-2006 R&D Adverse Effects because, as the European Union argues, Article 7.10,

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<sup>64</sup> Decision by the Arbitrator, *US – Upland Cotton* (Article 22.6 – US II), paras. 4.49-4.53.

<sup>65</sup> See Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), paras. 6.15-6.27.

<sup>66</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.27.

<sup>67</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.26.

which establishes the Arbitrator's mandate, places no explicit limitations on the scope of what may comprise 'the adverse effects determined to exist'"<sup>68</sup>

44. The Arbitrator began its analysis by reviewing Article 7.10 of the SCM Agreement. The Arbitrator considered that a reasonable interpretation of the term "countermeasures" refers to "measures taken to act against, or in response to, a failure to remove the adverse effects of, or withdraw, an actionable subsidy within the required time-period".<sup>69</sup> The Arbitrator thus concluded that countermeasures should only be determined and applied *vis-à-vis* a subsidy with respect to which the respondent has failed to comply by the end of the implementation period, i.e. a subsidy that has not been withdrawn and still causes adverse effects in the post-implementation period.<sup>70</sup> Specifically, the Arbitrator stated the following:

"Article 7.10 does not specify whether 'the adverse effects determined to exist' must be those caused in the post-implementation period by a subsidy with respect to which the respondent has failed to comply with previously issued recommendations and rulings of the DSB. However, we note that the term 'countermeasures' has been (in our view, instructively) interpreted by both previous arbitrators operating under Article 7.10 as referring to 'measures taken to counteract' something, and specifically ... measures taken to act against, or in response to, a failure to remove the adverse effects of, or withdraw, an actionable subsidy within the required time-period'. This appears a reasonable interpretation in the light of the purpose of countermeasures, which is to induce a respondent's compliance. Thus, the nature of countermeasures suggests that countermeasures should only be determined and applied *vis-à-vis* a subsidy with respect to which the respondent has failed to comply by the end of the implementation period, i.e. a subsidy that has not been withdrawn and still causes adverse effects in the post-implementation period."<sup>71</sup>

45. The Arbitrator then took into account, *inter alia*, the context provided by Article 7.9 of the SCM Agreement, including the first part of Article 7.9. The Arbitrator noted that the first part of Article 7.9 triggers the obligation of the DSB to grant authorization for the application of countermeasures. This "trigger event" is the failure by the respondent to comply with the recommendations and rulings adopted by the DSB, issued following an original panel (and perhaps appellate) proceeding before the end of the six-month implementation period specified in Article 7.8. In the Arbitrator's view, Article 7.9 establishes that, for countermeasures to be authorized with respect to a particular subsidy, that subsidy must still cause adverse effects *in the post-implementation period*:

"Article 7.9 has two relevant parts. The latter part of Article 7.9 provides the basis for the DSB to 'grant authorization to the complaining Member to take countermeasures, commensurate with the degree and nature of the adverse effects determined to exist'. The former part conditions the DSB's authorization to grant such countermeasures with respect to a given 'subsidy' on the occurrence of an 'event' *vis-à-vis* that subsidy, which the parties refer to as a 'trigger' event. The 'trigger' event is the respondent's failure to comply with the recommendations and rulings of the DSB issued as a result of an original proceeding before the end of the six-month implementation period specified in Article 7.8. As per the terms of Article 7.8, that status of non-compliance arises if the respondent has neither withdrawn the subsidy nor taken appropriate steps to remove its adverse effects. It follows, therefore, that Article 7.9 establishes that, for countermeasures to be authorized with respect to a particular subsidy, that subsidy must still cause adverse effects *in the post-implementation period*. Accordingly, 'the adverse effects determined to exist', within the meaning of Article 7.9, must be those caused *in the post-implementation period* by a subsidy with respect to which a respondent has failed to comply with the DSB recommendations and rulings."<sup>72</sup>

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<sup>68</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.28.

<sup>69</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.31.

<sup>70</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.31.

<sup>71</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.31.

<sup>72</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.33.

46. The Arbitrator then turned to the relationship between Articles 7.9 and 7.10 of the SCM Agreement. The Arbitrator noted that an arbitration occurring under Article 7.10 is a step that occurs *before* the DSB authorizes countermeasures pursuant to the latter part of Article 7.9. The Arbitrator also noted that the overarching procedural purpose of an arbitration conducted under Article 7.10 is to advise the DSB as to what constitutes "countermeasures, commensurate with the degree and nature of the adverse effects determined to exist". The Arbitrator thus concluded that this additional context had supported its conclusions about the scope of the phrase "the adverse effects determined to exist" in Article 7.10:

"In the light of the above observations regarding Article 7.9, we note that Articles 7.9 and 7.10 are closely connected and should be read together. The procedures that they prescribe are intertwined both temporally and substantively. Indeed, an arbitration occurring under Article 7.10 is a step that occurs *before* the DSB authorizes countermeasures pursuant to the latter part of Article 7.9. Moreover, the overarching procedural purpose of an arbitration conducted under Article 7.10 is to advise the DSB as to what constitutes 'countermeasures, commensurate with the degree and nature of the adverse effects determined to exist'. We thus consider that the phrase 'the adverse effects determined to exist' should be interpreted the same way in Articles 7.9 and 7.10. That being the case, we consider that the scope of the phrase 'the adverse effects determined to exist' within the context of both Articles 7.9 and 7.10 is limited to adverse effects caused in the post-implementation period by a subsidy with respect to which a respondent has failed to comply with previously issued DSB recommendations and rulings. Indeed, if this were not the case, Article 7.10 may incongruously direct an arbitrator to advise the DSB to authorize something that the DSB is not permitted to authorize under the terms of Article 7.9."<sup>73</sup>

47. The Arbitrator subsequently noted the textual connections between Articles 22.2 and 22.6 of the DSU, on the one hand, and Articles 7.9 and 7.10, on the other hand. Specifically, the Arbitrator highlighted that Article 22.6 of the DSU is cross-referenced in Article 7.10 of the SCM Agreement, and that Articles 22.2 and 22.6 of the DSU contain conditional language similar to Article 7.9 of the SCM Agreement.<sup>74</sup> The Arbitrator then referred to an interpretation of Articles 22.2 and 22.6 of the DSU providing that the "nullification or impairment" to be valued by an arbitrator is that caused by a measure: (a) that has been evaluated in terms of whether a respondent has failed to comply with DSB recommendations and rulings, and (b) *that exists at the end of the deadline to comply*. In the light of this interpretation and the textual connections mentioned above, the Arbitrator considered that arbitrators under Article 7 of the SCM Agreement should also value the effects of measures that result from the respondent's failure to comply with the DSB's recommendations and rulings:

"The arbitrator in *EC – Bananas III (US) (Article 22.6 – EC)* explained that the language of Articles 22.2 and 22.6 of the DSU 'confirm[ed]' that 'any assessment of the level of nullification or impairment [as mandated under Article 22.7 of the DSU] presupposes an evaluation of consistency or inconsistency with WTO rules of the implementation measures taken by the [respondent]'. In other words, the 'nullification or impairment' that should be valued by an arbitrator under Article 22.7 is that caused by: (a) a measure with respect to which there has been an evaluation regarding whether the responding Member failed to comply with recommendations and rulings of the DSB; and (b) that exists at the end of deadline to comply. We agree with this interpretation of Articles 22.2 and 22.6. We further recall that suspension of concessions or other obligations authorized under Article 22 of the DSU and countermeasures authorized under Article 7 of the SCM Agreement have the same purpose, i.e. to induce compliance. Thus, we observe that there is no compelling reason to conclude that Article 22 of the DSU and Article 7 of the SCM Agreement should be interpreted differently in this specific context. That is, under both provisions, arbitrators should value the effects of measures that occur as a result of the failure of the respondent to comply with the relevant recommendations and rulings of the DSB."<sup>75</sup>

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<sup>73</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.34.

<sup>74</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.35.

<sup>75</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.35.

48. In conclusion, for multiple reasons, principally those referenced above, the Arbitrator found that "the adverse effects determined to exist", within the meaning of Article 7.10 of the SCM Agreement, are those caused *in the post-implementation period* by a subsidy with respect to which a respondent has failed to comply with the recommendations and rulings of the DSB.<sup>76</sup>

49. The Arbitrator then turned to consider whether the 2004-2006 R&D adverse effects could have been considered as among, or somehow representing, "the adverse effects determined to exist" within the meaning of Article 7.10.<sup>77</sup>

50. Among the arguments raised by the complainant that the 2004-2006 R&D adverse effects had qualified as "the adverse effects determined to exist", the Arbitrator examined the complainant's argument that "the European Union ha[d] established non-compliance *in the compliance proceedings* with respect to the B&O tax rate reduction".<sup>78</sup> The Arbitrator highlighted that the subsidies at issue for the purposes of the 2004-2006 R&D adverse effects were *not* the B&O tax rate reduction, but the pre-2007 aeronautics R&D subsidies, and thus the complainant's argument was inapposite.<sup>79</sup> Nevertheless, the Arbitrator did not discount the possibility, more generally, that an arbitrator could take into account an agreement or the lack of disagreement between the parties to address compliance-related issues:

"We recognize that the United States broaches the possibility that an agreement between the parties might suffice as to satisfy relevant conditions imposed by Article 7.9 of the SCM Agreement. We do not exclude the possibility that party agreements (or perhaps even lack of disagreements) with respect to compliance-related issues could be taken into account by an arbitrator."<sup>80</sup>

51. The Arbitrator then turned to examine the complainant's argument that the Arbitrator could determine whether the pre-2007 aeronautics R&D subsidies had caused adverse effects in the post-implementation period, and thus, whether the "trigger" condition in Article 7.9 would subsequently be satisfied *vis-à-vis* the pre-2007 aeronautics R&D subsidies.<sup>81</sup> The Arbitrator considered that, as its mandate under Article 7.10 is silent on this matter, it was not required to address this issue. The Arbitrator also stated that, were it to have the discretion to engage with compliance-related inquiries of this kind, it would decline to do so:

"Our mandate under Article 7.10 is silent as to determining a respondent's compliance status – a determination that involves, in this case, evaluating whether the pre-2007 aeronautics R&D subsidies cause adverse effects in the post-implementation period. We thus consider that we are not required to address this compliance issue. We further consider that we need not determine whether an arbitrator acting under Article 7.10 of the SCM Agreement has the discretion to engage in compliance-related inquiries of this kind, because even if we had such discretion, we would decline to exercise it in these circumstances."<sup>82</sup>

### **1.3.2 Purpose of countermeasures under Article 7.9**

52. The Arbitrator in *US – Upland Cotton (Article 22.6 – US II)* considered the purpose of countermeasures under Article 7.9 to be essentially the same as countermeasures under Article 4.10 of the SCM Agreement and retaliatory measures under Article 22.4 of the DSU:

"The question of the objective of retaliatory measures in the WTO has been addressed in the context of proceedings under Article 22.4 of the DSU. The arbitrator on *EC – Bananas III (US) (Article 22.6 – EC)* thus found that:

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<sup>76</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.38.

<sup>77</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.39.

<sup>78</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.41.

<sup>79</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.41.

<sup>80</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, fn 180 to para. 6.41.

<sup>81</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.42.

<sup>82</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.43.

'[T]he overall objective of compensation or the suspension of concessions or other obligations as described in Article 22.1:

'Compensation and the suspension of concession or other obligations are temporary measures available in the event that the recommendations or rulings are not implemented within a reasonable period of time. However, neither compensation nor the suspension of concessions or other obligations is preferred to full implementation of a recommendation to bring a measure into conformity with the covered agreements. Compensation is voluntary and, if granted, shall be consistent with the covered agreements.'

Accordingly, the authorization to suspend concessions or other obligations is a temporary measure pending full implementation by the Member concerned. We agree with the United States that this *temporary* nature indicates that it is the purpose of countermeasures to *induce compliance*. But this purpose does not mean that the DSB should grant authorization to suspend concessions beyond what is *equivalent* to the level of nullification or impairment. In our view, there is nothing in Article 22.1 of the DSU, let alone in paragraphs 4 and 7 of Article 22, that could be read as a justification for counter-measures of a *punitive* nature.'

This objective of suspension of concessions or other obligations under Article 22.4 of the DSU has been recently confirmed by the Appellate Body in *US – Continued Suspension*.<sup>83</sup> Arbitrators have also found that the objective of countermeasures under Article 4.10 of the *SCM Agreement* is to 'induce compliance'.<sup>84</sup>

We see no reason to assume that countermeasures under Article 7.9 of the *SCM Agreement* would serve a different purpose. The authorization of countermeasures in relation to actionable subsidies arises in circumstances comparable to those relating to countermeasures under Article 4.10 of the *SCM Agreement* or Article 22.4 of the DSU, i.e. in a situation where the responding Member has failed to comply with the recommendations and rulings of the DSB in the prescribed time period. As under Article 22.4 of the DSU and Article 4.10 of the *SCM Agreement*, countermeasures under Article 7.9 of the *SCM Agreement* constitute temporary measures taken in response to a continued breach of the obligations of the Member concerned, and pending full compliance with the recommendations and rulings of the DSB. We consider, therefore, that countermeasures under Article 7.9 of the *SCM Agreement* also serve to 'induce compliance'.<sup>85</sup>

### 1.3.3 Task of the Arbitrator

53. In *US – Upland Cotton (Article 22.6 – US II)*, the Arbitrator referred to Article 7.10 and described their mandate as follows:

"In these proceedings, we are therefore called upon to determine whether the countermeasures proposed by Brazil in relation to the marketing loans and countercyclical payments are "commensurate with the degree and nature of the adverse effects determined to exist" within the meaning of Article 7.9 of the *SCM Agreement*. ...

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<sup>83</sup> (footnote original) See Appellate Body Report, *US – Continued Suspension*, para. 309.

<sup>84</sup> (footnote original) See Decision by the Arbitrator, *US – FSC (Article 22.6 – US)*, para. 5.57; Decision by the Arbitrator, *Canada – Aircraft Credits and Guarantees (Article 22.6 – Canada)*, paras. 3.47-3.48; Decision by the Arbitrator, *Brazil – Aircraft (Article 22.6 – Brazil)*, paras. 3.44, 3.54, 3.57 and 3.58.

<sup>85</sup> Decision by the Arbitrator, *US – Upland Cotton (Article 22.6 – US II)*, paras. 4.57-4.59.

We agree that, in the event that we find that Brazil's proposed countermeasures are not commensurate with the degree and nature of the adverse effects determined to exist, we would be required also to determine what would constitute such countermeasures. This would enable the complaining party to seek an authorization consistent with our decision, as foreseen in Article 22.7 of the DSU. In order to fulfil this part of our mandate, we may be required to adopt an approach or methodology that differs from those proposed by the parties."<sup>86</sup>

54. In *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – United States)*, the Arbitrator noted that its arbitration proceeding was governed by both Article 7.10 of the SCM Agreement and Article 22.6 of the DSU. Highlighting that Article 22.7 of the DSU defines the mandate of the arbitrator somewhat differently than Article 7.10 of the SCM Agreement, and that Article 7.10 constitutes one of the "special or additional rules and procedures" listed in Appendix 2 of the DSU, the Arbitrator stated that it would conduct its arbitration with reference to the mandate set forth in Article 7.10 of the SCM Agreement:

"This arbitration proceeding is governed by both Article 7.10 of the SCM Agreement and Article 22.6 of the DSU.<sup>87</sup> Article 22.7 of the DSU defines the mandate for an arbitrator acting exclusively under Article 22.6; that is, the arbitrator 'shall determine whether the level of suspension is equivalent to the level of nullification or impairment' Article 7.10 of the SCM Agreement defines the mandate of an arbitrator somewhat differently. It states that in the event that a party to a dispute requests arbitration under Article 22.6 of the DSU, the arbitrator 'shall determine whether the countermeasures are commensurate with the degree and nature of the adverse effects determined to exist'. In accordance with the status of Article 7.10 of the SCM Agreement as one of the special or additional rules and procedures listed in Appendix 2 of the DSU, we conduct this arbitration with reference to the mandate set out in Article 7.10 of the SCM Agreement.

Articles 7.9 and 7.10 constitute 'special or additional rules and procedures' under Appendix 2 of the DSU. According to Article 1.2 of the DSU, '[t]o the extent that there is a difference between the rules and procedures of this Understanding and the special or additional rules and procedures set forth in Appendix 2, the special or additional rules and procedures in Appendix 2 shall prevail'.<sup>88</sup>

55. As required by its mandate under Article 7.10 of the SCM Agreement, the Arbitrator then stated that it was obliged to determine whether the countermeasures proposed by the complainant were "commensurate with the degree and nature of the adverse effects determined to exist". The Arbitrator added that, should it not find the requested countermeasures to be consistent with this principle, or should it find the complainant's methodology for calculating the countermeasures not to be appropriate, it could make its own determination as to the appropriate countermeasures or methodology:

"As indicated in Article 7.10, our mandate in this arbitration proceeding is to determine whether the countermeasures proposed by the European Union are 'commensurate with the degree and nature of the adverse effects determined to exist'. However, should we find that the level of countermeasures proposed by the European Union is not commensurate, we must go on to make our own determination of the level of countermeasures that is commensurate with the degree and nature of adverse effects determined to exist. Similarly, should we determine that the methodology proposed by the European Union for calculating the level of countermeasures, or any alternative methodology proposed by the United States, has

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<sup>86</sup> Decision by the Arbitrator, *US – Upland Cotton (Article 22.6 – US II)*, paras. 4.8, 4.16.

<sup>87</sup> (footnote original) Article 7.10 refers explicitly to a request for arbitration under Article 22.6 of the DSU, thereby confirming that arbitrations governed by Article 7.10 of the SCM Agreement are, at the same time, governed by Article 22.6 of the DSU. Article 4.11 of the SCM Agreement, which begins with an introductory clause that states: "In the event a party to the dispute requests arbitration under paragraph 6 of Article 22 of the [DSU]", likewise confirms that arbitrations under Article 4.11 are, at the same time, arbitrations under Article 22.6 of the DSU.

<sup>88</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, paras. 3.3-3.4.



shortcomings and is not appropriate, as presented, we may either make appropriate adjustments, or develop another, appropriate, methodology ourselves."<sup>89</sup>

56. Later in its decision, the Arbitrator noted that it had agreed with the analysis and reasoning in support of the DS316 arbitrator's conclusion as to the determination of the maximum level of countermeasures in its dispute. Specifically, according to the Arbitrator, the DS316 arbitrator had considered it permissible, under Article 7.10 of the SCM Agreement, to determine the maximum level of countermeasures in the form of annual suspension based on the value of the adverse effects determined to exist in the reference period of the compliance panel in that dispute.<sup>90</sup>

57. As noted by the Arbitrator, the DS316 arbitrator had found it consistent with its mandate under Article 7.10 to determine the maximum level of countermeasures based on specific instances of lost sales under Articles 6.3(a) and 6.3(b), and impedance under Article 6.3(c), of the SCM Agreement. These specific instances were determined to have existed in the DS316 compliance panel's reference period and were deemed to be the "adverse effects determined to exist" within the meaning of Article 7.10 of the SCM Agreement.<sup>91</sup> The DS316 arbitrator had further supported its conclusion on the basis that the maximum level of countermeasures would be maintained subject to the continued non-compliance of the respondent. The Arbitrator explained the DS316 arbitrator's rationale as follows:

"Moreover, the DS316 arbitrator considered that under the SCM Agreement and the DSU, the maximum level of countermeasures or suspension of concessions that may be authorized can be a function of the effects of relevant measures during a past reference period. However, the maintenance of suspension of concessions at that maximum level is predicated, not on the ongoing effects of the relevant measures, but on continued non-compliance of the responding party. The DS316 arbitrator accordingly concluded that it was appropriate to determine the maximum level of Annual Suspension based on the value of the adverse effects determined to exist in the temporally circumscribed compliance panel reference period and to grant countermeasures in the form of Annual Suspension."<sup>92</sup>

58. The DS353 Arbitrator's agreement with the DS316 arbitrator's analysis on this matter led the DS353 Arbitrator, in its preliminary ruling in Annex C-7 to its decision, to reject the United States' request to file an additional submission arguing that the recent elimination of the B&O tax rate reduction was a relevant consideration for the Arbitrator. The United States argued, *inter alia*, that the elimination of a WTO-inconsistent measure necessarily affects the maximum level of permitted countermeasures.<sup>93</sup> The Arbitrator rejected the United States' argument on the basis that no analysis regarding the presence of relevant adverse effects had been conducted *vis-à-vis* any time-period following the reference period used in the compliance proceedings. The Arbitrator also noted that the compliance reference period also occurred immediately after the time the United States should have come into compliance, and thus the adverse effects identified therein represent the harm to the European Union caused by the United States' failure to comply.<sup>94</sup>

### **1.3.4 Burden of proof**

59. In *US – Upland Cotton (Article 22.6 – US II)*, the Arbitrator considered that the approach taken to the burden of proof under Article 4.11 was equally applicable in the context of Article 7.10:

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<sup>89</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 3.5.

<sup>90</sup> See Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, paras. 6.49-6.51.

<sup>91</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.50.

<sup>92</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.50 (referring to Decision by the Arbitrator, *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)*, paras. 6.46-6.60 and 6.76).

<sup>93</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, Annex C-7, paras. 1.3 and 1.8.

<sup>94</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, Annex C-7, para. 9.

"In the context of proceedings under Article 4.11 of the *SCM Agreement* and Article 22.6 of the DSU, arbitrators have consistently determined that the party objecting to the proposed countermeasure bears the burden to establish a prima facie case or presumption that the countermeasures are not 'appropriate' within the meaning of Article 4.11 and that it is then up to the party proposing the countermeasures to rebut such presumption.<sup>95</sup>

The same approach applies, in our view, to proceedings under Article 22.6 of the DSU and Article 7.10 of the *SCM Agreement*. We therefore find that the United States bears the initial burden of establishing the countermeasures are not 'commensurate with the degree and nature of the adverse effects determined to exist' and that Brazil bears the burden of rebutting such conclusions.

The Arbitrator is also of the view that this allocation of burden of proof does not alleviate the burden on each party to establish the facts that it alleges during the proceedings. As observed by the arbitrator on *US – FSC (Article 22.6 – EC)*, 'it is generally for each party asserting a fact, whether complainant or respondent, to provide proof thereof'. Accordingly, it is also for Brazil to provide evidence in support of the facts that it advances. The Arbitrator will consider all the evidence and arguments provided by both parties (United States and Brazil) to determine whether the proposed countermeasures are 'commensurate with the degree and nature of the adverse effects determined to exist'.<sup>96</sup>

60. According to the Arbitrator in *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, the respondent bore the overall burden of demonstrating that the complainant's methodology results in countermeasures that are not "commensurate" within the meaning of Article 7.10 of the SCM Agreement:

"For present purposes, it is sufficient to state that we regard the United States, as the party challenging the proposed level of countermeasures, to bear the overall burden of demonstrating that the European Union's methodology results in countermeasures that are not 'commensurate' with the degree and nature of the adverse effects determined to exist. To discharge that burden, it is not sufficient for the United States merely to propose an alternative methodology that it asserts is more appropriate. Rather, the United States must engage with the methodology used by the European Union, in the sense that the United States must demonstrate why that methodology would result in countermeasures that are not 'commensurate' within the meaning of Article 7.10 of the SCM Agreement."<sup>97</sup>

61. The Arbitrator also considered that each party has the duty to produce evidence in support of its assertions of fact and to collaborate with an Article 22.6 arbitrator in presenting evidence:

"We agree with the DS316 arbitrator that each party has the duty to produce evidence in support of its assertions of fact and to collaborate with an Article 22.6 arbitrator in presenting evidence. Consistent with this duty and prior arbitrations, we requested that, as a first step in the proceeding, the European Union as the party seeking authorization to take countermeasures submit a methodology paper substantiating how it arrived at the proposed countermeasures."<sup>98</sup>

### **1.3.5 Article 7.9 as a special or additional rule and procedure**

62. In *US – Upland Cotton (Article 22.6 – US II)*, the Arbitrator were mindful that Article 7.9 establishes a special or additional rule and procedure under Appendix 2 of the DSU:

"The terms of Article 7.9 of the *SCM Agreement*, as a 'special or additional rule and procedure', should be interpreted on their own terms. It is clear that they may

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<sup>95</sup> (footnote original) See Decision of the Arbitrator, *Brazil – Aircraft (Article 22.6 – Brazil)*, paras. 2.8-2.9.

<sup>96</sup> Decision by the Arbitrator, *US – Upland Cotton (Article 22.6 – US II)*, paras. 4.12-4.14.

<sup>97</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 4.3.

<sup>98</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 4.4.

embody different rules, which would prevail in case of conflict. Nonetheless, Article 22.6 of the DSU remains relevant, as the general legal basis under which the proceedings are conducted. Indeed, Article 7.9 of the *SCM Agreement* refers expressly to Article 22.6 of the DSU as the legal basis for arbitral proceedings relating to countermeasures in relation to actionable subsidies."<sup>99</sup>

### 1.3.6 Article 7.10 arbitrations

63. The Arbitrator in *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)* considered that the arbitration in that case was covered by both Article 7.10 of the SCM agreement and Article 22.6 of the DSU. In contrast to Article 22.7, which defines the mandate of an arbitrator under an Article 22.6 arbitration, the mandate under Article 7.10 of the SCM Agreement "is to determine whether the countermeasures proposed by the United States are 'commensurate with the degree and nature of the adverse effects determined to exist'".<sup>100</sup> The Arbitrator further noted that Article 7.10 makes explicit reference to Article 22.6, "thereby confirming that arbitrations governed by Article 7.10 are, at the same time, governed by Article 22.6".<sup>101</sup>

#### 1.3.6.1 Events occurring outside the Reference Period

64. In considering events occurring outside the Reference Period, the Arbitrator in *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)* stated the following:

"[W]e emphasize that, insofar as we take into account in our assessment any particular evidence that was not available during the 2011-2013 Reference Period, we do so in order to place as accurate a value as reasonably possible on the orders that represent the lost sales that occurred in the 2011-2013 Reference Period, and not to alter adverse effects already established in the compliance proceedings or to establish any additional adverse effects. Instead, in our assessment we take into account evidence, including post-Reference Period evidence, only insofar as it sheds light on how we should quantify the adverse effects determined to exist in the 2011-2013 Reference Period."<sup>102</sup>

65. The Arbitrator in *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)* pointed out that Articles 5 and 6 of the SCM Agreement describe multiple types of adverse effects and that therefore Article 7.10 "clearly envisions that an arbitrator may assess multiple kinds of different adverse effects, the 'degree and nature' of which may differ."<sup>103</sup>

66. The Arbitrator in *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)* rejected the argument that it should calculate a countermeasures or suspension of concessions for individual product markets. In the view of the Arbitrator, "providing a single maximum level of Annual Suspension based on the 'degree and nature of the adverse effects determined to exist' is consistent with [the Arbitrator's] mandate."<sup>104</sup>

67. The Arbitrator in *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)* considered that its mandate under Article 7.10 to determine countermeasures that are "commensurate with the adverse effects determined to exist" meant, in its proceeding, that it would examine the value assigned to the identified lost sales and threat of impedance. One issue that arose in this regard was whether evidence of events pertaining to these lost sales and threatened impedance that occurred *after* the reference period and, therefore, was not available to the compliance panels and

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<sup>99</sup> Decision by the Arbitrator, *US – Upland Cotton (Article 22.6 – US II)*, para. 4.19.

<sup>100</sup> Decision by the Arbitrator, *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)*, para. 3.4.

<sup>101</sup> Decision by the Arbitrator, *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)*, para. 3.5.

<sup>102</sup> Decision by the Arbitrator, *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)*, para. 6.215.

<sup>103</sup> Decision by the Arbitrator, *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)*, para. 6.119.

<sup>104</sup> Decision by the Arbitrator, *EC and certain member States – Large Civil Aircraft (Article 22.6 – EU)*, para. 6.190.

the Appellate Body, could be taken into account by the Arbitrator in determining the value of these adverse effects.<sup>105</sup>

68. The Arbitrator considered that there was no reason for it not to consider facts in its valuation exercise solely because those facts were not available to the previous adjudicators in that proceeding. In arriving at this conclusion, the Arbitrator noted the lack of a legal impediment in the SCM Agreement or the DSU, the different focus of the arbitral proceeding as compared to that of an original or compliance panel proceeding, and the understanding that post-reference-period events do not disturb compliance findings regarding significant lost sales or threatened impedance:

"We observe that there is no legal impediment in the SCM Agreement or in the DSU for the Arbitrator to consider facts that were not on the record of a previously conducted proceeding in this dispute. Further, as was noted by the DS316 arbitrator, considering that the focus of an arbitration proceeding is different from that of an original or compliance proceeding, the factual information that is placed on the record of the arbitrator could differ from the factual information that forms part of the evidentiary records of previous original or compliance proceedings. Accordingly, there is no reason not to take information into account in the arbitrator's valuation exercise only because it was not available to the previous adjudicators in that proceeding.

We also discern no way in which considering events which occurred after the reference period in any way disturbs any findings of the compliance panel regarding either significant lost sales or threatened impedance. In our view, facts pertaining to events that would have occurred after the placement of the relevant LCA order (whether that order was the basis for the finding of significant lost sales or threat of impedance), including facts that arose after the reference period (e.g. cancellation of a delivery) could have a bearing on the ultimate value realized by Airbus from the counterfactual orders and deliveries by Airbus. Thus, if there is evidence on the record indicating that the ultimate value realized from a counterfactual order or delivery would have been affected by a subsequent event, we consider it appropriate to take that evidence into consideration in determining the value of the identified lost sale or threatened impeded delivery. Indeed, as the DS316 arbitrator recognized, not taking such evidence into account could result in the complaining party being granted countermeasures in response to a quantum of determined adverse effects that it would not have suffered in the counterfactual and would not be in keeping with Article 7.10."<sup>106</sup>

69. The Arbitrator also emphasized that it would consider evidence of post-reference-period events to place an accurate value on the adverse effects identified in the compliance proceedings. The Arbitrator added that it would not consider evidence of such events either to alter adverse effects established during the compliance proceedings or to establish additional adverse effects:

"Finally, we emphasize that, insofar as we take into account evidence that was not available during the reference period, we do so in order to place as accurate a value as reasonably possible on the adverse effects identified in the compliance proceedings, and not to alter adverse effects already found to exist in the compliance proceedings or to establish any additional adverse effects. Indeed, in our assessment we take into account evidence, including post-reference period evidence, only insofar as it sheds light on how we should quantify the adverse effects determined to exist, and thus assist us in determining a level of countermeasures that is commensurate with the degree and nature of those adverse effects."<sup>107</sup>

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<sup>105</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.62.

<sup>106</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), paras. 6.63-6.64.

<sup>107</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.65.

### 1.3.7 Relationship with other provisions of the SCM Agreement

#### 1.3.7.1 Article 4.10

70. The Arbitrator in *US – FSC (Article 22.6 – US)* referred to the wording of Articles 7.9 and 7.10 as context for the interpretation of Article 4.10 and considered that "the explicit precision of these indications [in Articles 7.9 and 7.10] clearly highlights the lack of any analogous explicit textual indication in Article 4.10 and contrasts with the broader and more general test of "appropriateness" found in Articles 4.10 and 4.11". For the Arbitrator, such a difference in the text "must be given a meaning."<sup>108</sup>

71. The Arbitrator in *US – Upland Cotton (Article 22.6 – US I)* contrasted the terms of Article 4.10 with the terms used in Article 7.9:

"[W]ithin the context of the *SCM Agreement*, the terms of Article 4.10 contrast with those of Article 7.9, which foresees, in relation to actionable subsidies, countermeasures 'commensurate with the degree and nature of the adverse effects determined to exist'. Here too, the terms of Article 7.9, through this reference to the 'degree and nature of the adverse effects determined to exist', point to a single specific benchmark as reference, and require the countermeasures to be 'commensurate' with this benchmark, which is carefully defined in relation to the specific adverse effects that form the basis of the underlying findings. These elements distinguish the terms of Article 7.9 from the terms of Article 4.10. This difference can be understood in the broader context of the *SCM Agreement*, where actionable subsidies may only be challenged to the extent that they result in certain enumerated adverse effects for other WTO Members. By contrast, prohibited subsidies are prohibited independently of any demonstration of adverse effects. In such cases, no specific 'adverse effects' will have been 'determined to exist' prior to the request for authorization to apply countermeasures, and therefore there are none that could be referred to."<sup>109</sup>

### 1.3.8 Conceptual issues regarding the valuation of certain adverse effects

72. The Arbitrator in *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)* examined conceptual issues raised by the complainant's proposed methodology. Specifically, the Arbitrator examined the concept of annualization and whether the complainant's proposed general methodologies to value the findings of the threat of impedance were consistent with its mandate.<sup>110</sup>

73. The Arbitrator first addressed the concept of annualization. The Arbitrator recalled that it had accepted the complainant's request that the countermeasures be structured in the form of annual suspension, i.e. setting one maximum level of countermeasures that the European Union may take per year until the authorization to take such countermeasures lapses. Both parties agreed that the maximum level of annual suspension was not the total aggregate value of the adverse effects determined to exist, but their *annualized* value. The annualized value was the value of the adverse effects determined to exist divided by the relevant number of months and multiplied by 12. The parties disagreed, however, as to the period of time over which to annualize the value of certain adverse effects.<sup>111</sup>

74. The Arbitrator stated that its understanding of the function, and propriety, of annualization arose from its mandate under Article 7.10 of the SCM Agreement. This mandate was to ensure that the level of countermeasures would be *commensurate* with the *degree and nature* of the adverse effects determined to exist. In the light of the definition of the term "commensurate" and the purpose of countermeasures to induce compliance, the Arbitrator considered that there should be a "relationship of correspondence and proportionality" between the maximum level of annual suspension and the *annualized* value of the adverse effects determined to exist:

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<sup>108</sup> Panel Report, *US – FSC (Article 22.6 – US)*, paras. 5.32-5.34.

<sup>109</sup> Decision by the Arbitrator, *US – Upland Cotton (Article 22.6 – US I)*, para. 4.98.

<sup>110</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.66.

<sup>111</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint) (Article 22.6 – US)*, para. 6.67.

"Our understanding of the function, and propriety, of annualization arises from our mandate. Article 7.10 of the SCM Agreement requires that the level of countermeasures be *commensurate* with the *degree and nature* of the adverse effects determined to exist. The term 'commensurate' indicates a 'relationship of correspondence and proportionality between the two elements', which may be 'qualitative as well as quantitative'. It will further be recalled that the purpose of countermeasures is to induce compliance, and, more concretely, to enable a complaining Member to inflict economic harm on the respondent to induce such compliance. Therefore, we observe that, under our mandate, there should be a 'relationship of correspondence and proportionality' between the maximum level of Annual Suspension and the *annualized* value of the adverse effects determined to exist. In other words, the maximum level of Annual Suspension should be 'commensurate with' the economic impact of the adverse effects determined to exist over one year as valued by the Arbitrator."<sup>112</sup>

75. Accordingly, the Arbitrator concluded that, in that proceeding, the choice of an appropriate period of annualization should be made with reference to a period over which the economic harm being measured had occurred.<sup>113</sup>

76. Subsequently, the Arbitrator turned to the valuation of the findings of threatened impedance. The complainant had proposed that the Arbitrator value the threatened impedance using a "lost sales" approach. This lost sales approach consisted of two steps. The first step consisted of the calculation of net delivery-date prices as part of a counterfactual in which Airbus LCA would have received certain opportunities that otherwise were not obtained:

"Under its lost sales approach, the European Union values the threat of impedance in the US and UAE markets, based on the 2011 Delta Airlines and 2008 Fly Dubai lost sales, respectively, in the same way that it values the significant lost sales findings in respect of the three lost sales that occurred in the post-implementation period (2013 Icelandair, 2013 Air Canada and 2014 Fly Dubai). Accordingly, the European Union calculates the net delivery-date prices of all of the Airbus LCA that would have been delivered in the counterfactual in the 2011 Delta Airlines and 2008 Fly Dubai campaigns, had Airbus rather than Boeing won those sales campaigns, and discounts those values back to the relevant order date to arrive at the expected value of those lost sales at the time of the order."<sup>114</sup>

Second, after restating the valuations in 2015 US dollars, the complainant annualized those valuations over the 33-month period that the complainant argued was the compliance panel's reference period.<sup>115</sup>

77. The parties disagreed on the time-period over which the resulting valuation should be allocated to provide an *annualized* value of the threat of impedance that was found to exist in the compliance panel's reference period.<sup>116</sup> Specifically, the respondent argued that annualizing the values identified by the complainant over the compliance panel's reference period, instead of over the 105 months over which all five of the lost sales underpinning the adverse effects findings occurred, *contradicted* the compliance panel's findings.<sup>117</sup>

78. The Arbitrator began its analysis by recalling that its mandate under Article 7.10 of the SCM Agreement requires that a maximum level of annual suspension is commensurate with the *nature* of the adverse effects determined to exist. The Arbitrator then noted the differences between the valuation of a lost sale, as occurring at the time of each order of LCA, and the valuation of impedance, as focusing on the value of a *delivery* logically at the time that the delivery occurred:

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<sup>112</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.68.

<sup>113</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.70.

<sup>114</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.77.

<sup>115</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.77.

<sup>116</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.81.

<sup>117</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.78.

"Our mandate under Article 7.10 of the SCM Agreement requires that a maximum level of Annual Suspension is commensurate with the *nature* of the adverse effects determined to exist. [L]ost sales occur at the time of the order for LCA. The valuation of a lost sale is thus order-centric, focusing on the value of the order logically at the time that the order occurred. By contrast, impedance refers to a phenomenon in which the imports or exports of the like product of the complaining Member would have expanded had they not been obstructed or hindered by the subsidized product, or did not materialize at all because production was held back by the subsidized product. In the context of the LCA industry, imports and exports of LCA are synonymous with *deliveries* of LCA to customers. The valuation of impedance is therefore focused on the value of a *delivery* logically at the time that the delivery occurred."<sup>118</sup>

79. Based on the differences between lost sales and impedance, the Arbitrator considered that a valuation of a threat of *impedance* as lost sales is inconsistent with the nature of impedance as a market phenomenon. The use of a lost sales approach, in the Arbitrator's view, valued a threat of impedance on the basis of the wrong event occurring at the wrong time:

"We consider that a valuation of a threat of *impedance* that is based on the valuation of the underlying lost sales, as lost sales, is inconsistent with the nature of impedance as a market phenomenon focused on the deliveries of LCA at the time that the deliveries occurred. Simply stated, a lost sales approach values a threat of impedance on the basis of the wrong event (the LCA order rather than the deliveries that result from the order) occurring at the wrong time (time of the LCA order rather than the times at which the deliveries occur). We are aware that the compliance panel's specific threat of impedance findings were dependent on findings of underlying lost sales. However, this fact does not, in our view, mean that it is reasonable to value the adverse effect of threat of impedance (concerning deliveries of LCA) as though it were the adverse effect of lost sales (concerning the loss of an LCA order). Moreover, in reaching this conclusion, we acknowledge that the value of an LCA order ultimately may be derived from delivery prices. But to obtain that order value one still must temporally adjust those prices to, and aggregate them at, the time of order. That coordinated temporal adjustment and associated aggregation make no sense if one focuses on the deliveries themselves as independent of the time of the associated order. We further see no basis to use a lost sales approach as some kind of acceptable alternate technical approach for the value of the deliveries at the time of delivery."<sup>119</sup>

80. Later in its decision, the Arbitrator addressed the disagreement between the parties as to whether it should value, as part of the compliance panel's threat of impedance findings, counterfactual deliveries of LCA that would have occurred in the reference period. Relatedly, the parties also disagreed on the appropriate annualization period for valuation of the counterfactual deliveries to comprise the threat of impedance findings. The Arbitrator considered that these two disagreements were based on differing perspectives as to the point in time at which the compliance panel situated itself when making the threat of impedance findings, and more generally, as to the nature of a *threat* of impedance as a specific form of economic harm.<sup>120</sup>

81. Given the Arbitrator's mandate under Article 7.10 and the fact that the *threat* of impedance was the relevant form of serious prejudice, the Arbitrator considered the nature of a *threat* of serious prejudice. The Arbitrator did so on the basis of a textual analysis of Article 6.3 of the SCM Agreement and footnote 13 to Article 5(c) thereof, which references Article XVI of the GATT 1994.<sup>121</sup>

82. In the Arbitrator's view, the reference to Article XVI of the GATT 1994 in footnote 13, coupled with the present-tense expression of serious prejudice in Article 6.3, indicates that the

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<sup>118</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.82.

<sup>119</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.83.

<sup>120</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), paras. 6.103-6.104.

<sup>121</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), paras. 6.107-6.109.

scope of serious prejudice under the SCM Agreement includes both present and threatened serious prejudice:

"Article 6.3 of the SCM Agreement is formulated in the present tense ('the effect of the subsidy is') when identifying the specific forms of economic harm that constitute serious prejudice for purposes of Article 5(c), including impedance of imports and exports under Articles 6.3(a) and (b). Footnote 13 to paragraph (c) of Article 5 provides that the term 'serious prejudice to the interests of another Member' is used in the SCM Agreement in the same sense as it is used in paragraph 1 of Article XVI of GATT 1994 'and includes threat of serious prejudice'.

Footnote 13 also references Article XVI of the GATT 1994[...]

The reference to Article XVI of the GATT 1994 in footnote 13, coupled with the present-tense expression of serious prejudice in Article 6.3, indicates that the scope of serious prejudice under the SCM Agreement includes both present and threatened serious prejudice, thereby aligning with Article XVI of the GATT 1994.<sup>122</sup> The SCM Agreement does not define a threat of serious prejudice, nor does it explain the relationship between serious prejudice as delineated in Article 6.3 and threat of serious prejudice, other than as provided in footnote 13."<sup>123</sup>

83. The Arbitrator then conducted a textual analysis of the term "threat" as it appears in footnote 13. The Arbitrator considered the ordinary meaning of the term, as supported by context provided by Article 4.1(b) of the Agreement on Safeguards, Article 3.7 of the Anti-Dumping Agreement, and Article 15.7 of the SCM Agreement. In the view of the Arbitrator, a threat of impedance is a forward-looking concept, i.e. impedance that has not yet occurred but will soon occur:

"A 'threat' is ordinarily understood as 'an indication of impending evil'. Something is 'impending' when it is 'about to fall or happen; hanging over one's head; imminent; or near at hand'. A threat of impedance, in our view, is therefore a forward-looking concept, i.e. impedance that has not yet occurred but will soon occur.

Instructive guidance by the Appellate Body accords with this understanding. The Appellate Body has discussed the concept of 'threat' in the context of interpreting the phrase 'threat of serious injury' in Article 4.1(b) of the Agreement on Safeguards, explaining that "threat" refers to something that 'has *not* yet occurred, but remains a future event whose actual materialization cannot, in fact be assured with certainty'. This understanding of threat as something that has not occurred at the relevant time, but that will occur at a future time is consistent also with the nature of threat of material injury in Article 3.7 of the Anti-Dumping Agreement and Article 15.7 of the SCM Agreement. We discern no reason to think that the nature of 'threat' in these

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<sup>122</sup> (footnote original) We observe a similar structure as regards the concept of injury in Article 5(a): footnote 11 to paragraph (a) of Article 5 provides that the term "injury to the domestic industry" is used in the same sense as it is used in Part V of the SCM Agreement. Part V (fn 45 to Article 15) provides that, unless otherwise specified, the term "injury" includes both present material injury and a "threat of material injury". The Anti-Dumping Agreement is structured in a similar way, with footnote 9 providing that the term "injury" shall, unless otherwise specified, be taken to mean material injury to a domestic industry, threat of material injury to a domestic industry or material retardation of the establishment of such an industry. Article 10.3 of the Anti-Dumping Agreement (dealing with retroactivity) states that, except as provided in paragraph 2 "where a determination of threat of injury or material retardation is made (but no injury has yet occurred) a definitive anti-dumping duty may be imposed only from the date of the determination of the threat of injury or material retardation", suggesting that threat of injury arises where material injury does not yet exist. The Agreement on Safeguards also separately defines "serious injury" and "threat of serious injury", with "serious injury" meaning a significant overall impairment in the position of a domestic industry while "threat of serious injury" means "serious injury that is clearly imminent in accordance with the provisions of paragraph 2."

<sup>123</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), paras. 6.109-6.111.



agreements and the threat of serious prejudice in the SCM Agreement should be interpreted differently."<sup>124</sup>

84. The Arbitrator also noted additional connections between Article 6.3 of the SCM Agreement and footnote 13 thereto, leading to the conclusion that the relationship between present serious prejudice in Article 6.3 and the threat of serious prejudice is temporal:

"More generally, the present tense formulation in Article 6.3 of the types of economic harm that constitute serious prejudice, when read with footnote 13 (indicating that serious prejudice includes threat of serious prejudice), suggest that the relationship between present serious prejudice in Article 6.3 and threat of serious prejudice, is temporal. We note that the way in which the Appellate Body has referred to the relationship between threatened and present serious prejudice is consistent with this understanding:

A claim of present serious prejudice relates to the existence of prejudice in the past, and present, and that may continue in the future. By contrast, a claim of threat of serious prejudice relates to prejudice that *does not yet exist*, but is imminent such that it will materialize in the near future. Therefore, a threat of serious prejudice claim does not necessarily capture and provide a remedy with respect to the same scenario as a claim of present serious prejudice.<sup>125</sup><sup>126</sup>

85. Finally, the Arbitrator considered the object and purpose of the inclusion of threat of serious prejudice as part of serious prejudice under Article 5(c) of the SCM Agreement. The Arbitrator noted that, as the assessment of serious prejudice in Article 6.3 is fundamentally backward-looking, and the threat of serious prejudice is included within the scope of serious prejudice, a claim under the latter allows a complainant to address subsidization without waiting to need for the harm to be manifest:

"Finally, we consider the object and purpose of the inclusion of threat of serious prejudice as part of serious prejudice within the meaning of Article 5(c) of the SCM Agreement. Part III of the SCM Agreement ('Actionable Subsidies') provides that specific subsidies give rise to the remedies in Article 7 *only* where they are demonstrated (*ex post*) to cause adverse effects to the interests of a complaining Member. Serious prejudice is one of these forms of adverse effects, as referred to in Articles 5(c) and 6.3. The present-tense formulation of serious prejudice in Article 6.3 means that the assessment of serious prejudice (and thus the WTO-consistency of a subsidy under Part III) is fundamentally *backward-looking*.

The inclusion of threat of serious prejudice within the scope of serious prejudice, in the context of the effects-based discipline of Part III of the SCM Agreement, enables Members to obtain remedies under Article 7 in respect of serious prejudice that does not presently exist but will exist in the future. A threat of serious prejudice claim is therefore a means to address subsidization that imminently threatens to cause economic harm, without needing to wait until that harm actually manifests. Understood in this context, a threat of serious prejudice is not a form of harm separate from the present form of the particular serious prejudice phenomena in Article 6.3. Rather, it addresses the same harm as the phenomena in Article 6.3, but from a forward-looking perspective because it has not yet occurred but can be expected to do so imminently.<sup>127</sup> This temporal difference between threatened and

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<sup>124</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), paras. 6.112-6.113.

<sup>125</sup> (*footnote original*) Appellate Body Report, *US – Upland Cotton* (Article 21.5 – Brazil), para. 244 (emphasis added). In saying that a threat of serious prejudice "does not necessarily capture and provide a remedy with respect to the same scenario as a claim of present serious prejudice", we understand the Appellate Body to mean that a threat of serious prejudice does not necessarily include present serious prejudice, because a threat, by definition, relates to something that does not yet exist.

<sup>126</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.116.

<sup>127</sup> (*footnote original*) If the drafters had intended that a threat of serious prejudice would be a distinct form of harm from the Article 6.3 phenomena, it is reasonable to expect that they would have done so by adding a paragraph (e) to Article 6.3 that says: "the effect of the subsidy is a threat of the effects set forth in

present serious prejudice also means that the argumentation and evidence in support of a claim of threat of serious prejudice will differ from that required to support a present serious prejudice claim."<sup>128</sup>

86. In the light of the above, the Arbitrator considered a threat of impedance to be a situation in which the threatened impedance has not yet manifested itself as impedance in the time-period considered by the adjudicator:

"The foregoing considerations lead us to expect that, when a threat of impedance is identified by a WTO adjudicator working with the disciplines of Part III of the SCM Agreement, the adjudicator would be referring to a situation whereby the threatened impedance has not yet manifested itself as impedance in the time-period considered by the adjudicator. In other words, we would expect that a panel makes a finding of threat of impedance when it is not yet able to observe the manifestation of the threatened impedance (i.e. impedance). Indeed, if this were not the case, it would appear to us that the line between findings of threat of serious prejudice and present serious prejudice would become, at minimum, significantly blurred."<sup>129</sup>

87. Later in its decision, the Arbitrator addressed the parties' disagreement as to whether, in its valuation of the adverse effects, it should include a probabilistic adjustment to the expected value of the lost revenues from each of the relevant sales campaigns to account for the alleged uncertainty of Airbus winning certain sales campaigns in its counterfactual.<sup>130</sup>

88. The Arbitrator began by noting that an assessment of lost sales normally involves a counterfactual assessment to establish that sales made by the subsidized firm(s) of the respondent would have been made instead by the competing firm(s) of the complainant:

"The Appellate Body has previously explained that 'lost sales' are sales that suppliers of the complaining Member 'failed to obtain' and that *instead were won* by suppliers of the respondent [M]ember. The Appellate Body has further explained that an assessment of lost sales normally entails a counterfactual assessment in order to establish that 'sales won by the subsidized firm(s) of the respondent Member *would have been made instead* by the competing firm(s) of the complaining Member'. The findings of significant lost sales in the compliance proceedings in this dispute were based on a counterfactual assessment that the Washington State B&O tax rate reduction contributed in a genuine and substantial way to determining the outcome of the relevant sales campaigns."<sup>131</sup>

89. The Arbitrator ultimately concluded that, once a legal finding is made that a subsidy causes significant lost sales within the meaning of Article 6.3(c), at the legal standard of "genuine and substantial" cause determined by the Appellate Body to be the appropriate legal standard under Article 6.3, the sales in question are sales that would have been won by the complainant, absent the subsidy:

"In sum, and as explained above, the counterfactual assessment reflected in the adopted findings from the compliance proceedings is that, absent the Washington State B&O tax rate reduction, Airbus would have won the five sales campaigns in question. Once there is a legal finding that a subsidy causes significant lost sales within the meaning of Article 6.3(c), it follows that the sales in question are sales that would have been won by the complaining Member, absent the subsidy. The Appellate Body upheld the compliance panel's causation findings, *at the genuine and substantial causation standard*. The European Union's methodology in this proceeding

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paragraphs (a) through (d) of this Article". On the contrary, the reference to threat of serious prejudice in a footnote to Article 5(c), the provision that sets forth the obligation not to cause adverse effects through the use of a subsidy, suggests that serious prejudice in Article 5(c) can be established where the market harm specified in Article 6.3 does not yet exist and not only when it has already occurred.

<sup>128</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), paras. 6.118-6.119.

<sup>129</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.120.

<sup>130</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.154.

<sup>131</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.162.

is consistent with the counterfactual assessment from the compliance proceedings, and with the findings of significant lost sales."<sup>132</sup>

90. The Arbitrator therefore rejected the respondent's proposal to include, in its valuation of the adverse effects, a probabilistic assessment to the expected value of each sales campaign to account for the alleged uncertainty of Airbus winning that sales campaign in the counterfactual. The Arbitrator reiterated that doing so would be inconsistent with the degree and nature of the adverse effects determined to exist, in contravention of its mandate.<sup>133</sup>

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<sup>132</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.164.

<sup>133</sup> Decision by the Arbitrator, *US – Large Civil Aircraft (2<sup>nd</sup> complaint)* (Article 22.6 – US), para. 6.165.