



WORLD TRADE
ORGANIZATION

WT/DS487/R

28 November 2016

(16-6452)

Page: 1/107

Original: English

UNITED STATES – CONDITIONAL TAX INCENTIVES FOR LARGE CIVIL AIRCRAFT

REPORT OF THE PANEL

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<i>Australia – Automotive Leather II</i>	Panel Report, <i>Australia – Subsidies Provided to Producers and Exporters of Automotive Leather</i> , WT/DS126/R, adopted 16 June 1999, DSR 1999:III, p. 951
<i>Brazil – Aircraft</i>	Appellate Body Report, <i>Brazil – Export Financing Programme for Aircraft</i> , WT/DS46/AB/R, adopted 20 August 1999, DSR 1999:III, p. 1161
<i>Brazil – Aircraft</i>	Panel Report, <i>Brazil – Export Financing Programme for Aircraft</i> , WT/DS46/R, adopted 20 August 1999, as modified by Appellate Body Report WT/DS46/AB/R, DSR 1999:III, p. 1221
<i>Canada – Aircraft</i>	Appellate Body Report, <i>Canada – Measures Affecting the Export of Civilian Aircraft</i> , WT/DS70/AB/R, adopted 20 August 1999, DSR 1999:III, p. 1377
<i>Canada – Aircraft</i>	Panel Report, <i>Canada – Measures Affecting the Export of Civilian Aircraft</i> , WT/DS70/R, adopted 20 August 1999, upheld by Appellate Body Report WT/DS70/AB/R, DSR 1999:IV, p. 1443
<i>Canada – Aircraft (Article 21.5 – Brazil)</i>	Appellate Body Report, <i>Canada – Measures Affecting the Export of Civilian Aircraft – Recourse by Brazil to Article 21.5 of the DSU</i> , WT/DS70/AB/RW, adopted 4 August 2000, DSR 2000:IX, p. 4299
<i>Canada – Aircraft Credits and Guarantees</i>	Panel Report, <i>Canada – Export Credits and Loan Guarantees for Regional Aircraft</i> , WT/DS222/R and Corr.1, adopted 19 February 2002, DSR 2002:III, p. 849
<i>Canada – Autos</i>	Appellate Body Report, <i>Canada – Certain Measures Affecting the Automotive Industry</i> , WT/DS139/AB/R, WT/DS142/AB/R, adopted 19 June 2000, DSR 2000:VI, p. 2985
<i>Canada – Periodicals</i>	Appellate Body Report, <i>Canada – Certain Measures Concerning Periodicals</i> , WT/DS31/AB/R, adopted 30 July 1997, DSR 1997:I, p. 449
<i>Canada – Renewable Energy / Canada – Feed-in Tariff Program</i>	Appellate Body Reports, <i>Canada – Certain Measures Affecting the Renewable Energy Generation Sector / Canada – Measures Relating to the Feed-in Tariff Program</i> , WT/DS412/AB/R / WT/DS426/AB/R, adopted 24 May 2013, DSR 2013:I, p. 7
<i>China – Auto Parts</i>	Appellate Body Reports, <i>China – Measures Affecting Imports of Automobile Parts</i> , WT/DS339/AB/R / WT/DS340/AB/R / WT/DS342/AB/R, adopted 12 January 2009, DSR 2009:I, p. 3
<i>Colombia – Ports of Entry</i>	Panel Report, <i>Colombia – Indicative Prices and Restrictions on Ports of Entry</i> , WT/DS366/R and Corr.1, adopted 20 May 2009, DSR 2009:VI, p. 2535
<i>EC – Hormones</i>	Appellate Body Report, <i>EC Measures Concerning Meat and Meat Products (Hormones)</i> , WT/DS26/AB/R, WT/DS48/AB/R, adopted 13 February 1998, DSR 1998:I, p. 135
<i>EC and certain member States – Large Civil Aircraft</i>	Appellate Body Report, <i>European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft</i> , WT/DS316/AB/R, adopted 1 June 2011, DSR 2011:I, p. 7
<i>EC and certain member States – Large Civil Aircraft</i>	Panel Report, <i>European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft</i> , WT/DS316/R, adopted 1 June 2011, as modified by Appellate Body Report, WT/DS316/AB/R, DSR 2011:II, p. 685
<i>India – Patents (US)</i>	Appellate Body Report, <i>India – Patent Protection for Pharmaceutical and Agricultural Chemical Products</i> , WT/DS50/AB/R, adopted 16 January 1998, DSR 1998:I, p. 9
<i>Indonesia – Autos</i>	Panel Report, <i>Indonesia – Certain Measures Affecting the Automobile Industry</i> , WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R, Corr.1 and Corr.2, adopted 23 July 1998, and Corr.3 and Corr.4, DSR 1998:VI, p. 2201
<i>Japan – Alcoholic Beverages II</i>	Appellate Body Report, <i>Japan – Taxes on Alcoholic Beverages</i> , WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, DSR 1996:I, p. 97
<i>Japan – DRAMs (Korea)</i>	Panel Report, <i>Japan – Countervailing Duties on Dynamic Random Access Memories from Korea</i> , WT/DS336/R, adopted 17 December 2007, as modified by Appellate Body Report WT/DS336/AB/R, DSR 2007:VII, p. 2805

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<i>Korea – Alcoholic Beverages</i>	Appellate Body Report, <i>Korea – Taxes on Alcoholic Beverages</i> , WT/DS75/AB/R, WT/DS84/AB/R, adopted 17 February 1999, DSR 1999:I, p. 3
<i>Korea – Alcoholic Beverages</i>	Panel Report, <i>Korea – Taxes on Alcoholic Beverages</i> , WT/DS75/R, WT/DS84/R, adopted 17 February 1999, as modified by Appellate Body Report WT/DS75/AB/R, WT/DS84/AB/R, DSR 1999:I, p. 44
<i>US – Anti-Dumping Measures on Oil Country Tubular Goods</i>	Appellate Body Report, <i>United States – Anti-Dumping Measures on Oil Country Tubular Goods (OCTG) from Mexico</i> , WT/DS282/AB/R, adopted 28 November 2005, DSR 2005:XX, p. 10127
<i>US – Carbon Steel</i>	Appellate Body Report, <i>United States – Countervailing Duties on Certain Corrosion-Resistant Carbon Steel Flat Products from Germany</i> , WT/DS213/AB/R and Corr.1, adopted 19 December 2002, DSR 2002:IX, p. 3779
<i>US – Carbon Steel (India)</i>	Appellate Body Report, <i>United States – Countervailing Measures on Certain Hot-Rolled Carbon Steel Flat Products from India</i> , WT/DS436/AB/R, adopted 19 December 2014, DSR 2014:V, p. 1727
<i>US – Corrosion-Resistant Steel Sunset Review</i>	Appellate Body Report, <i>United States – Sunset Review of Anti-Dumping Duties on Corrosion-Resistant Carbon Steel Flat Products from Japan</i> , WT/DS244/AB/R, adopted 9 January 2004, DSR 2004:I, p. 3
<i>US – Countervailing and Anti-Dumping Measures (China)</i>	Appellate Body Report, <i>United States – Countervailing and Anti-Dumping Measures on Certain Products from China</i> , WT/DS449/AB/R and Corr.1, adopted 22 July 2014, DSR 2014:VIII, p. 3027
<i>US – FSC</i>	Appellate Body Report, <i>United States – Tax Treatment for "Foreign Sales Corporations"</i> , WT/DS108/AB/R, adopted 20 March 2000, DSR 2000:III, p. 1619
<i>US – FSC</i>	Panel Report, <i>United States – Tax Treatment for "Foreign Sales Corporations"</i> , WT/DS108/R, adopted 20 March 2000, as modified by Appellate Body Report WT/DS108/AB/R, DSR 2000:IV, p. 1675
<i>US – FSC (Article 21.5 – EC)</i>	Appellate Body Report, <i>United States – Tax Treatment for "Foreign Sales Corporations" – Recourse to Article 21.5 of the DSU by the European Communities</i> , WT/DS108/AB/RW, adopted 29 January 2002, DSR 2002:I, p. 55
<i>US – FSC (Article 21.5 – EC)</i>	Panel Report, <i>United States – Tax Treatment for "Foreign Sales Corporations" – Recourse to Article 21.5 of the DSU by the European Communities</i> , WT/DS108/RW, adopted 29 January 2002, as modified by Appellate Body Report WT/DS108/AB/RW, DSR 2002:I, p. 119
<i>US – Gambling</i>	Appellate Body Report, <i>United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services</i> , WT/DS285/AB/R, adopted 20 April 2005, DSR 2005:XII, p. 5663 (and Corr.1, DSR 2006:XII, p. 5475)
<i>US – Hot-Rolled Steel</i>	Appellate Body Report, <i>United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan</i> , WT/DS184/AB/R, adopted 23 August 2001, DSR 2001:X, p. 4697
<i>US – Hot-Rolled Steel</i>	Panel Report, <i>United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan</i> , WT/DS184/R, adopted 23 August 2001 modified by Appellate Body Report WT/DS184/AB/R, DSR 2001:X, p. 4769
<i>US – Large Civil Aircraft (2nd complaint)</i>	Appellate Body Report, <i>United States – Measures Affecting Trade in Large Civil Aircraft (Second Complaint)</i> , WT/DS353/AB/R, adopted 23 March 2012, DSR 2012:I, p. 7
<i>US – Large Civil Aircraft (2nd complaint)</i>	Panel Report, <i>United States – Measures Affecting Trade in Large Civil Aircraft (Second Complaint)</i> , WT/DS353/R, adopted 23 March 2012, as modified by Appellate Body Report WT/DS353/AB/R, DSR 2012:II, p. 649
<i>US – Offset Act (Byrd Amendment)</i>	Appellate Body Report, <i>United States – Continued Dumping and Subsidy Offset Act of 2000</i> , WT/DS217/AB/R, WT/DS234/AB/R, adopted 27 January 2003, DSR 2003:I, p. 375
<i>US – Poultry (China)</i>	Panel Report, <i>United States – Certain Measures Affecting Imports of Poultry from China</i> , WT/DS392/R, adopted 25 October 2010, DSR 2010:V, p. 1909
<i>US – Shrimp</i>	Appellate Body Report, <i>United States – Import Prohibition of Certain Shrimp and Shrimp Products</i> , WT/DS58/AB/R, adopted 6 November 1998, DSR 1998:VII, p. 2755

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<i>US – Softwood Lumber IV</i>	Appellate Body Report, <i>United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada</i> , WT/DS257/AB/R, adopted 17 February 2004, DSR 2004:II, p. 571
<i>US – Upland Cotton</i>	Panel Report, <i>United States – Subsidies on Upland Cotton</i> , WT/DS267/R, Add.1 to Add.3 and Corr.1, adopted 21 March 2005, as modified by Appellate Body Report WT/DS267/AB/R, DSR 2005:II, p. 299
<i>US – Wool Shirts and Blouses</i>	Appellate Body Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/AB/R, adopted 23 May 1997, and Corr.1, DSR 1997:I, p. 323

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<i>Japan – Alcoholic Beverages I</i>	GATT Panel Report, <i>Japan – Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages</i> , L/6216, adopted 10 November 1987, BISD 34S/83
<i>US – Section 337 Tariff Act</i>	GATT Panel Report, <i>United States Section 337 of the Tariff Act of 1930</i> , L/6439, adopted 7 November 1989, BISD 36S/345
<i>US – Superfund</i>	GATT Panel Report, <i>United States – Taxes on Petroleum and Certain Imported Substances</i> , L/6175, adopted 17 June 1987, BISD 34S/136

EXHIBITS REFERRED TO IN THIS REPORT

Panel Exhibit	Title	Short Title
EU-3	Engrossed Substitute Senate Bill 5952, Chapter 2, Laws of 2013 3rd Special Session, 2014 Wash. Sess. Laws 2	ESSB 5952
EU-4	Final Bill Report ESSB 5952	ESSB 5952 Final Bill Report
EU-5	Department of Revenue Fiscal Note (5952 SB)	ESSB 5952 Fiscal Note
EU-21	House Bill 2294, 2003 Wash. Sess. Laws 2767	HB 2294
EU-22	RCW 82.04.260: Tax on manufacturers and processors of various foods and by-products - Research and development organizations - Travel agents - Certain international activities - Stevedoring and associated activities - Low-level waste disposers - Insurance producers, surplus line brokers, and title insurance agents - Hospitals - Commercial airplane activities - Timber product activities - Canned salmon processors. (Effective until July 1, 2015.)	RCW Section 82.04.260
EU-23	RCW 82.04.4461: Credit - Preproduction development expenditures. (Expires July 1, 2040.)	RCW Section 82.04.4461
EU-24	RCW 82.04.4463: Credit - Property and leasehold taxes paid on property used for manufacture of commercial airplanes. (Expires July 1, 2040.)	RCW Section 82.04.4463
EU-25	RCW 82.08.975: Exemptions - Computer parts and software related to the manufacture of commercial airplanes. (Expires July 1, 2040.)	RCW Section 82.08.975
EU-26	RCW 82.12.975: Computer parts and software related to the manufacture of commercial airplanes. (Expires July 1, 2040.)	RCW Section 82.12.975
EU-27	RCW 82.08.980: Exemptions - Labor, services, and personal property related to the manufacture of commercial airplanes. (Expires July 1, 2040.)	RCW Section 82.08.980
EU-28	RCW 82.12.980: Exemptions - Labor, services, and personal property related to the manufacture of commercial airplanes. (Expires July 1, 2040.)	RCW Section 82.12.980
EU-29	RCW 82.29A.137: Exemptions - Certain leasehold interests related to the manufacture of superefficient airplanes. (Expires July 1, 2040.)	RCW Section 82.29A.137
EU-30	RCW 84.36.655: Property related to the manufacture of superefficient airplanes. (Expires July 1, 2040.)	RCW Section 84.36.655
EU-32	RCW 82.04.220: Business and occupation tax imposed.	RCW Section 82.04.220
EU-33	Department of Revenue, Washington State, Business & occupation tax	B&O Tax Explanation, Washington State Department of Revenue
EU-35	House Bill 2466, 2006 Wash. Sess. Laws 787	HB 2466
EU-36	RCW 82.04.240: Tax on manufacturers. (Contingent expiration date.)	RCW Section 82.04.240
EU-37	RCW 82.04.450: Value of products, how determined.	RCW Section 82.04.450
EU-38	RCW 82.04.250: Tax on retailers.	RCW Section 82.04.250
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EU-40	RCW 82.04.070: "Gross proceeds of sales".	RCW Section 82.04.070
EU-41	WAC 458-20-19301: Multiple activities tax credits.	WAC Section 458-20-19301
EU-42	Substitute Senate Bill 6828, 2008 Wash. Sess. Laws 365	SSB 6828
EU-44	Snohomish County Council, Executive/Council Approval Form, 25 July 2012	Snohomish County Council, Lease Approval
EU-45	Paine Field Community Council, Meeting Minutes, November 12, 2013	Paine Field Community Council, Minutes of Meeting of 12 November 2013
EU-48	The Seattle Times, "State gave Boeing a free pass on \$19.5M in sales tax", by Jim Brunner, originally published November 29, 2015 / Updated November 30, 2015	The Seattle Times, "State gave Boeing a free pass on \$19.5M in sales tax", 30 November 2015
EU-49	Department of Revenue, Washington State, Leasehold excise tax	Leasehold Excise Tax, Washington State Department of Revenue
EU-50	WAC 458-29A-100: Leasehold excise tax - Overview and definitions.	WAC Section 458-29A-100

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EU-51	Washington State Department of Revenue, Personal Property Tax, December 2012	Personal Property Tax, Washington State Department of Revenue
EU-58	RCW 82.32.850: Significant commercial airplane manufacturing – Tax preference – Contingent effective date.	RCW Section 82.32.850
EU-59	Office of Washington Governor – Jay Inslee, "Legislature approves key elements of 777X incentive package", 10 November 2013	Office of Washington Governor, "Legislature approves key elements of 777X incentive package", 10 November 2013
EU-61	Notification Letter from Carol K. Nelson, Director, Washington State Department of Revenue, to Kyle Thiessen, Washington State Code Reviser, 10 July 2014	Letter from the Director of the Washington State Department of Revenue to the Code Reviser, 10 July 2014
EU-62	Department of Revenue, Washington State, Tax Classifications for Common Business Activities	Tax Classifications for Common Business Activities, Washington State Department of Revenue
EU-65	Reuters, "Boeing seen in advanced talks to make 777X near Seattle", by Tim Hephher and Alwyn Scott, 4 November 2013	Reuters, "Boeing seen in advanced talks to make 777X near Seattle", 4 November 2013
EU-78	Boeing Presentation, "Introducing the 787", by Tom Dodt, September 2011	Boeing Presentation, "Introducing the 787", September 2011
EU-79	Boeing, "Randy's Journal: Arrivals", posted on 22 May 2007	Boeingblogs, "Randy's Journal: Arrivals", 22 May 2007
EU-82	RCW 82.32.550: "Commercial airplane," "component," and "superefficient airplane" – Definitions.	RCW Section 82.32.550(3)
EU-83	Reuters, "Boeing hopeful of 777X deal, may build wings in Japan if rejected", 11 November 2013	Reuters, "Boeing hopeful of 777X deal, may build wings in Japan if rejected", 11 November 2013
EU-84	Airbus, "How is an aircraft built? Production"	Airbus, "How is an aircraft built? Production"
EU-86	Airbus, "How is an aircraft built? Final assembly and tests"	Airbus, "How is an aircraft built? Final assembly and tests"
EU-87	Airbus Video, "The A350 XWB Final Assembly Line: efficiency in motion", 23 October 2012	Airbus Video, "The A350 XWB Final Assembly Line: efficiency in motion", 23 October 2012
EU-88	Airbus Video, "A350 XWB final assembly: a step-by-step overview", 23 October 2012	Airbus Video, "A350 XWB final assembly: a step-by-step overview", 23 October 2012
EU-91	BBC Documentary, "How to Build A Super Jumbo Wing", 24 August 2013	BBC Documentary, "How to Build A Super Jumbo Wing", 24 August 2013
EU-92	RCW 82.08.020: Tax imposed – Retail sales – Retail car rental. (Contingent expiration date.)	RCW Section 82.08.020
EU-95	Department of Revenue, Washington State, 2016 Tax Exemption Study: A Study of Tax Exemptions, Exclusions or Deductions From the Base of a Tax; a Credit Against a Tax; a Deferral of a Tax; or a Preferential Tax Rate: As Authorized by RCW 43.06.400	2016 Tax Exemption Study, Washington State Department of Revenue
EU-97	Boeing Video, "Boeing 747 Dreamlifter", 17 January 2009	Boeing Video, "Boeing 747 Dreamlifter", 17 January 2009
EU-104	Airbus Video, "A380 from dream to reality: Final assembly", 18 October 2007	Airbus Video, "A380 from dream to reality: Final assembly", 18 October 2007
EU-110	Washington State House Finance Committee, Video, "Testimony of Governor Inslee before House Finance Committee", 7 November 2013	Washington State House Finance Committee, Video, "Testimony of Governor Inslee before House Finance Committee", 7 November 2013
EU-121	The Seattle Times, "Boeing must disclose tax-break savings, state Department of Revenue rules", by Jim Brunner, originally published January 7, 2016 / Updated January 8, 2016	The Seattle Times, "Boeing must disclose tax-break savings, state Department of Revenue rules", 8 January 2016
EU-122	Boeing Frontiers, "Supersize! The 747-700 will be transformed into an even larger freighter to save significant time and costs in transporting 787 assemblies", by Tom Koehler, June 2005	Boeing Frontiers, "The 747-700 will be transformed into an even larger freighter", June 2005

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USA-1	[[BCI]]	Boeing expert statement (BCI)
USA-2	[[BCI]]	Boeing, Make/Buy Model 777-300ER, July 2007 (BCI)
USA-6	Boeing Backgrounder, "The Boeing 777 Family: Preferred by Passengers and Airlines around the World", April 2015	Boeing 777 Backgrounder
USA-8	[[BCI]]	Boeing, 777X Make/Buy, All Commodities, Status as of 17 December 2014 (BCI)
USA-11	Department of Revenue, Washington State, Question: What are the major B&O tax classifications?	Question: What are the major B&O tax classifications?, Washington State Department of Revenue
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USA-14	Department of Revenue, Washington State, Digital Products including Digital Goods	Digital Products including Digital Goods, Washington State Department of Revenue
USA-15	<i>Shorter Oxford English Dictionary on Historical Principles</i> , 5 th edition, Volume 2, p. 2044	<i>Shorter Oxford English Dictionary</i> , 5 th edition, Volume 2, p. 2044
USA-16	Department of Revenue, Washington State, Local Sales, Use Tax Rates and Changes (Effective January 1 – March 31, 2016)	Local Sales, Use Tax Rates and Changes, Washington State Department of Revenue
USA-17	RCW 82.12.020: Use tax imposed. (<i>Effective until January 1, 2016.</i>)	RCW Section 82.12.020
USA-18	RCW 82.12.035: Credit for retail sales or use taxes paid to other jurisdictions with respect to property used. (<i>Effective until January 1, 2016.</i>)	RCW Section 82.12.035
USA-19	Department of Revenue, Washington State, Use Tax	Use Tax Explanation, Washington State Department of Revenue
USA-20	RCW 84.36.005: Property subject to taxation	RCW Section 84.36.005
USA-21	RCW 84.36.010: Public, certain public-private and tribal property exempt. (<i>Effective until January 1, 2022.</i>)	RCW Section 84.36.010
USA-22	RCW 84.36.020: Cemeteries, churches, parsonages, convents, and grounds. (<i>Effective until December 31, 2020.</i>)	RCW Section 84.36.020
USA-23	RCW 84.36.477: Business inventories.	RCW Section 84.36.477
USA-25	Department of Revenue, Washington State, Leasehold excise tax	Leasehold Excise Tax Explanation, Washington State Department of Revenue
USA-26	RCW 82.29A.030: Tax imposed—Credit—Additional tax imposed. (<i>Effective until January 1, 2019.</i>)	RCW Section 82.29A.030
USA-28	<i>Le Nouveau Petit Robert</i> , 2009, pp. 2034-2035	<i>Le Nouveau Petit Robert</i> , 2009, pp. 2034-2035
USA-29	<i>Diccionario de la Lengua Española</i> , 2001, pp. 1839-1840	<i>Diccionario de la Lengua Española</i> , 2001, pp. 1839-1840
USA-30	Boeing, 777X Content Sources, Major Structures & Propulsion, Status as of 27 October 2015	Boeing, 777X Content Sources, Major Structures & Propulsion, Status as of 27 October 2015 (BCI)
USA-31	RCW 82.04.440: Credit – Persons taxable on multiple activities.	RCW Section 82.04.440
USA-32	[[BCI]]	Boeing letter to the Director of the Washington State Department of Revenue (BCI), 9 July 2014

Panel Exhibit	Title	Short Title
USA-33	Collective Bargaining Agreement between Boeing and the International Association of Machinists and Aerospace Workers, AFL-CIO, of 2 November 2008, including Contract Extension and Modification Agreements of 7 December 2011 and 3 January 2014	Collective Bargaining Agreement between Boeing and the International Association of Machinists and Aerospace Workers, 2 November 2008, including Contract Extension and Modification Agreements, 7 December 2011 and 3 January 2014
USA-34	[[BCI]]	Addendum No. 14 to the 1991 Boeing Everett Mitigation Decision Document SEPA #14-009, 27 March 2014 (BCI)
USA-35	[[BCI]]	Addendum No. 15 to the 1991 Boeing Everett Mitigation Decision Document SEPA #14-011 – Composite Wing Manufacturing Facility, 30 May 2014 (BCI)
USA-37	RCW 82.04.120: "To manufacture".	RCW Section 82.04.120
USA-38	Supreme Court of Washington, Citizens Alliance for Property Rights Legal Fund v. San Juan County et al. (2015)	Supreme Court of Washington, Citizens Alliance for Property Rights Legal Fund v. San Juan County et al. (2015)
USA-42	Mitsubishi Heavy Industries, Boeing 787	Mitsubishi Heavy Industries, Boeing 787
USA-51	<i>Shorter Oxford English Dictionary</i> , 6 th edition, pp. 2044-2045	<i>Shorter Oxford English Dictionary</i> , 6 th edition, pp. 2044-2045
USA-52	Spirit AeroSystems, "Spirit celebrates completion of first Boeing 737 MAX fuselage	Spirit AeroSystems, "Spirit celebrates completion of first Boeing 737 MAX fuselage
USA-63	Chapter 1.04 RCW	Chapter 1.04 RCW
USA-64	Chapter 82.08 RCW: Retail Sales Tax	RCW Chapter 82.08
USA-65	Department of Revenue, Washington State, 2016 Tax Exemption Study, Introduction and Summary of Findings	2016 Tax Exemption Study, Introduction and Summary of Findings, Washington State Department of Revenue
USA-67	[[BCI]]	Boeing 787 customs invoice and related shipment documentation (BCI)
USA-68	Boeing Frontiers, "Wings around the world", by Adam Morgan, March 2006	Boeing Frontiers, "Wings around the world", March 2006
USA-73	[[BCI]]	Email from Erik Zahn, Boeing Commercial Airplanes, 15 April 2016 (BCI)
USA-84	Washington Court of Appeals, Nationscapital Mortgage Corporation et al. v. Department of Financial Institutions, 133 Wn. App. 723, 737-738 (Wash. Ct. App. 2006), June 2006	Washington Court of Appeals, Nationscapital Mortgage Corporation et al. v. Department of Financial Institutions, June 2006

ABBREVIATIONS USED IN THIS REPORT

Abbreviation	Description
B&O tax	Business and occupation tax
BCI	Business Confidential Information
DSB	Dispute Settlement Body
DSU	Understanding on Rules and Procedures Governing the Settlement of Disputes
ESSB 5952	Washington State Legislature Engrossed Substitute Senate Bill 5952
GATT 1994	General Agreement on Tariffs and Trade 1994
HB 2294	Washington State Legislature House Bill 2294
HB 2466	Washington State Legislature House Bill 2466
HSBI	Highly Sensitive Business Information
RCW	Revised Code of Washington (Washington State)
SCM Agreement	Agreement on Subsidies and Countervailing Measures
SSB 6828	Washington State Substitute Senate Bill 6828
Vienna Convention	Vienna Convention on the Law of Treaties, Done at Vienna, 23 May 1969, 1155 UNTS 331; 8 International Legal Materials 679
WAC	Washington Administrative Code (Washington State)
WTO	World Trade Organization

1 INTRODUCTION

1.1 Complaint by the European Union

1.1. On 19 December 2014, the European Union requested consultations with the United States pursuant to Articles 4.1 and 30 of the Agreement on Subsidies and Countervailing Measures (SCM Agreement); Article XXIII:1 of the General Agreement on Tariffs and Trade 1994 (GATT 1994), to the extent incorporated by Article 30 of the SCM Agreement; and Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), with respect to the measures and claims set out below.¹

1.2. Consultations were held on 2 February 2015. These consultations did not lead to a mutually satisfactory solution.²

1.2 Panel establishment and composition

1.3. On 12 February 2015, the European Union requested the establishment of a panel pursuant to Articles 4.4 and 30 of the SCM Agreement, Article XXIII:2 of the GATT 1994 (to the extent incorporated by Article 30 of the SCM Agreement), and Article 6 of the DSU (as modified by Article 4.4 of the SCM Agreement, and in light of Article 1.2 and Appendix 2 to the DSU), with standard terms of reference.³ At its meeting on 23 February 2015, the Dispute Settlement Body (DSB) established a panel pursuant to the request of the European Union, in accordance with the provisions of Article 4.4 of the SCM Agreement and Article 6 of the DSU, with standard terms of reference.⁴

1.4. The Panel's terms of reference are the following:

To examine, in the light of the relevant provisions of the covered agreements cited by the parties to the dispute, the matter referred to the DSB by the European Union in document WT/DS487/2 and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements.⁵

1.5. On 13 April 2015, the European Union requested the Director-General to determine the composition of the panel, pursuant to Article 8.7 of the DSU. On 22 April 2015, the Director-General accordingly composed the Panel as follows:

Chairperson: Mr Daniel Moulis
Members: Mr Terry Collins-Williams
Mr Wilhelm Meier

1.6. Australia; Brazil; Canada; China; India; Japan; the Republic of Korea (Korea); and the Russian Federation (Russia) notified their interest in participating in the Panel proceedings as third parties.

1.3 Panel proceedings

1.3.1 General

1.7. The commencement of the Panel's work was delayed as a result of a lack of available resources in the World Trade Organization (WTO) Secretariat.⁶ The parties were notified of this circumstance. The Panel held its organizational meeting with the parties on 4 December 2015.

¹ See Request for Consultations by the European Union, WT/DS487/1, 23 December 2014.

² See Request for the Establishment of a Panel by the European Union, WT/DS487/2, 13 February 2015.

³ Ibid.

⁴ See Dispute Settlement Body, Minutes of Meeting held in the Centre William Rappard on 23 February 2015, WT/DSB/M/357, 17 April 2015, pp. 14-15.

⁵ Constitution of the Panel Established at the Request of the European Union – Note by the Secretariat, WT/DS487/3, 23 April 2015.

⁶ Communication from the Panel to the DSB, WT/DS487/4, 30 September 2015.

After consultation with the parties, the Panel adopted its Working Procedures on 7 December 2015⁷, its timetable on 16 December 2015, and a revised timetable on 19 April 2016.

1.8. The European Union filed its first written submission on 9 December 2015. The United States filed its first written submission on 19 January 2016. Third-party submissions were received on 26 January 2016 from Australia, Brazil, Canada, China, and Japan.

1.9. The Panel held a first substantive meeting with the parties on 24 and 25 February 2016. A session with the third parties took place on 25 February 2016, in which oral statements were made by Australia, Brazil, China, and Japan. Written responses to questions posed by the Panel were received on 9 March 2016 from the European Union, the United States, Australia, Brazil, Canada, China, and Japan.

1.10. The parties filed their second written submissions on 18 March 2016.

1.11. The Panel held a second substantive meeting with the parties on 5 April 2016. Written responses to questions posed by the Panel were received on 18 April 2016. Comments by the parties on each other's responses to questions were received on 25 April 2016.

1.12. On 9 May 2016, the Panel issued the descriptive sections of its draft report to the parties. Parties provided comments to the descriptive sections of the Panel report on 17 May 2016.

1.13. The Panel issued its Interim Report to the parties on 6 July 2016. On 15 July 2016, the European Union and the United States each submitted written requests for review of precise aspects of the interim report. Neither party requested an interim review meeting. On 20 July 2016, each of the parties submitted comments on the other's requests for review. The Panel issued its Final Report to the parties on 29 July 2016.

1.3.2 Changes to the timetable

1.14. On 5 January 2016, the United States requested an adjustment to the timetable so that the deadline for the second written submission was set no earlier than 25 March 2016 (one week later than originally scheduled). The European Union commented on the United States' request on 7 January 2016. On 15 January 2016, the Panel informed the parties that it had declined the United States' request for an extension of the deadline for the second written submissions.⁸

1.15. In the course of the second meeting with the parties on 5 April 2016, the Panel informed the parties that in order to have sufficient time to assess the legal and factual issues in the dispute, the timetable would have to be adjusted so that the interim report was issued to parties on 15 June 2016 and all subsequent dates were similarly adjusted. The parties had no comments to this proposal. On 19 April 2016, the Panel issued the revised timetable.

1.16. On 28 April 2016, the United States requested an opportunity to comment on certain factual evidence and arguments that were submitted by the European Union with its comments on the United States' responses to Panel questions. The European Union commented on the United States' request on 2 May 2016. On 4 May 2016, the Panel informed the parties that it had declined the United States' request.⁹

1.17. On 13 June 2016, the Panel informed the parties that it intended to issue the interim report to parties on 6 July 2016 and to adjust all subsequent dates similarly. The European Union submitted comments to this notice on 14 June. On 15 June 2016, the Panel issued a revised timetable.

1.18. On 12 July 2016, the United States requested a two-day extension for parties to request the review of precise aspects of the interim report. On the same date, the European Union communicated its agreement to the United States' request, under the understanding that subsequent dates on the schedule would not change. On 13 July 2016, the Panel informed the

⁷ See the Panel's Working Procedures in Annex A-1.

⁸ See letter from the Panel in Annex D-1.

⁹ Ibid.

parties that it had extended by two days the deadline for parties to request the review of precise aspects of the interim report, and that subsequent deadlines had not been revised. The Panel issued a revised timetable to the parties.

1.3.3 Additional Working Procedures for the Protection of Business Confidential Information (BCI) and Highly Sensitive Business Information (HSBI)

1.19. At the request of the United States, and having considered comments from the European Union, the Panel adopted Additional Working Procedures for the Protection of Business Confidential Information and Highly Sensitive Business Information (BCI/HSBI Procedures) on 13 January 2016.¹⁰

1.3.4 Additional Working Procedures for the Partial Opening to the Public of the Meetings of the Panel

1.20. On 22 February 2016 and 23 March 2016, at the request of the United States, and noting the European Union's agreement, the Panel adopted additional working procedures for the partial opening to the public of the meetings of the Panel. These procedures provided for public viewing of a video-recording of non-confidential portions of each meeting by means of delayed broadcast. Closed sessions were foreseen for the parties to address BCI or HSBI and for those third parties that had requested not to make their statements in the video-recorded session for public viewing.¹¹ The public screening of the video-recording of the non-confidential portions of the Panel meetings took place on 17 and 18 May 2016.

2 FACTUAL ASPECTS

2.1. The claims brought by the European Union concern tax-related provisions for civil aircraft provided by the state of Washington in the United States, as amended by Engrossed Substitute Senate Bill 5952 (ESSB 5952), Chapter 2, Laws of 2013 3rd Special Session, 2014 Wash. Sess. Laws 2. Specifically, this dispute concerns the following tax-related provisions contained in the Revised Code of Washington (RCW):

- a. a 0.2904% business and occupation tax rate with respect to the manufacture or sale of commercial airplanes, contained in RCW Section 82.04.260(11);
- b. tax credits for property taxes and leasehold excise taxes on commercial airplane manufacturing facilities, contained in RCW Section 82.04.4463;
- c. tax credits for aerospace product development, contained in RCW Section 82.04.4461;
- d. sales tax exemption for computer hardware, software, and peripherals, contained in RCW Section 82.08.975;
- e. sales tax exemption for construction services and materials, contained in RCW Section 82.08.980;
- f. use tax exemption for computer hardware, software, and peripherals, contained in RCW Section 82.12.975;
- g. use tax exemption for construction services and materials, contained in RCW Section 82.12.980;
- h. leasehold excise tax exemption, contained in RCW Section 82.29A.137; and
- i. leaseholder property tax exemption, contained in RCW Section 84.36.655.

¹⁰ See the Additional Working Procedures for the Protection of BCI/HSBI in Annex A-2.

¹¹ See the Additional Working Procedures for the partial opening to the public of the meetings of the Panel in Annexes A-3 and A-4.

2.2. The European Union claims that the availability of the above tax incentives is subject to the conditions in Sections 2, 5, and 6 of ESSB 5952 (as codified at RCW Sections 82.32.850 and 82.04.260(11)(e)(ii)). These conditions relate to a decision on the initial siting of a "significant commercial airplane manufacturing program" (as defined in the relevant legislation¹²) in the state of Washington, as well as to the future siting outside the state of Washington of "any final assembly or wing assembly of any version or variant of a commercial airplane that is the basis of a siting of a significant commercial airplane manufacturing program".¹³

3 PARTIES' REQUESTS FOR FINDINGS AND RECOMMENDATIONS

3.1. The European Union requests that the Panel find that each of the challenged Washington State tax incentives, as amended and extended by ESSB 5952, constitutes a subsidy that is prohibited pursuant to Articles 3.1(b) and 3.2 of the SCM Agreement due to being contingent on the use of domestic over imported goods. The European Union further requests, pursuant to Article 4.7 of the SCM Agreement, that the Panel recommend that the United States withdraw the subsidies without delay.

3.2. The United States requests that the Panel reject the European Union's claims in this dispute and find that the challenged measures are not inconsistent with the United States' obligations under Articles 3.1(b) and 3.2 of the SCM Agreement.

4 ARGUMENTS OF THE PARTIES

4.1. The arguments of the parties are reflected in their executive summaries, provided to the Panel in accordance with paragraph 20 of the Working Procedures adopted by the Panel (see Annexes B-1, B-2, B-3, and B-4).

5 ARGUMENTS OF THE THIRD PARTIES

5.1. The arguments of Australia, Brazil, Canada, China, and Japan are reflected in their executive summaries, provided in accordance with paragraph 21 of the Working Procedures adopted by the Panel (see Annexes C-1, C-2, C-3, C-4, and C-5). India, Korea, and Russia did not submit written or oral arguments to the Panel.

6 INTERIM REVIEW

6.1. On 6 July 2016, the Panel issued its Interim Report to the parties. On 15 July 2016, the European Union and the United States each submitted written requests for review of precise aspects of the Interim Report. Neither party requested an interim review meeting. On 20 July 2016, each of the parties submitted comments on the other's requests for review.

6.2. In accordance with Article 15.3 of the DSU, this section sets out the Panel's response to the parties' requests for review of precise aspects of the Report made at the interim review stage. The parties' requests for substantive modifications are discussed below, generally in sequence according to the paragraphs to which the requests pertain.

6.3. The numbering of some of the paragraphs and footnotes in the Final Report has changed from the numbering in the Interim Report. The discussion below refers to the numbering in the Interim Report and, where it differs, includes the corresponding numbering in the Final Report.

6.4. The United States notes that **paragraph 7.4** summarizes the requests of the United States "but omits an issue raised by the United States for the Panel's consideration regarding the Panel's terms of reference". In particular, the United States requests inclusion of a reference to its opening

¹² In turn, "significant commercial airplane manufacturing program" is defined as: "[A]n airplane program in which the following products, including final assembly, will commence manufacture at a new or existing location within Washington state on or after the effective date of this section: (i) The new model, or any version or variant of an existing model, of a commercial airplane; and (ii) Fuselages and wings of a new model, or any version or variant of an existing model, of a commercial airplane." ESSB 5952 Sections 2(2)(c) and (d), codified at RCW Sections 82.32.850(2)(c) and (d) (Exhibits EU-3 and EU-58).

¹³ ESSB 5952 Sections 5(11)(e)(ii) and 6(11)(e)(ii), codified at RCW Section 82.04.260(11)(e)(ii) (Exhibits EU-3 and EU-22).

statement at the first meeting of the Panel, in which the United States noted that, prior to the establishment of this Panel, the European Union had maintained that the measures at issue in this dispute were properly within the terms of reference of the compliance panel in the proceeding under Article 21.5 of the DSU in *US – Large Civil Aircraft (2nd complaint)*.¹⁴ The United States identifies **paragraph 7.41** of the Interim Report (paragraph 7.39 of this Report) as "a logical place for the Panel to address the terms of reference issue identified by the United States".¹⁵ The European Union considers that this is an inappropriate request for review of an interim report and that it should be rejected by the Panel. The European Union requests that, to the extent that the Panel elects to include a discussion on the United States' statements related to terms of reference, the Panel reflect "the United States' repeated statements that it did not consider any of the measures to be outside the [Panel's] terms of reference".¹⁶ The Panel declines the United States' request for inclusion of a reference to this issue in the Panel's findings. In its statement to the Panel, the United States explicitly clarified that "the United States does not itself consider that any of the measures at issue are outside the Panel's terms of reference".¹⁷ Although the Panel recognizes that the vesting of jurisdiction is a fundamental issue that may need to be considered even in the absence of any objection by a party, the Panel does not find any reason to question the vesting of its jurisdiction in the present case. Moreover, apart from any potential relevance of statements by a party made in another dispute, it is an uncontested fact that the measures at issue in this dispute are not presently being considered in any other dispute. The Panel addresses the legislative background and scope of the measures within its terms of reference in Section 7.3.3, and does not consider any additional discussion of the issue raised by the United States to be necessary.

6.5. The United States proposes an addition at the end of the second sentence of **paragraph 7.7** to "elaborate the function of the Panel" in examining municipal law, which according to the United States is "to determine the proper factual predicate against which WTO-consistency will be judged".¹⁸ The European Union considers that the addition proposed by the United States is not necessary, as the current formulation is an accurate description of the existing jurisprudence on the matter.¹⁹ The United States also requests a revision to **paragraph 7.8** to "avoid implying that an analysis of the meaning of a Member's municipal law could disregard the interpretive rules of a Member's domestic legal system".²⁰ The European Union considers that the modification proposed by the United States is not necessary, as the current formulation is an accurate and succinct description of the existing jurisprudence relating to the identification of the meaning and content of domestic law.²¹ The Panel considers that paragraphs 7.7 and 7.8 adequately refer to Appellate Body reports and consequently does not consider the elaboration of the issue requested by the United States to be necessary.

6.6. The European Union proposes to consolidate the discussions in **paragraphs 7.7-7.8 and 7.15-7.16** on a panel's role in examining the meaning of municipal law.²² The United States recalls its comments on paragraphs 7.7-7.8 and requests that the Panel take those comments into account in making any modifications in response to the European Union's request.²³ The Panel has consolidated this discussion to avoid duplication by deleting paragraphs 7.15 and 7.16 of the Interim Report.

6.7. The European Union requests changes to **paragraphs 7.17, 7.40, 7.81-7.84, and 7.245** of the Interim Report (paragraphs 7.15, 7.38, 7.79-7.82, and 7.243 of this Report), to "reflect the uncontested fact that the challenged aerospace tax incentives existed in Washington State prior to

¹⁴ United States' request for review of the Panel's Interim Report, paras. 2-3.

¹⁵ Ibid. para. 12.

¹⁶ European Union's comments on United States' request for review of the Panel's Interim Report, para. 1.

¹⁷ United States' opening statement at the first meeting of the Panel, para. 34.

¹⁸ United States' request for review of the Panel's Interim Report, paras. 4-5.

¹⁹ European Union's comments on United States' request for review of the Panel's Interim Report, para. 2.

²⁰ United States' request for review of the Panel's Interim Report, para. 6.

²¹ European Union's comments on United States' request for review of the Panel's Interim Report, para. 3.

²² European Union's request for review of the Panel's Interim Report, para. 5.

²³ United States' comments on European Union's request for review of the Panel's Interim Report, para. 6.

ESSB 5952, which amended the terms of those incentives".²⁴ The United States has no objection to the revisions requested by the European Union.²⁵ The Panel has revised the paragraphs identified by the European Union to refer to the measures "as amended and extended by" ESSB 5952.

6.8. The United States requests revisions to **paragraph 7.36** of the Interim Report (paragraph 7.34 of this Report) to reflect its view of the legislative history of the measures at issue in this dispute and the measures at issue in *US – Large Civil Aircraft (2nd complaint)*.²⁶ The European Union requests that the Panel reject the United States' request for modification, which in its view "is predicated on a series of erroneous factual premises".²⁷ In the light of the parties' comments, the Panel has made minor adjustments to the paragraph.

6.9. Both the European Union and the United States suggest changes to **paragraphs 7.39 and 7.42** of the Interim Report (paragraphs 7.37 and 7.40 of this Report) to provide a more accurate characterization of legislation in Washington State.²⁸ The Panel has made consequential revisions to paragraphs 7.39 and 7.42 of the Interim Report in the light of the parties' comments.

6.10. The United States requests the elimination of a sentence in **paragraph 7.55** of the Interim Report (paragraph 7.53 of this Report), which states that an entitlement granted by virtue of the relevant legislation "could only be re-established through further legislation revoking or amending the previous legislation". The United States notes that "revoking or amending the particular legislation at issue are not the only alternatives" and revenue may no longer be foregone, for example, if the measure providing for the benchmark tax were changed.²⁹ The European Union considers that the sentence, as currently worded, is correct.³⁰ In the light of the parties' comments, the Panel has removed the word "only" from the sentence identified by the United States.

6.11. The European Union requests in **paragraphs 7.89, 7.104, 7.117, 7.113, 7.139, and 7.148** of the Interim Report (paragraphs 7.87, 7.102, 7.115, 7.131, 7.137, and 7.146 of this Report) the addition of a reference to the objectives of HB 2294 (along with the existing reference to ESSB 5952) in discussing the "objective reasons" for the relevant tax treatment of each aerospace tax measure.³¹ The United States does not agree with the European Union's request, and considers that it is unclear what relevance the European Union ascribes to the objectives of HB 2294 in the context of the relevant paragraphs. As part of its comments on the European Union's request, the United States requests a modification of **paragraph 7.65** of the Interim Report (paragraph 7.63 of this Report), as legislation such as ESSB 5952 does not amend or extend previous legislation but rather amends or extends tax treatment provided for in the Revised Code of Washington, which itself reflects earlier legislation.³² The Panel does not consider the additional references requested by the European Union to be necessary. The paragraphs identified by the European Union clarify the "objective reasons" for each of the aerospace tax measures with supporting cross-references to the more extensive discussion in the context of the B&O aerospace tax rate, including reference to the objectives of prior legislation. The Panel has made the change requested by the United States in paragraph 7.63 of this Report.

6.12. The United States requests a revision of the first sentence of **paragraph 7.142** of the Interim Report (paragraph 7.140 of this Report) to reflect that, as noted in the remainder of the paragraph, the leasehold excise tax is an excise tax, and not a property tax.³³ The European Union

²⁴ European Union's request for review of the Panel's Interim Report, para. 6.

²⁵ United States' comments on European Union's request for review of the Panel's Interim Report, para. 7.

²⁶ United States' request for review of the Panel's Interim Report, para. 8.

²⁷ European Union's comments on United States' request for review of the Panel's Interim Report, para. 4.

²⁸ European Union's request for review of the Panel's Interim Report, paras. 8-10; United States' request for review of the Panel's Interim Report, paras. 10-11 and 13.

²⁹ United States' request for review of the Panel's Interim Report, para. 14.

³⁰ European Union's comments on United States' request for review of the Panel's Interim Report, para. 6.

³¹ European Union's request for review of the Panel's Interim Report, para. 11.

³² United States' comments on European Union's request for review of the Panel's Interim Report, paras. 11-12.

³³ United States' request for review of the Panel's Interim Report, para. 15.

requests that the Panel reject the United States' proposed modification and retain the current language. In the European Union's view, the leasehold excise tax is functionally a property tax. To the extent that the United States wishes to clarify that the leasehold excise tax is not formally a "property tax" within the specific meaning of the Revised Code of Washington, the European Union considers that the Panel could replace the phrase "property tax" in the sentence at issue with the phrase "tax on property", when referring to the leasehold excise tax.³⁴ The Panel has partially modified the first sentence of paragraph 7.142 of the Interim Report to accommodate the United States' request. However, the Panel has used the word "supplements" instead of "complements" (which was the word suggested by the United States) to describe the relationship of the "leasehold excise tax" to the "property taxes".

6.13. The European Union requests in **footnote 263 to paragraph 7.143** of the Interim Report (footnote 300 to paragraph 7.141 of this Report), in relation to the reference to the parties' arguments on the quantitative coverage of property tax exemptions, clarification of the cross-reference to the discussion of the parties' arguments concerning sales and use tax exemptions.³⁵ The United States has no comment on the European Union's request.³⁶ The Panel has made the requested clarification to footnote 263 of the Interim Report. The Panel has also provided a supplemental reference to the parties' arguments in a footnote to the last sentence of paragraph 7.121 of this Report.

6.14. The European Union requests a revision of **paragraph 7.176** of the Interim Report (paragraph 7.174 of this Report) to refer to "wing assembly", rather than "final assembly of a wing", in the description of its argument as to the potential triggering of the Second Siting Provision.³⁷ The United States has no objection to the European Union's request.³⁸ The Panel has made the requested correction to paragraph 7.176 of the Interim Report.

6.15. The United States requests a revision of **paragraph 7.187** of the Interim Report (paragraph 7.185 of this Report) to better capture the substance of the United States' argument in rejecting the European Union's interpretation of the word "use" in Article 3.1(b) of the SCM Agreement.³⁹ The European Union makes no comment on the United States' request. The Panel has made the requested change.

6.16. The European Union requests rephrasing **paragraph 7.231** of the Interim Report (paragraph 7.229 of this Report), specifically by removing the word "challenged" before "aerospace tax measures", so as not to inaccurately convey that the measures challenged by the European Union are the aerospace tax incentives as they stood before the amendments and extensions effected by ESSB 5952.⁴⁰ The United States agrees with the European Union's explanation and considers further that the first sentence in paragraph 7.231 of the Interim Report should be revised as explained in the United States' comments on paragraph 7.36 of the Interim Report discussed above.⁴¹ The Panel has made the modification requested by the European Union. The Panel has added a footnote to the first sentence of paragraph 7.229 of this Report referring to the earlier discussion of the legislative background of ESSB 5952, but declines to make the additional changes to the sentence requested by the United States.

6.17. The European Union requests a change in **paragraph 7.231** of the Interim Report of the phrase "the entry into force of the amended and extended aerospace tax measures was contingent" to instead state "the entry into force of the amendment and extension of the aerospace tax measures was contingent". According to the European Union, this change would clarify that it was only the amendment and extension of the tax measures that were conditional upon fulfilment of the First Siting Provision, rather than the entirety of the aerospace tax

³⁴ European Union's comments on United States' request for review of the Panel's Interim Report, para. 7.

³⁵ European Union's request for review of the Panel's Interim Report, para. 13.

³⁶ United States' comments on European Union's request for review of the Panel's Interim Report, para. 14.

³⁷ European Union's request for review of the Panel's Interim Report, para. 14.

³⁸ United States' comments on European Union's request for review of the Panel's Interim Report, para. 14.

³⁹ United States' request for review of the Panel's Interim Report, para. 16.

⁴⁰ European Union's request for review of the Panel's Interim Report, para. 16.

⁴¹ United States' comments on European Union's request for review of the Panel's Interim Report, para. 17.

measures. The European Union requests similar changes to **paragraphs 7.289 and 7.315(a)** of the Interim Report to refer to the entry into force of the amendment and extension by ESSB 5952 of the aerospace tax measures.⁴² The United States has no objection to the European Union's requests.⁴³ The Panel has made the requested modifications to paragraphs 7.231, 7.289, and 7.315(a) of the Interim Report (paragraphs 7.229, 7.287, and 7.313(a) of this Report).

6.18. The European Union requests an additional citation in **footnote 450 to paragraph 7.243** of the Interim Report (footnote 488 to paragraph 7.241 of this Report) to its submissions on the point that the measures at issue do not place any conditions on the use of elements or components of commercial airplanes, other than wings and fuselages.⁴⁴ The United States has no objection to the European Union's request.⁴⁵ The Panel has made the requested addition to the footnote.

6.19. The European Union requests a modification of **paragraph 7.289** of the Interim Report (paragraph 7.287 of this Report) to reflect that only wings *or* fuselages, not both, are required to be made of carbon fibre as noted elsewhere by the Panel.⁴⁶ The United States has no objection to the European Union's request.⁴⁷ The Panel has made the requested modification.

6.20. The European Union requests inclusion in **paragraph 7.352** of the Interim Report (paragraph 7.350 of this Report) of references to its submissions and exhibits that, in addition to evidence related to the 777X aircraft programme, "would support the more general proposition in relation to the aerospace industry" regarding the variety of aircraft manufacturing processes, as well as continuing innovation within the aerospace industry.⁴⁸ The United States does not consider that adding the requested citations would provide additional clarity to the report, as they are not "illustrative for the purposes of the Panel's sentence".⁴⁹ The Panel does consider them to be illustrative of the statements made in the paragraph and therefore has included the references identified by the European Union.

6.21. The United States requests a revision of **paragraph 7.358** of the Interim Report (paragraph 7.356 of this Report) as, in its view, the word "coincident" used in the paragraph "does not accurately capture the sequence of events" of Boeing's decision to site the 777X aircraft programme in Washington State. The United States also considers the same sentence "problematic in its reference to 'certain wing structures that the same manufacturer had previously imported for other commercial airplane manufacturing programmes'."⁵⁰ The European Union requests that the Panel reject the United States' request for modification. In the European Union's view, the statement at issue is a "factual finding ... based on an objective assessment of the evidence that the Parties placed before the Panel, and should not be rewritten based on the United States' own view of the evidence".⁵¹ In the light of the parties' comments, the Panel has made modifications and clarifications to the sentence in question.

6.22. The European Union requests in **paragraph 7.368** of the Interim Report (paragraph 7.366 of this Report) an adjustment of the left parenthesis in the phrase "(outside Washington State, including overseas)" as the current formulation "could potentially be misunderstood to indicate that the reference to Washington State is not an essential aspect of the explanation".⁵² The

⁴² European Union's request for review of the Panel's Interim Report, para. 17.

⁴³ United States' comments on European Union's request for review of the Panel's Interim Report, para. 18.

⁴⁴ European Union's request for review of the Panel's Interim Report, para. 19.

⁴⁵ United States' comments on European Union's request for review of the Panel's Interim Report, para. 20.

⁴⁶ European Union's request for review of the Panel's Interim Report, para. 21.

⁴⁷ United States' comments on European Union's request for review of the Panel's Interim Report, para. 22.

⁴⁸ European Union's request for review of the Panel's Interim Report, para. 22.

⁴⁹ United States' comments on European Union's request for review of the Panel's Interim Report, para. 23.

⁵⁰ United States' request for review of the Panel's Interim Report, paras. 18-20.

⁵¹ European Union's comments on United States' request for review of the Panel's Interim Report, para. 8.

⁵² European Union's request for review of the Panel's Interim Report, para. 23.

United States has no comment on the European Union's request.⁵³ The Panel has made the requested modification.

6.23. In addition to the requests discussed above, the Panel has made corrections for typographical and other non-substantive errors in the Interim Report, including those identified by the parties.

7 FINDINGS

7.1 Introduction

7.1. In this dispute, the European Union claims that the United States is acting inconsistently with the SCM Agreement by providing prohibited subsidies to the aerospace industry in the state of Washington. The European Union argues that these subsidies are provided by the state of Washington in the United States.

7.2. More specifically, the European Union challenges seven aerospace tax measures⁵⁴, namely: (i) a reduced business and occupation (B&O) tax rate for the manufacture and sale of commercial airplanes; (ii) a credit for the B&O tax for pre-production development of commercial airplanes and components; (iii) a credit for the B&O tax for property taxes on commercial airplane manufacturing facilities; (iv) an exemption from sales and use taxes for certain computer hardware, software, and peripherals; (v) an exemption from sales and use taxes for certain construction services and materials; (vi) an exemption from leasehold excise taxes on port district facilities used to manufacture superefficient airplanes; and (vii) an exemption from property taxes for the personal property of port district lessees used to manufacture superefficient airplanes.

7.3. The European Union claims that the alleged subsidies are prohibited under Articles 3.1(b) and 3.2 of the SCM Agreement as subsidies that are contingent on the use of domestic over imported goods. According to the European Union this contingency results from two siting provisions – a First Siting Provision and a Second Siting Provision – contained in Engrossed Substitute Senate Bill 5952 (ESSB 5952). The European Union requests that the Panel recommend that the United States withdraw the subsidies without delay, on the basis that they are prohibited subsidies, as required by Article 4.7 of the SCM Agreement.

7.4. The United States requests the Panel to find that the United States has acted consistently with its obligations under the SCM Agreement and to deny the relief requested by the European Union.

7.5. This Report is organized as follows. Section 7.2 sets out the relevant principles regarding the Panel's function, the burden of proof, and treaty interpretation. Section 7.3 provides a description and background of the measures at issue. In section 7.4, the Panel examines whether the measures challenged by the European Union constitute subsidies within the meaning of Article 1 of the SCM Agreement. In section 7.5 the Panel turns to an examination of whether the challenged measures are prohibited under Article 3 of the SCM Agreement. The Panel sets forth its conclusions and recommendation in section 8.

7.2 Function of the Panel, Burden of Proof, and Treaty Interpretation

7.2.1 Function of the Panel

7.6. According to Article 11 of the DSU:

The function of panels is to assist the DSB in discharging its responsibilities under this Understanding and the covered agreements. Accordingly, a panel should make an objective assessment of the matter before it, including an objective assessment of the

⁵³ United States' comments on European Union's request for review of the Panel's Interim Report, para. 24.

⁵⁴ These seven aerospace tax measures correspond to the nine tax-related provisions cited in para. 2.1 above. In the articulation of its claims, the European Union groups the sales and use tax exemptions for computer hardware, software, and peripherals in subparagraphs 2.1(d) and (f); and the sales tax exemptions for construction services and materials in subparagraphs 2.1(e) and (g).

facts of the case and the applicability of and conformity with the relevant covered agreements, and make such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the covered agreements.

7.7. The Panel has been required to examine municipal law in the course of exercising its functions under Article 11 of the DSU in this dispute. In this regard, the Appellate Body has explained that, "[a]lthough it is not the role of panels or the Appellate Body to interpret a Member's domestic legislation as such, it is permissible, indeed essential, to conduct a detailed examination of that legislation in assessing its consistency with WTO law".⁵⁵ The Appellate Body has added that:

As part of their duties under Article 11 of the DSU, panels have the obligation to examine the meaning and content of the municipal law at issue in order to make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability and conformity with the covered agreements. This obligation under Article 11 means that panels must conduct their own objective and independent assessment of the meaning of municipal law, instead of deferring to a party's characterization of such law.⁵⁶

7.8. In respect of the types and threshold of evidence that may be required to prove the WTO-inconsistency of municipal law, the Appellate Body has explained that "[i]f the meaning and content of the measure are clear on its face, then the consistency of the measure as such can be assessed on that basis alone. If, however, the meaning ... is not evident on its face, further examination is required."⁵⁷ The nature and the extent of the evidence required to satisfy the burden of proof will vary from case to case.⁵⁸ In some cases, the text of the relevant legislation may be sufficient to clarify the content and the meaning of the relevant legal instruments. In other cases, the parties will also need to support their understanding of the content and meaning of such legal instruments with evidence beyond the text of the instrument, such as evidence of consistent application of such laws, pronouncements of domestic courts on the meaning of such laws, the opinions of legal experts, and the writings of recognized scholars.⁵⁹ The task of a panel may be facilitated by agreement between the parties about the meaning of the law and its interpretation, being an interpretation that it is open for the panel to itself adopt. The Appellate Body has added that, "in ascertaining the meaning of municipal law, a panel should undertake a holistic assessment of all relevant elements, starting with the text of the law and including, but not limited to, relevant practices of administering agencies" as well as "legal interpretation[s] given by a domestic court or by a domestic administering agency as to the meaning of municipal law with respect to the measure being reviewed for consistency with the covered agreements".⁶⁰

7.2.2 Burden of proof

7.9. The general rule in WTO dispute settlement is that the burden of proof rests upon the party, whether complaining or defending, who asserts the affirmative of a particular claim or defence.⁶¹ Following this principle, the Appellate Body has explained that the complaining party in any given dispute should establish a *prima facie* case of inconsistency of a measure with a provision of the WTO covered agreements, before the burden of showing consistency with that provision or defending it under an exception must be assumed by the defending party.⁶² In other words, "a

⁵⁵ Appellate Body Report, *US – Hot-Rolled Steel*, para. 200. See also Appellate Body Report, *US – Carbon Steel (India)*, p. 4.445.

⁵⁶ Appellate Body Report, *US – Carbon Steel (India)*, p. 4.445 (citing Appellate Body Report, *India – Patents (US)*, para. 66).

⁵⁷ Appellate Body Report, *US – Corrosion-Resistant Steel Sunset Review*, para. 168.

⁵⁸ Appellate Body Report, *US – Carbon Steel*, para. 157. See also Appellate Body Report, *US – Carbon Steel (India)*, p. 4.446.

⁵⁹ Appellate Body Reports, *US – Countervailing and Anti-Dumping Measures (China)*, para. 4.100; *US – Carbon Steel*, para. 157; *US – Carbon Steel (India)*, para. 4.446.

⁶⁰ Appellate Body Report, *US – Countervailing and Anti-Dumping Duties (China)*, para. 4.101. See also Appellate Body Report, *US – Carbon Steel (India)*, para. 4.446.

⁶¹ Appellate Body Report, *US – Wool Shirts and Blouses*, p. 14, DSR 1997:I, p. 323 at p. 335.

⁶² Appellate Body Report, *EC – Hormones*, para. 104.

party claiming a violation of a provision of the *WTO Agreement* by another Member must assert and prove its claim."⁶³

7.10. A *prima facie* case is "one which, in the absence of effective refutation by the defending party, requires a panel, as a matter of law, to rule in favour of the complaining party presenting the *prima facie* case."⁶⁴ To establish a *prima facie* case, the party asserting a particular claim must adduce evidence sufficient to raise a presumption that what is claimed is true. If the complaining party "adduces evidence sufficient to raise a presumption that what is claimed is true, the burden then shifts to the other party, who will fail unless it adduces sufficient evidence to rebut the presumption."⁶⁵ In this regard, the Appellate Body has stated that:

[P]recisely how much and precisely what kind of evidence will be required to establish such ... [presumptions] will necessarily vary from measure to measure, provision to provision, and case to case.⁶⁶

7.11. The Appellate Body has also stated that "[a] complaining party may not simply submit evidence and expect the panel to divine from it a claim of WTO-inconsistency. Nor may a complaining party simply allege facts without relating them to its legal arguments".⁶⁷

7.12. In this dispute, the European Union bears the burden of establishing a *prima facie* case that the disputed measures are prohibited subsidies inconsistent with Article 3 of the SCM Agreement. In addition, if the Panel finds that the European Union has made out its *prima facie* case, it is for the United States to provide rebuttal arguments and evidence that is needed to support that rebuttal.

7.2.3 Treaty interpretation

7.13. Article 3.2 of the DSU provides that Members recognise that the dispute settlement system serves to clarify the provisions of the covered agreements "in accordance with customary rules of interpretation of public international law". It is well established that the principles codified in Articles 31 and 32 of the Vienna Convention on the Law of Treaties (the "Vienna Convention")⁶⁸ are such customary rules of interpretation of public international law.⁶⁹ They provide as follows:

ARTICLE 31 *General rule of interpretation*

1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.
2. The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes:
 - (a) any agreement relating to the treaty which was made between all the parties in connexion with the conclusion of the treaty;
 - (b) any instrument which was made by one or more parties in connexion with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.
3. There shall be taken into account together with the context:

⁶³ Appellate Body Report, *US – Wool Shirts and Blouses*, p. 16, DSR 1997:I, p. 323 at p. 337.

⁶⁴ Appellate Body Report, *EC – Hormones*, para. 104.

⁶⁵ Appellate Body Report, *US – Wool Shirts and Blouses*, p. 14, DSR 1997:I, p. 323 at p. 335. (footnote omitted)

⁶⁶ Ibid.

⁶⁷ Appellate Body Report, *US – Gambling*, para. 140.

⁶⁸ Done at Vienna, 23 May 1969, 1155 United Nations Treaty Series 331 (1980); 8 *International Legal Materials* 679 (1969).

⁶⁹ See, e.g. Appellate Body Report, *US – Shrimp*, para. 114.

- (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
 - (b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
 - (c) any relevant rules of international law applicable in the relations between the parties.
4. A special meaning shall be given to a term if it is established that the parties so intended.

ARTICLE 32 *Supplementary means of interpretation*

Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31:

- (a) leaves the meaning ambiguous or obscure; or
- (b) leads to a result which is manifestly absurd or unreasonable.

7.14. There is a considerable body of WTO case law dealing with the application of these provisions. It is clear that interpretation must be based above all on the text of the treaty⁷⁰, but that the context of the treaty also plays a role. It is also well-established that these principles of interpretation "neither require nor condone the imputation into a treaty of words that are not there or the importation into a treaty of concepts that were not intended."⁷¹ Furthermore, panels "must be guided by the rules of treaty interpretation set out in the Vienna Convention, and must not add to or diminish rights and obligations provided in the WTO Agreement."⁷²

7.3 Description and background of the measures at issue

7.3.1 Aerospace tax measures

7.15. The European Union challenges seven separate tax measures for civil aircraft provided by the state of Washington (aerospace tax measures) as amended and extended by ESSB 5952⁷³:

- (a) reduced business and occupation (B&O) tax rate for the manufacture and sale of commercial airplanes (B&O aerospace tax rate)⁷⁴;

⁷⁰ Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 11, DSR 1996:I, 97, at p. 105.

⁷¹ Appellate Body Report, *India – Patents (US)*, para. 45.

⁷² Ibid. para. 46.

⁷³ Engrossed Substitute Senate Bill 5952, Chapter 2, Laws of 2013 3rd Special Session, 2014 Wash. Sess. Laws 2, (ESSB 5952) (Exhibit EU-3). See European Union's first written submission, para. 15. Throughout these proceedings, the European Union has consistently referred to this legislation as "SSB 5952", rather than "ESSB 5952", explaining that it "omitted the 'Engrossed' and the 'E', in an effort to abbreviate the name". European Union's response to Panel question No. 52, para. 4. The United States has noted that the bill enacting the relevant legislation and conditions was *Engrossed* Substitute Senate Bill 5952, rather than Substitute Senate Bill 5952. United States' first written submission, fn 1. The United States has also clarified the legislative process beginning with Senate Bill 5952 as well as the series of amendments that led to the "Substitute" bill and subsequently the "Engrossed" bill that was passed by the Washington State legislature and approved by the Governor. United States' response to Panel question No. 52, paras. 1-5. The United States also confirmed that the citation in the European Union's panel request corresponds to ESSB 5952, and that the United States does not take the position that ESSB 5952 is outside the Panel's terms of reference. United States' response to Panel question No. 52, paras. 6-8. In light of this clarification and confirmation by the United States, the Panel refers to the legislation cited in the European Union's panel request as Engrossed Substitute Senate Bill 5952 (ESSB 5952) throughout this Report.

⁷⁴ ESSB 5952 (Exhibit EU-3), Sections 5-6, codified at RCW Section 82.04.260 (Exhibit EU-22).

- (b) B&O tax credit for pre-production development for commercial airplanes and components (B&O tax credit for aerospace product development)⁷⁵;
- (c) B&O tax credit for property taxes on commercial airplane manufacturing facilities (B&O tax credit for property and leasehold excise taxes)⁷⁶;
- (d) exemption from sales and use taxes for certain computer hardware, software, and peripherals (computer sales and use tax exemptions)⁷⁷;
- (e) exemption from sales and use taxes for certain construction services and materials (construction sales and use tax exemptions)⁷⁸;
- (f) exemption from leasehold excise taxes on port district facilities used to manufacture superefficient airplanes (leasehold excise tax exemption)⁷⁹; and
- (g) exemption from property taxes for the personal property of port district lessees used to manufacture superefficient airplanes (leaseholder property tax exemption)⁸⁰.

7.16. A person claiming the B&O tax credit for property and leasehold excise taxes, listed above as (c), is not eligible for either the leasehold excise tax exemption or the leaseholder property tax exemption, listed above as (f) and (g), respectively.

7.3.1.1 Measures related to the B&O tax

7.17. The first three aerospace tax measures listed above pertain to the business and occupation (B&O) tax, which is the state of Washington's "major business tax"⁸¹, in that the state of Washington "relies primarily on a B&O tax – rather than a corporate tax or an income tax – for purposes of business taxation".⁸² The B&O tax is imposed "for the act or privilege of engaging in business activities" and "is measured by the application of rates against the value of products, gross proceeds of sales, or gross income of the business, as the case may be".⁸³ The B&O tax applies to distinct business activities (such as retailing, manufacturing, wholesaling, extracting, and services). A business may have more than one B&O tax rate, depending on the types of activities conducted.⁸⁴

7.18. The first tax measure above (B&O aerospace tax rate) provides for a B&O tax rate of 0.2904% for specified business activities.⁸⁵ The other two B&O tax-related measures (B&O tax credits for aerospace product development and for property and leasehold excise taxes) provide credits against B&O tax liability based on specified expenditures or other tax payments made by the taxpayer concerned.⁸⁶ The rules regarding the calculation of B&O tax liability for different types of activities as well as the amount of B&O tax credits are discussed below in connection with whether there is a financial contribution in the sense of Article 1 of the SCM Agreement.

⁷⁵ ESSB 5952 (Exhibit EU-3), Section 9, codified at RCW Section 82.04.4461 (Exhibit EU-23).

⁷⁶ ESSB 5952 (Exhibit EU-3), Section 10, codified at RCW Section 82.04.4463 (Exhibit EU-24).

⁷⁷ ESSB 5952 (Exhibit EU-3), Sections 11-12, codified at RCW Section 82.08.975 (Exhibit EU-25) and RCW Section 82.12.975 (Exhibit EU-26).

⁷⁸ ESSB 5952 (Exhibit EU-3), Sections 3-4, codified at RCW Section 82.08.980 (Exhibit EU-27) and RCW Section 82.12.980 (Exhibit EU-28).

⁷⁹ ESSB 5952 (Exhibit EU-3), Section 13, codified at RCW Section 82.29A.137 (Exhibit EU-29).

⁸⁰ ESSB 5952 (Exhibit EU-3), Section 14, codified at RCW Section 84.36.655 (Exhibit EU-30).

⁸¹ See Final Bill Report, Engrossed Substitute Senate Bill 5952, (ESSB 5952 Final Bill Report) (Exhibit EU-4), p. 1.

⁸² United States' first written submission, para. 39.

⁸³ RCW Section 82.04.220(1) (Exhibit EU-32). See also United States' first written submission, paras. 39-41.

⁸⁴ See ESSB 5952 Final Bill Report (Exhibit EU-4), p. 1. See para. 7.77 below regarding B&O taxation of multiple business activities.

⁸⁵ See ESSB 5952 (Exhibit EU-3), Sections 5-6; RCW Section 82.04.260(11) (Exhibit EU-22); ESSB 5952 Final Bill Report (Exhibit EU-4), p. 3.

⁸⁶ See RCW Section 82.04.4461(2) (Exhibit EU-23).

7.3.1.2 Exemptions from sales and use taxes

7.19. The next two aerospace tax measures in the above list are exemptions from the state of Washington's retail sales and use taxes. The retail sales tax is Washington State's principal source of tax revenue (including business and non-business tax revenue)⁸⁷, and is collected from customers by businesses making retail sales in Washington State. The retail sales tax is generally imposed on the sale of tangible personal property⁸⁸ and digital products⁸⁹, as well as certain services⁹⁰, to the final consumer or end user of such property, digital product, or service.⁹¹ The use tax is a tax on the use of goods or certain services in the state of Washington when sales tax has not been paid.⁹² Goods used in Washington State are subject to either sales or use tax, but not to both; thus, the use tax compensates when the sales tax has not been paid.⁹³

7.20. The computer sales and use tax exemptions relate to sales or use "of computer hardware, computer peripherals, or software ... used primarily in the development, design, and engineering of aerospace products or in providing aerospace services".⁹⁴ These exemptions also relate to sales or use of "labor and services rendered in respect to installing the computer hardware, computer peripherals, or software".⁹⁵

7.21. The construction sales and use tax exemptions concern labour, services, and personal property used to construct new buildings for the manufacture of commercial airplanes or the fuselages and wings of commercial airplanes. More specifically, the sales tax exemption applies to retail sales taxes on "[c]harges, for labor and services rendered in respect to the constructing of new buildings, made to a manufacturer engaged in the manufacturing of commercial airplanes or the fuselages or wings of commercial airplanes".⁹⁶ Sales and use tax exemptions apply to the sales and use of "tangible personal property that will be incorporated as an ingredient or component"⁹⁷ in constructing such buildings. These construction sales and use tax exemptions also apply to charges for construction labour and services made to, and tangible personal property used in constructing new buildings for, "a port district, political subdivision, or municipal corporation, to be leased to a manufacturer engaged in the manufacturing of commercial airplanes or the fuselages or wings of commercial airplanes".⁹⁸

7.22. The applicable tax rates and coverage of retail sales and use taxes in Washington State are considered in greater detail below in connection with whether these exemptions constitute a financial contribution in the sense of Article 1 of the SCM Agreement.

⁸⁷ United States' first written submission, para. 42; Retail Sales Tax Explanation, Washington State Department of Revenue (Exhibit USA-12).

⁸⁸ Retail Sales Tax Explanation, Washington State Department of Revenue (Exhibit USA-12).

⁸⁹ Digital Products including Digital Goods, Washington State Department of Revenue (Exhibit USA-14).

⁹⁰ Services Subject to Sales Tax, Washington State Department of Revenue (Exhibit USA-13).

⁹¹ See ESSB 5952 Final Bill Report (Exhibit EU-4), p.1.

⁹² Use Tax Explanation, Washington State Department of Revenue (Exhibit USA-19). See also ESSB 5952 Final Bill Report (Exhibit EU-4), p.1; United States' first written submission, para. 44. For example, the use tax is owed if goods are purchased in another state that does not have a sales tax or a state with a sales tax lower than that of the state of Washington, and then used in the state of Washington. The use tax would also be owed if goods are purchased from someone who is not authorized to collect sales tax (e.g. purchases of furniture from an individual through a newspaper classified ad or a purchase of artwork from an individual collector), or if personal property is acquired with the purchase of real property.

⁹³ Use Tax Explanation, Washington State Department of Revenue (Exhibit USA-19).

⁹⁴ RCW Section 82.08.975 (Exhibit EU-25); RCW Section 82.12.975 (Exhibit EU-26); ESSB 5952 (Exhibit EU-3), Sections 11-12.

⁹⁵ RCW Section 82.08.975 (Exhibit EU-25); RCW Section 82.12.975 (Exhibit EU-26); ESSB 5952 (Exhibit EU-3), Sections 11-12.

⁹⁶ RCW Section 82.08.980 (Exhibit EU-27); ESSB 5952 (Exhibit EU-3), Section 3.

⁹⁷ RCW Section 82.08.980 (Exhibit EU-27); RCW Section 82.12.980 (Exhibit EU-28); ESSB 5952 (Exhibit EU-3), Sections 3-4. The United States explains that the "use tax is not due on construction services", which "accounts for why the language of the statute on its face appears to have a more limited scope when compared with the language for the exemption for the retail sales tax". United States' first written submission, fn 118.

⁹⁸ RCW Section 82.08.980(1)(a)(ii) (Exhibit EU-27); RCW Section 82.12.980(1)(a)(ii) (Exhibit EU-28).

7.3.1.3 Exemptions from taxes imposed on certain leaseholds

7.23. The final two aerospace tax measures concern property taxes imposed on certain leaseholds in Washington State. Real and personal property in Washington State is generally subject to property taxes based on its value, unless a specific exemption is provided by law.⁹⁹ For example, all property owned by federal, state, and local governments is exempt from the Washington State property tax.¹⁰⁰

7.24. The leasehold excise tax exemption relates to the Washington State leasehold excise tax, which is imposed in lieu of a property tax on the use of public property by a private party.¹⁰¹ More specifically, Washington State imposes "a leasehold excise tax on the act or privilege of occupying or using publicly owned real or personal property ... through a leasehold interest".¹⁰² The leasehold excise tax exemption applies to "[a]ll leasehold interests in port district facilities exempt from tax under [the construction sales and use tax exemptions] and used by a manufacturer engaged in the manufacturing of superefficient airplanes".¹⁰³

7.25. Under the leaseholder property tax exemption, Washington State also exempts from property taxation "all buildings, machinery, equipment, and other personal property of a lessee of a port district eligible [for the construction sales and use tax exemptions], used exclusively in manufacturing superefficient airplanes".¹⁰⁴

7.26. Neither the leasehold excise tax exemption nor the leaseholder property tax exemption is available to a person claiming the B&O tax credit for property and leasehold excise taxes.¹⁰⁵

7.3.2 Siting provisions

7.27. The European Union identifies two "siting" provisions that govern the availability of the above aerospace tax measures, namely a First Siting Provision¹⁰⁶ relating to all of the aerospace tax measures, and a Second Siting Provision¹⁰⁷ relating only to the B&O aerospace tax rate.¹⁰⁸

7.3.2.1 First Siting Provision

7.28. Each of the above aerospace tax measures is extended, and certain others are also amended, by ESSB 5952, which, according to the First Siting Provision in Section 2 of ESSB 5952, "takes effect contingent upon the siting of a significant commercial airplane manufacturing program in the state of Washington". Alternatively, "[i]f a significant commercial airplane manufacturing program is not sited in the state of Washington by June 30, 2017, ... [this act] does not take effect".¹⁰⁹

⁹⁹ See ESSB 5952 Final Bill Report (Exhibit EU-4), p. 1; RCW Section 84.36.005 (Exhibit USA-20); United States' first written submission, para. 46.

¹⁰⁰ RCW Section 84.36.010 (Exhibit USA-21). See also ESSB 5952 Final Bill Report (Exhibit EU-4), pp. 1-2; United States' first written submission, para. 46.

¹⁰¹ Leasehold Excise Tax Explanation, Washington State Department of Revenue (Exhibit USA-25).

¹⁰² RCW Section 82.29A.030 (Exhibit USA-26).

¹⁰³ RCW Section 82.29A.137 (Exhibit EU-29). Under Washington State law, "superefficient airplane" is defined as "a twin aisle airplane that carries between two hundred and three hundred fifty passengers, with a range of more than seven thousand two hundred nautical miles, a cruising speed of approximately mach .85, and that uses fifteen to twenty percent less fuel than other similar airplanes on the market". RCW Section 82.32.550(3) (Exhibit EU-82).

¹⁰⁴ RCW Section 84.36.655 (Exhibit EU-30).

¹⁰⁵ RCW 82.29A.137(1) (Exhibit EU-29); RCW 84.36.655(1) (Exhibit EU-30). These refer to measures (f), (g), and (c), respectively, in the list in para. 7.15 above.

¹⁰⁶ The European Union refers to this as the "Programme-Siting Condition". See European Union's first written submission, paras. 42-45. The United States refers to this as the "Initial Siting Provision".

United States' first written submission, paras. 74-78.

¹⁰⁷ The European Union refers to this as the "Exclusive-Production Condition". European Union's first written submission, paras. 46-52. The United States refers to this as the "Future Siting Provision". See United States' first written submission, paras. 55-56, 79-80.

¹⁰⁸ See Request for the Establishment of a Panel by the European Union, WT/DS487/2, 13 February 2015, p. 2.

¹⁰⁹ ESSB 5952 (Exhibit EU-3), Section 2, codified at RCW Section 82.32.850 (Exhibit EU-58).

7.29. The First Siting Provision defines "siting" to mean "a final decision, made on or after November 1, 2013, by a manufacturer to locate a significant commercial airplane manufacturing program in Washington State". In turn, "significant commercial airplane manufacturing program" is defined as:

[A]n airplane program in which the following products, including final assembly, will commence manufacture at a new or existing location within Washington state on or after the effective date of this section:

- (i) The new model, or any version or variant of an existing model, of a commercial airplane; and
- (ii) Fuselages and wings of a new model, or any version or variant of an existing model, of a commercial airplane.¹¹⁰

7.30. The First Siting Provision additionally defines "new model, or any version or variant of an existing model, of a commercial airplane" to mean "a commercial airplane manufactured with a carbon fiber composite fuselage or carbon fiber composite wings or both".¹¹¹

7.31. Both parties agree that the First Siting Provision has been fulfilled and, as a result, the measures set out in ESSB 5952 are in effect.¹¹²

7.3.2.2 Second Siting Provision

7.32. ESSB 5952 also contains a Second Siting Provision, relating only to the B&O aerospace tax rate¹¹³, which provides as follows:

With respect to the manufacturing of commercial airplanes or making sales, at retail or wholesale, of commercial airplanes, this subsection (11) [i.e. the B&O aerospace tax rate] does not apply on and after July 1st of the year in which the department [i.e. the Department of Revenue] makes a determination that any final assembly or wing assembly of any version or variant of a commercial airplane that is the basis of a siting of a significant commercial airplane manufacturing program in the state under section 2 of this act [i.e. the First Siting Provision] has been sited outside the state of Washington. This subsection (11)(e)(ii) [i.e. the Second Siting Provision] only applies to the manufacturing or sale of commercial airplanes that are the basis of a siting of a significant commercial airplane manufacturing program in the state under section 2 of this act.

7.33. The Second Siting Provision thus concerns the continued availability of the B&O aerospace tax rate for the version or variant of the commercial airplane that is the basis of the First Siting Provision. The Second Siting Provision specifically pertains to the siting of "any final assembly or wing assembly" of that commercial airplane. As agreed by the parties, and as explained more fully below, the Boeing 777X is the relevant version or variant of commercial airplane that served as the basis for fulfilment of the First Siting Provision.¹¹⁴

¹¹⁰ ESSB 5952 (Exhibit EU-3), Section 2(2)(c) and (d), codified at RCW 82.32.850(2)(c) and (d) (Exhibit EU-58).

¹¹¹ ESSB 5952 (Exhibit EU-3), Section 2(2)(b), codified at RCW 82.32.850(2)(b) (Exhibit EU-58).

¹¹² Notification Letter from Carol K. Nelson, Director, Washington State Department of Revenue, to Kyle Thiessen, Washington State Code Reviser, 10 July 2014 (Exhibit EU-61). United States' first written submission, para. 78. See para. 7.273 below regarding the details of fulfilment of the First Siting Provision.

¹¹³ ESSB 5952 (Exhibit EU-3), Sections 5-6(11)(e)(ii), codified at RCW 82.04.260(e)(ii) (Exhibit EU-22).

¹¹⁴ See European Union's first written submission, para. 46; United States' first written submission, para. 56.

7.3.3 Legislative background and scope of the measures at issue

7.34. ESSB 5952 amends and extends certain tax measures established in 2003 under Washington State Legislature House Bill 2294 (HB 2294)¹¹⁵, which were measures at issue in the dispute *US – Large Civil Aircraft (2nd complaint)*.¹¹⁶

7.35. The parties have raised different views as to the temporal scope of the measures at issue and the applicability of the contingencies introduced by ESSB 5952. For example, with reference to pre-existing tax measures in Washington State, the United States submits that "[a]bsent ESSB 5952, aerospace activity through 2024 subject to the B&O tax, the sales and use tax, the property excise tax, and the leasehold excise tax would have qualified under HB 2294 and for the [aerospace tax measures] identified by the European Union", and thus contends that "the treatment prior to 2024 under any of these measures, even if the measure were determined to be a subsidy, is *a priori* not contingent on any conditions introduced by ESSB 5952".¹¹⁷ By contrast, the European Union asserts that its challenge is not limited to the *extended* tax treatment from 2024 to 2040 effected by ESSB 5952, but rather that "the European Union is challenging the subsidies at issue from the point in time that they became contingent on satisfaction of the [First Siting Provision] conditions in SSB 5952, i.e., November 2013. The European Union challenges the existence of a financial contribution for the whole period from November 2013 through June 2040."¹¹⁸

7.36. In light of these differing assertions, the Panel first reviews the legislative background and scope of the measures at issue before turning to the claims raised in this dispute. The tax measures adopted by the Washington State Legislature in 2003 under HB 2294 included a reduction in the B&O tax rate¹¹⁹; a B&O tax credit for pre-production development expenditures¹²⁰; a B&O tax credit for computer software and hardware¹²¹; and a B&O tax credit for property taxes paid on property used in the manufacture of commercial airplanes and airplane components.¹²² Also included were sales and use tax exemptions for computer equipment and software, and their installation, as well as construction services and equipment, used primarily in the development of commercial airplanes and components.¹²³ A leasehold excise tax exemption and property tax exemption for port district facilities was also available to manufacturers of superefficient airplanes that were not using the B&O tax credit for property taxes.¹²⁴ These measures were scheduled to end in 2024.¹²⁵

7.37. ESSB 5952 extended the availability of these tax measures to 2040 upon fulfilment of the First Siting Provision through the siting of the Boeing 777X programme. ESSB 5952 also provided that the B&O aerospace tax rate would no longer apply to that programme if the conditions foreseen in the Second Siting Provision occurred. At the same time, the aerospace tax measures reflect substantive amendments made by ESSB 5952 as well as other legislative changes made to the tax measures in the intervening period between HB 2294 and ESSB 5952. For example, with regard to the B&O aerospace tax rate, in 2006, Washington State Legislature House Bill 2466 (HB 2466) also extended the reduced B&O tax rate to certain certified repair stations¹²⁶, and consolidated the B&O aerospace tax rates for the manufacture of commercial airplanes and

¹¹⁵ House Bill 2294, 2003 Wash. Sess. Laws 2767, (HB 2294) (Exhibit EU-21).

¹¹⁶ See Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.39.

¹¹⁷ United States' response to Panel question No. 2, para. 3. See also United States' response to Panel question Nos. 53, 54, and 58.

¹¹⁸ European Union's second written submission, para. 18. See also European Union's response to Panel question No. 6, para. 8.

¹¹⁹ HB 2294 (Exhibit EU-21), Sections 3-4; Panel Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 7.47-7.49.

¹²⁰ HB 2294 (Exhibit EU-21), Section 7; Panel Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 7.51-7.52.

¹²¹ HB 2294 (Exhibit EU-21), Section 8; Panel Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 7.53-7.54.

¹²² HB 2294 (Exhibit EU-21), Section 15; Panel Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 7.55-7.56.

¹²³ HB 2294 (Exhibit EU-21), Sections 9-12; Panel Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 7.59-7.62.

¹²⁴ HB 2294 (Exhibit EU-21), Sections 13-14; Panel Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 7.64-7.68.

¹²⁵ HB 2294 (Exhibit EU-21); ESSB 5952 Final Bill Report (Exhibit EU-4), p. 2.

¹²⁶ House Bill 2466, 2006 Wash. Sess. Laws 787, (HB 2466) (Exhibit EU-35), Section 5.

components, and for the sales of commercial airplanes and components, into a single provision covering both manufacture and sales.¹²⁷ In addition, Substitute Senate Bill 6828 (SSB 6828) of 2008 extended the reduced B&O tax rate to the manufacture and retailing of tooling used in the manufacture of commercial airplanes and components of airplanes.¹²⁸ The B&O tax credit for aerospace product development reflects an extension of the credit to non-manufacturing firms under HB 2466 of 2006.¹²⁹ It further reflects the extension under SSB 6828 of the credit for preproduction development to "aerospace product development", which was subsequently carried over in the provisions extended by ESSB 5952.¹³⁰ The B&O tax credit for property and leasehold excise taxes amended by ESSB 5952 reflects the prior 2006 amendment under HB 2466 to include leasehold excise taxes in addition to property taxes as part of this B&O tax credit.¹³¹ The computer sales and use tax exemptions amended by ESSB 5952 reflect prior changes made under HB 2466 of 2006 and under SSB 6828 of 2008.¹³² Further, ESSB 5952 amends the construction sales and use tax exemptions originally established in HB 2294 by changing their application to "the manufacturing of commercial airplanes or the fuselages and wings of commercial airplanes" rather than to "manufacturing of superefficient airplanes".¹³³

7.38. ESSB 5952 was enacted in November 2013 by the Washington State legislature. Pursuant to the First Siting Provision, the aerospace tax measures, as amended and extended by ESSB 5952, were to take effect upon the determination by the Department of Revenue of Washington State that the First Siting Provision had been satisfied, based on the "siting" of a "significant commercial airplane manufacturing program" as defined in that provision. On 9 July 2014, Boeing submitted a letter to the Department of Revenue of Washington State providing formal notification that Boeing had made a final decision to manufacture the 777X in Washington State, and describing how the 777X satisfied the requirements of the First Siting Provision.¹³⁴ The Department of Revenue of Washington State provided written notice on 10 July 2014 of its determination that the First Siting Provision had been fulfilled and that ESSB 5952 had taken effect on 9 July 2014.¹³⁵ The Boeing 777X was the model of commercial airplane that served as the basis for determining that the First Siting Provision had been fulfilled.¹³⁶

7.39. For the purposes of this dispute, the measures that are within the Panel's terms of reference are those identified by the European Union in its request for the establishment of a panel.¹³⁷ These measures are the aerospace tax measures, as presently codified in the RCW provisions cited in the European Union's panel request.¹³⁸ The aerospace tax measures as codified¹³⁹ reflect the substantive amendments made under ESSB 5952 as well as other legislative amendments

¹²⁷ HB 2466 (Exhibit EU-35), Section 4.

¹²⁸ Substitute Senate Bill 6828, 2008 Wash. Sess. Laws 365, (SSB 6828) (Exhibit EU-42), Section 4.

¹²⁹ HB 2466 (Exhibit EU-35), Section 3; ESSB 5952 Final Bill Report (Exhibit EU-4), p. 2; United States' first written submission, para. 62.

¹³⁰ SSB 6828 (Exhibit EU-42), Section 7; United States' first written submission, para. 62 (noting that this "broadened the B&O tax credit for aerospace product development to include expenditures in developing aerospace products, such as machinery for maintaining and repairing commercial airplanes and tooling equipment").

¹³¹ See HB 2466 (Exhibit EU-35), Section 10.

¹³² Thus, the currently codified provisions of these exemptions omit the limitation to manufacturers or processors for hire of commercial airplanes or components of such airplanes that originally existed under HB 2294. See HB 2294 (Exhibit EU-21), Sections 9-10; ESSB 5952 (Exhibit EU-3), Sections 11-12.

¹³³ See HB 2294 (Exhibit EU-21), Sections 11-12; ESSB 5952 (Exhibit EU-3), Sections 3-4.

¹³⁴ Letter from Boeing to Carol K. Nelson, Director, Washington State Department of Revenue, regarding decision to site 777X programme, 9 July 2014 (Exhibit USA-32) (BCI).

¹³⁵ Letter from the Director of the Washington State Department of Revenue to the Code Reviser, 10 July 2014 (Exhibit EU-61).

¹³⁶ United States' first written submission, para. 56.

¹³⁷ See Constitution of the Panel Established at the Request of the European Union – Note by the Secretariat, WT/DS487/3, 23 April 2015.

¹³⁸ The Panel notes that the United States has focused upon the enacted results of ESSB 5952, rather than the legislative bill itself, stating that "ESSB 5952 is not itself a measure challenged by the EU." United States' first written submission, fn 99. As further explained by the United States, "provisions of legislation like HB 2294 or ESSB 5952 operate as law to the extent they are codified in the RCW, and any provision so codified will continue to do so until it is amended, rescinded, or expires." United States' comments the European Union's response to Panel question No. 54, para. 10.

¹³⁹ In this connection, RCW Section 1.04.020 states that "[a]ny section of the Revised Code of Washington ... expressly amended by the legislature, including the entire context set out, shall, as so amended, constitute the law and the ultimate declaration of legislative intent." RCW Section 1.04.020 in Chapter 1.04 RCW (Exhibit USA-63).

subsequent to the enactment of HB 2294 in 2003, and are presently in effect until 2040. The aerospace tax measures are further subject to the First and Second Siting Provisions, which were introduced by ESSB 5952.

7.40. Recalling the parties' different views as to the temporal scope of the measures at issue and the applicability of the contingencies introduced by ESSB 5952, the Panel considers that the measures at issue are not limited to tax treatment for the period of extension from 2024 to 2040. Rather, given the Panel's terms of reference as well as the various substantive amendments effected by ESSB 5952 and prior to its passage, the aerospace tax measures and Siting Provisions at issue are those that are in effect pursuant to codified provisions of Washington State law following the enactment and entry into force of ESSB 5952.

7.4 Existence of a subsidy under Article 1 of the SCM Agreement

7.4.1 Arguments of the parties

7.41. The European Union contends that the aerospace tax measures are subsidies within the meaning of Article 1 of the SCM Agreement.¹⁴⁰ According to the European Union, each of the aerospace tax measures at issue constitutes a financial contribution under Article 1.1(a)(1)(ii) of the SCM Agreement because "government revenue that is otherwise due is foregone or not collected". In support of its contention, the European Union proposes various benchmarks for comparison for the aerospace tax measures and contends that, in relation to these benchmarks, government revenue that would otherwise be due is foregone. The European Union also draws upon findings in *US – Large Civil Aircraft (2nd complaint)* and contends that similar considerations apply in respect of measures that are analogous to those that were found to constitute financial contributions in that dispute. At the same time, the European Union distinguishes its claim from that made in *US – Large Civil Aircraft (2nd complaint)* as it argues in the present case "that a financial contribution exists in the abstract" rather than being entity-specific.¹⁴¹ The European Union contends that government revenue does not need to have been *actually* foregone for there to be a financial contribution, but rather that it is the foregoing of the government's *entitlement* to collect revenue that is determinative of a financial contribution.¹⁴² Further, the European Union argues that the conferral of a benefit is a natural consequence of the foregoing of government revenue in comparison to "market" conditions.¹⁴³

7.42. The United States asserts that the European Union fails to make a *prima facie* case that any of the challenged measures constitutes a financial contribution. The United States also disputes the European Union's reliance on findings made in respect of contested measures in *US – Large Civil Aircraft (2nd complaint)* to demonstrate a financial contribution in this dispute.¹⁴⁴ While acknowledging the European Union's clarification as to a financial contribution existing "in the abstract", the United States contends that the present tense drafting of Article 1.1(a)(ii) means that "this provision covers revenue foregone or not collected *in the present*".¹⁴⁵ In addition, the United States disagrees with various legal interpretations advanced by the European Union, including that the term "maintain" in Article 3.2 refers to the continuation of a subsidy that has been "granted"¹⁴⁶, as well as the European Union's distinction between the terms "not collected" and "foregone", arguing that both are in the present passive tense, and that "the two verbs describe different ways that the government may obtain tax income".¹⁴⁷ With respect to the

¹⁴⁰ European Union's first written submission, para. 53; second written submission, para. 9; opening statement at the first meeting of the Panel, para. 15; opening statement at the second meeting of the Panel, para. 12.

¹⁴¹ European Union's response to Panel question No. 23, para. 45 (quoting Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.151). See also European Union's second written submission, para. 34.

¹⁴² See European Union's second written submission, para. 21; opening statement at the second meeting of the Panel, paras. 15-16.

¹⁴³ European Union's first written submission, paras. 67-68; second written submission, paras. 36-37; opening statement at the first meeting of the Panel, para. 35; opening statement at the second meeting of the Panel, para. 23.

¹⁴⁴ United States' first written submission, para. 94-99.

¹⁴⁵ United States' second written submission, para. 86. (emphasis original) The United States further submits that the European Union's legal arguments do not overcome "the implication of the present tense drafting of Article 1.1(a)(ii)". United States' second written submission, para. 87.

¹⁴⁶ United States' second written submission, para. 88.

¹⁴⁷ United States' second written submission, para. 89.

benefit allegedly conferred, the United States agrees with the European Union that "the concept of financial contribution in the form of revenue foregone that is otherwise due often overlaps with the concept of benefit", but contends that "[t]he European Union has not identified with sufficient clarity what the benefit is that it is alleging, much less provided evidence that the two concepts fully overlap in the present case."¹⁴⁸ The United States further contends that the European Union erroneously argues that a finding of benefit proceeds automatically from a finding that revenue is foregone.¹⁴⁹

7.4.2 Third-party views

7.43. Australia submits "that by the very nature of the type of transaction relating to the foregoing or non-collection of government revenue, the actual use or exercise of the fiscal incentive by a beneficiary/recipient may not necessarily be determinative in establishing the existence of a financial contribution".¹⁵⁰ Accordingly, Australia frames the question as "whether, but for the tax incentive, the beneficiary of the tax measure would owe revenue payable as a debt, but expect it to be forgone or not collected".¹⁵¹ With regard to the benefit conferred, Australia refers to the standard of a measure making a recipient "better off" in comparison to the marketplace, and that, "[i]n this instance, the marketplace would be made up of other companies facing the usual tax rates set by Washington State, without provision of the discounts offered to companies that qualified for the tax exemption/discount".¹⁵²

7.4.3 Whether there is a financial contribution as "government revenue that is otherwise due is foregone or not collected"

7.44. Article 1.1(a)(1)(ii) of the SCM Agreement provides in relevant part:

1.1 For the purpose of this Agreement, a subsidy shall be deemed to exist if:

(a)(1) there is a financial contribution by a government ... , i.e. where:

(ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits); (footnote omitted)

7.45. With regard to the legal standard under Article 1.1(a)(1)(ii) of the SCM Agreement, the Appellate Body has set out the following considerations:

In our view, the "*foregoing*" of revenue "*otherwise due*" implies that less revenue has been raised by the government than would have been raised in a different situation, or, that is, "*otherwise*". Moreover, the word "*foregone*" suggests that the government has given up an entitlement to raise revenue that it could "*otherwise*" have raised. This cannot, however, be an entitlement in the abstract, because governments, in theory, could tax *all* revenues. There must, therefore, be some defined, normative benchmark against which a comparison can be made between the revenue actually raised and the revenue that would have been raised "*otherwise*".¹⁵³ (emphasis original)

7.46. The Appellate Body therefore considered that "the term 'otherwise due' implies some kind of comparison between the revenues due under the contested measure and revenues that would be due in some other situation", and that "the basis of comparison must be the tax rules applied by the Member in question".¹⁵⁴ The Appellate Body further stated that, "[i]n identifying the appropriate benchmark for comparison, panels must obviously ensure that they identify and examine fiscal situations which it is legitimate to compare. In other words, there must be a

¹⁴⁸ United States' response to Panel question No. 22, para. 53.

¹⁴⁹ United States' second written submission, para. 93.

¹⁵⁰ Australia's response to Panel question No. 1.

¹⁵¹ Ibid.

¹⁵² Australia's response to Panel question No. 2.

¹⁵³ Appellate Body Report, *US – FSC*, para. 90.

¹⁵⁴ Ibid. The Appellate Body further noted that a "WTO Member, in principle, has the sovereign authority to tax any particular categories of revenue it wishes" and that "[w]hat is 'otherwise due', therefore, depends on the rules of taxation that each Member, by its own choice, establishes for itself."

rational basis for comparing the fiscal treatment of the income subject to the contested measure and the fiscal treatment of certain other income."¹⁵⁵

7.47. The Appellate Body considered that there may be situations where the measures at issue might be described as an "exception" to a general rule of taxation, and that in such situations it may be possible to apply a "but for" test to examine the fiscal treatment of income absent the contested measure. At the same time, given the variety and complexity of domestic tax systems, the Appellate Body did not consider that "Article 1.1(a)(1)(ii) always *requires* panels to identify, with respect to any particular income, the 'general' rule of taxation prevailing in a Member".¹⁵⁶ Instead, the Appellate Body explained "that panels should seek to compare the fiscal treatment of legitimately comparable income to determine whether the contested measure involves the foregoing of revenue which is 'otherwise due', in relation to the income in question".¹⁵⁷

7.48. In *US – Large Civil Aircraft (2nd complaint)*, the Appellate Body reiterated the principle that it is necessary to identify "legitimately comparable" situations of taxation in order to determine whether government revenue is foregone.¹⁵⁸ The Appellate Body further articulated three analytical steps for a panel examining a claim under Article 1.1(a)(1)(ii) of the SCM Agreement.

7.49. First, a panel should "identify the tax treatment that applies to the income of the alleged recipients", which "will entail consideration of the objective reasons behind that treatment and, where it involves a change in a Member's tax rules, an assessment of the reasons underlying that change".¹⁵⁹

7.50. Second, "the panel should identify a benchmark for comparison – that is, the tax treatment of comparable income of comparably situated taxpayers", which "involves an examination of the structure of the domestic tax regime and its organizing principles".¹⁶⁰ The Appellate Body noted the potential difficulty of this exercise given that such principles may "be unique to the particular domestic regime" or "that disparate tax measures, implemented over time, do not easily offer up coherent principles serving as a benchmark".¹⁶¹ Nevertheless, "the task of the panel is to develop an understanding of the tax structure and principles that best explains that Member's tax regime, and to provide a reasoned basis for identifying what constitutes comparable income of comparably situated taxpayers".¹⁶²

7.51. Third, "the panel should compare the reasons for the challenged tax treatment with the benchmark tax treatment it has identified after scrutinizing a Member's tax regime".¹⁶³ According to the Appellate Body, this "comparison will enable a panel to determine whether, in the light of the treatment of the comparable income of comparably situated taxpayers, the government is foregoing revenue that is otherwise due in relation to the income of the alleged recipients."¹⁶⁴

7.52. Before proceeding to the analysis of each aerospace tax measure under Article 1.1(a)(1)(ii) of the SCM Agreement, the Panel will address the United States' argument that aerospace activity until 1 July 2024 would have qualified for certain tax treatment under legislation pre-dating ESSB 5952, and that the extent of any financial contribution in this dispute would be limited to revenue foregone at some point in the future.¹⁶⁵ The Panel recalls that the European Union has argued that, unlike in a past dispute under another provision of the SCM Agreement, in this case the European Union is advancing its claim in the abstract, on the basis of the pertinent legislation as such, and that it considers that Article 1.1(a)(1)(ii) covers not only the foregoing of actual revenue in the present, but also the foregoing of an entitlement to future revenue.¹⁶⁶

¹⁵⁵ Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 90.

¹⁵⁶ Ibid. para. 91. (emphasis original)

¹⁵⁷ Ibid.

¹⁵⁸ See Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 810-812.

¹⁵⁹ Ibid. para. 812.

¹⁶⁰ Ibid. para. 813.

¹⁶¹ Ibid.

¹⁶² Ibid.

¹⁶³ Ibid. para. 814.

¹⁶⁴ Ibid.

¹⁶⁵ United States' response to Panel question Nos. 2 and 21; second written submission, paras. 85-92.

¹⁶⁶ European Union's response to Panel question Nos. 6 and 21.

7.53. In respect of the measures at issue, the Panel agrees with the European Union that Article 1.1(a)(1)(ii) of the SCM Agreement encompasses the foregoing of revenue in the future.¹⁶⁷ In the particular context of tax-based measures, the underlying legislation may be effective over a period defined in the legislation itself, or indefinitely. Where such legislation gives rise to a financial contribution in the form of revenue foregone, the fact of a government having forgone such revenue is true for the entire period during which the legislation is in force. Even if the effective start date of a period defined in the legislation is subsequent to the date on which the legislation enters into force, as of the date of entry into force the government would have, by virtue of the legislation, already given up its entitlement to the future tax revenue during the defined future period.¹⁶⁸ That entitlement could be re-established through further legislation revoking or amending the previous legislation. This principle is implicit in past cases involving financial contributions from tax-based measures. Where the rulings in those cases have been based on the underlying legislation as such, they have not only concerned particular revenue streams foregone in particular periods, but instead have concerned all of the implicit future revenue streams that would be foregone pursuant to the underlying legislation.¹⁶⁹

7.54. In this connection, the present tense of the verb "is" in Article 1.1(a)(1)(ii) relates to a government presently foregoing an entitlement to collect revenue either now or in the future.¹⁷⁰ It is this government action taken with respect to otherwise applicable tax liabilities that is the focus of the analysis under Article 1.1(a)(1)(ii), particularly where the measures are challenged as such rather than "against the application ... during any given point in time or in any specific instance".¹⁷¹ In this dispute, the Panel has determined that the aerospace tax measures at issue are those that are presently in effect pursuant to codified provisions of Washington State law following the enactment and entry into force of ESSB 5952.¹⁷² A finding that the aerospace tax measures result in government revenue being foregone, or that they cause government revenue to be foregone, be it currently or in the future, applies to the measures themselves. This foregoing of revenue would apply to taxpayers at any time during the entire period in which the measures are in force. The foregoing of revenue is constituted by the government's promise to do so, and not only by particular instances of it being done.

7.55. Having addressed the threshold issue of revenue foregone in the future, the Panel now examines each of the challenged aerospace tax measures, as such, on the basis of the analytical framework outlined above, to assess whether any of them involves a financial contribution in the form of government revenue foregone within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement.

7.4.3.1 B&O aerospace tax rate

7.56. The legislation for the B&O aerospace tax rate provides in relevant part:

(11)(a) Beginning October 1, 2005, upon every person engaging within this state in the business of manufacturing commercial airplanes, or components of such airplanes, or making sales, at retail or wholesale, of commercial airplanes or components of such airplanes, manufactured by the seller, as to such persons the amount of tax with respect to such business is, in the case of manufacturers, equal to the value of the product manufactured and the gross proceeds of sales of the product manufactured,

¹⁶⁷ The Panel notes that the United States does not categorically reject the possibility that a financial contribution may occur in the future.

¹⁶⁸ This is consistent with the Appellate Body's characterization of a government having "given up an entitlement to raise revenue that it could 'otherwise' have raised". Appellate Body Report, *US – FSC*, para. 90.

¹⁶⁹ See, e.g. Panel Report, *US – FSC*, paras. 7.98-7.101. In that dispute, the panel examined the "FSC scheme" as a whole, and noted *inter alia* that for any given fiscal year, a corporation was free to elect whether or not to have the status of a FSC. Thus, it was the existence and operation of the scheme itself, which was of indefinite duration under the US tax laws, that gave rise to the finding of revenue foregone, rather than individual instances of application of the scheme by particular corporations, or instances of application of the scheme during any particular period. This aspect of the panel report was not appealed.

¹⁷⁰ See United States' second written submission, para. 86 ("By virtue of the present tense verb 'is', this provision covers revenue foregone or not collected *in the present*. Thus, Article 1.1(a)(1)(ii) deals with tax liabilities that exist in the present, and government actions with respect to those liabilities."). (emphasis added)

¹⁷¹ European Union's response to Panel question No. 6, para. 7.

¹⁷² See para. 7.41 above.

or in the case of processors for hire, equal to the gross income of the business, multiplied by the rate of:

(i) 0.4235 percent from October 1, 2005, through June 30, 2007; and

(ii) 0.2904 percent beginning July 1, 2007.

(b) Beginning July 1, 2008, upon every person who is not eligible to report under the provisions of (a) of this subsection (11) and is engaging within this state in the business of manufacturing tooling specifically designed for use in manufacturing commercial airplanes or components of such airplanes, or making sales, at retail or wholesale, of such tooling manufactured by the seller, as to such persons the amount of tax with respect to such business is, in the case of manufacturers, equal to the value of the product manufactured and the gross proceeds of sales of the product manufactured, or in the case of processors for hire, be equal to the gross income of the business, multiplied by the rate of 0.2904 percent.¹⁷³

7.4.3.1.1 First step: applicable tax treatment

7.57. Based on the available evidence, the Panel will first identify the applicable tax treatment under the B&O aerospace tax rate, including consideration of the objective reasons behind that treatment. As provided for in the relevant legislation, the B&O aerospace tax rate applies to "every person engaging within [the state of Washington] in the business of manufacturing commercial airplanes, or components of such airplanes, or making sales, at retail or wholesale, of commercial airplanes or components of such airplanes, manufactured by the seller".¹⁷⁴ The B&O aerospace tax rate also applies to those persons "engaging within [the state of Washington] in the business of manufacturing tooling specifically designed for use in manufacturing commercial airplanes or components of such airplanes, or making sales, at retail or wholesale, of such tooling manufactured by the seller".¹⁷⁵

7.58. Thus, the B&O aerospace tax rate applies to the following activities within the state of Washington: (i) the *manufacture* of commercial airplanes (and components thereof); (ii) *sales* of commercial airplanes (and components thereof) by such manufacturers; and (iii) the manufacture and sales of *tooling* for use in manufacturing commercial airplanes or components of such airplanes.

7.59. The B&O aerospace tax rate is a specific rate of taxation applicable to these activities. For the manufacture and sales of commercial airplanes and components thereof, this specific rate was implemented in two stages: first, a rate of 0.4235% from 1 October 2005 through 30 June 2007; and second, a rate of 0.2904% beginning 1 July 2007.¹⁷⁶ For the manufacture and sales of tooling for use in manufacturing commercial airplanes or components of such airplanes, the applicable rate as of 1 July 2008 is 0.2904%. As a result of the enactment of ESSB 5952, the B&O aerospace tax rate expires on 1 July 2040.¹⁷⁷

7.60. Thus, the relevant tax treatment at present and until the expiration of the B&O aerospace tax rate in 2040 is the tax rate of 0.2904%. This rate is multiplied by, "in the case of manufacturers ... the value of the product manufactured and the gross proceeds of sales of the product manufactured, or in the case of processors for hire ... the gross income of the business".¹⁷⁸

¹⁷³ RCW Section 82.04.260(11) (Exhibit EU-22).

¹⁷⁴ RCW Section 82.04.260(11)(a) (Exhibit EU-22). Under Washington State law, the term "commercial airplane" "has its ordinary meaning, which is an airplane certified by the federal aviation administration for transporting persons or property, and any military derivative of such an airplane". RCW Section 82.32.550(1) (Exhibit EU-82). Further, the term "component" "means a part or system certified by the federal aviation administration for installation or assembly into a commercial airplane". RCW Section 82.32.550(2) (Exhibit EU-82).

¹⁷⁵ RCW Section 82.04.260(11)(b) (Exhibit EU-22).

¹⁷⁶ ESSB 5952 (Exhibit EU-3), Sections 5-6; RCW 82.04.260(11)(a) (Exhibit EU-22).

¹⁷⁷ ESSB 5952 (Exhibit EU-3), Sections 5-6.

¹⁷⁸ RCW Section 82.04.260(11) (Exhibit EU-22).

7.61. With regard to the "objective reasons" behind this tax treatment¹⁷⁹, the Panel notes that the underlying legislation itself repeatedly refers to tax "incentives" and "preferences" to encourage the aerospace industry (as such) to remain in Washington State and to expand its presence there. For instance, ESSB 5952 is entitled "Aerospace Industry – *Tax Preferences* – Tax Exemption".¹⁸⁰ The published Session Laws of Washington State containing ESSB 5952 characterize the act as "[r]elating to *incentivizing* a long term commitment to maintain and grow jobs in the aerospace industry in Washington state by extending the expiration date of aerospace *tax preferences*".¹⁸¹

7.62. In the text of the legislation itself, the Washington State legislature explicitly set out the reasons for enacting the aerospace tax measures in ESSB 5952:

The legislature finds that the people of Washington have benefited enormously from the presence of the aerospace industry in Washington state. The legislature further finds that the industry continues to provide good wages and benefits for the thousands of engineers, mechanics, and support staff working directly in the industry throughout the state. The legislature further finds that suppliers and vendors that support the aerospace industry in turn provide a range of well-paying jobs. In 2003, and again in 2006, and 2007, the legislature determined it was in the public interest to encourage the continued presence of the aerospace industry through the provision of tax incentives. To this end, and in recognition of the continuing extreme importance of the aerospace industry in Washington, it is the legislature's intent to reaffirm and build upon prior aerospace tax incentive legislation in a fiscally prudent manner.

...

It is the legislature's specific public policy objective to maintain and grow Washington's aerospace industry workforce. To help achieve this public policy objective, it is the legislature's intent to conditionally extend aerospace industry tax preferences until July 1, 2040, in recognition of intent by the state's aerospace industry sector to maintain and grow its workforce within the state.¹⁸²

7.63. These references make clear that the purpose of the legislation is to provide favourable tax treatment for the aerospace industry, in order to encourage the industry to remain in Washington State and to grow its workforce. As stated in the Final Bill Report of ESSB 5952, "[t]he explicitly described public policy objective of the act is to maintain and grow Washington [State]'s aerospace industry workforce."¹⁸³ This language is similar to that of the prior legislation in HB 2294. In HB 2294 the Washington State legislature "declare[d] that it is in the public interest to encourage the continued presence of [the aerospace] industry through the provision of tax incentives. The *comprehensive tax incentives* in this act address the cost of doing business in Washington state compared to locations in other states."¹⁸⁴ The mechanism for achieving the objective of encouraging the aerospace industry is, in the words of both pieces of legislation, the provision of tax "preferences", "exemptions", and "incentives".

7.4.3.1.2 Second step: benchmark for comparison

7.64. Having identified the relevant tax treatment and its objective reasons, the next step of this analysis is the identification of an appropriate "benchmark for comparison" within the Washington State tax regime to determine whether this tax treatment constitutes revenue foregone by the Washington State government that would otherwise be due. This benchmark must be ascertained with regard for "the structure of the domestic tax regime and its organizing principles".¹⁸⁵

¹⁷⁹ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 812.

¹⁸⁰ ESSB 5952 (Exhibit EU-3), p. 2. (emphasis added)

¹⁸¹ Ibid. (emphasis added)

¹⁸² ESSB 5952 (Exhibit EU-3), Section 1(1) and (3).

¹⁸³ ESSB 5952 Final Bill Report (Exhibit EU-4), p. 3.

¹⁸⁴ HB 2294 (Exhibit EU-21), Section 1. (emphasis added) See also SSB 6828 (Exhibit EU-42),

Section 1.

¹⁸⁵ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 813.

7.65. The European Union submits that the benchmarks for comparison are the "general B&O tax rate for manufacturing and wholesaling activities" of 0.484% and that of 0.471% otherwise applicable to retailing.¹⁸⁶ The United States generally contends that the European Union has not met its burden to identify the benchmark for each aerospace tax measure. With specific respect to the B&O aerospace tax rate, the United States submits that Washington State's unique B&O tax system results in a pyramiding effect and thus "the industry in which a taxpayer sits may impact whether it is comparably situated to a taxpayer in the aerospace industry".¹⁸⁷ The United States also submits that "there is no question that Boeing's 777X program would have qualified for the 0.2904 percent B&O tax rate established under HB 2294 through 2024 if Washington had not enacted ESSB 5952", and contends on this basis that "[Boeing's] eligibility for that rate during the 2014-2024 does not represent revenue foregone".¹⁸⁸

7.66. As a threshold matter, the Panel notes that the parties' arguments on the benchmark for examining the B&O aerospace tax rate relate specifically to the B&O tax regime, as distinguished from other types of taxation that exist in Washington State. Given that the B&O tax is the primary business tax in Washington State, and noting the parties' argumentation based on particular features of that regime, the Panel frames its assessment of "legitimately comparable" tax situations in the light of the specific structure and organizing principles of the B&O tax regime.

7.67. The Washington State B&O tax is imposed "for the act or privilege of engaging in business activities" and "is measured by the application of rates against the value of products, gross proceeds of sales, or gross income of the business, as the case may be".¹⁸⁹ In general, the B&O tax rate varies by activity, according to the following "major B&O tax classifications": (i) manufacturing; (ii) wholesaling; (iii) retailing; and (iv) services and other activities.¹⁹⁰

7.68. Because the B&O aerospace tax rate applies to manufacturing, wholesaling, and retailing activities for commercial airplanes (as well as their components and tooling), these are the B&O tax classifications that are pertinent to the benchmark for comparison. The provisions of Washington State law governing these three categories of B&O tax are set out below:

Manufacturing: *Upon every person* engaging within this state in business as a manufacturer, *except* persons taxable as manufacturers under other provisions of this chapter; as to such persons the amount of the tax with respect to such business shall be equal to the value of the products, including byproducts, manufactured, multiplied by the rate of 0.484 percent.¹⁹¹ (emphasis added)

Wholesale: *Upon every person* engaging within this state in the business of making sales at wholesale, *except* persons taxable as wholesalers under other provisions of this chapter; as to such persons the amount of tax with respect to such business shall be equal to the gross proceeds of sales of such business multiplied by the rate of 0.484 percent.¹⁹² (emphasis added)

¹⁸⁶ See European Union's response to Panel question No. 24, para. 48; first written submission, paras. 17-21, 59.

¹⁸⁷ United States' response to Panel question No. 56, para. 20.

¹⁸⁸ United States' second written submission, para. 92.

¹⁸⁹ RCW Section 82.04.220(1) (Exhibit EU-32). See also United States' first written submission, paras. 39-41. As further explained by the Washington State Department of Revenue, "Washington, unlike many other states, does not have an income tax. Washington's B&O tax is calculated on the gross income from activities. This means there are no deductions from the B&O tax for labor, materials, taxes, or other costs of doing business." Business & Occupation Tax Explanation, Washington State Department of Revenue (Exhibit EU-33). See also ESSB 5952 Final Bill Report (Exhibit EU-4), p. 1.

¹⁹⁰ Question: What are the major B&O tax classifications?, Washington State Department of Revenue (Exhibit USA-11); United States' first written submission, para. 41.

¹⁹¹ RCW Section 82.04.240 (Exhibit EU-36). Further, the "value of products, including by-products, extracted or manufactured shall be determined by the gross proceeds derived from the sale thereof whether such sale is at wholesale or at retail". RCW Section 82.04.450(1) (Exhibit EU-37).

¹⁹² RCW Section 82.04.270 (Exhibit EU-39). Further, the "[g]ross proceeds of sales" means the value proceeding or accruing from the sale of tangible personal property, digital goods, digital codes, digital automated services, and/or for other services rendered, without any deduction on account of the cost of property sold, the cost of materials used, labor costs, interest, discount paid, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses." RCW Section 82.04.070 (Exhibit EU-40).

Retail: Upon every person engaging within this state in the business of making sales at retail, *except* persons taxable as retailers under other provisions of this chapter, as to such persons, the amount of tax with respect to such business is equal to the gross proceeds of sales of the business, multiplied by the rate of 0.471 percent.¹⁹³ (emphasis added)

7.69. The Panel considers that these general rates, as set out in these provisions and identified by the European Union, properly serve as the "normative benchmark"¹⁹⁴ for comparison within the Washington State B&O tax system. The express wording of the relevant statutes contemplates a general rate of B&O taxation applicable to "every person" engaging in the relevant activity, "except" where such persons are taxable "under other provisions" of the same chapter.

7.70. Moreover, other documents produced by Washington State addressing the B&O aerospace tax rate support the understanding that, in the absence of an explicit provision for a different tax treatment, B&O taxation would generally operate according to these major activity classifications and the corresponding rates of taxation. The Final Bill Report to ESSB 5952 describes the B&O tax and explains that "[m]ajor tax rates are 0.471 per cent for *retailing*; 0.484 per cent for *manufacturing, wholesaling*, and extracting; and 1.5 per cent for services, and activities not classified elsewhere".¹⁹⁵ The Department of Revenue Fiscal Note in relation to ESSB 5952 provides a "narrative explanation" of the measures having a fiscal impact, which refers to "[r]educed business and occupation (B&O) tax rates of 0.2904% for manufacturers of commercial airplanes (instead of the *general manufacturing rate* of 0.484%)".¹⁹⁶ Further, the Washington State Administrative Code refers to the RCW Section containing the B&O aerospace tax rate as "provid[ing] several *special B&O tax rates/classifications* for manufacturers engaging in certain manufacturing activities".¹⁹⁷ Finally, a 2016 Tax Exemption Study by the Washington State Department of Revenue characterizes the B&O aerospace tax rate as a "preferential rate".¹⁹⁸

7.71. The Panel notes the United States' description of the B&O tax as a "pyramiding tax". According to the United States:

[G]oods and services are taxed multiple times as they move through the production chain, with a successively greater effective tax rate for each business in the chain. As a result, industries with multiple steps, such as the aerospace industry, have higher effective tax rates. In part to address this "pyramiding", Washington has introduced a number of industry-specific B&O tax rates.¹⁹⁹

7.72. The Panel also observes that the United States further suggests that because "Washington's unique B&O tax system results in a pyramiding effect", "the industry in which a taxpayer sits may impact whether it is comparably situated to a taxpayer in the aerospace industry".²⁰⁰

7.73. Arguments related to the "pyramiding" effect of the B&O tax were examined previously by the panel and the Appellate Body in *US – Large Civil Aircraft (2nd complaint)* in relation to similar (though subsequently amended and extended) measures under HB 2294. Reviewing arguments on average effective tax rates based on the panel record in that dispute, the Appellate Body saw "no indication ... that adjusting tax rates to approximate the average effective tax rate reflects a principle under the Washington State B&O tax regime. Rather, it appears to be more in the nature of an *ex post* explanation regarding the relationship of these rates to one another."²⁰¹ The Appellate Body further considered that the panel record in that dispute did "not support the

¹⁹³ RCW Section 82.04.250 (Exhibit EU-38).

¹⁹⁴ See Appellate Body Report, *US – FSC*, para. 90.

¹⁹⁵ ESSB 5952 Final Bill Report (Exhibit EU-4), p. 1. (emphasis added)

¹⁹⁶ ESSB 5952 Fiscal Note (Exhibit EU-5), p. 2. (emphasis added)

¹⁹⁷ WAC Section 458-20-136(5) (Exhibit USA-41).

¹⁹⁸ 2016 Tax Exemption Study, Washington State Department of Revenue (Exhibit EU-95), Appendix B, p. B-1.

¹⁹⁹ United States' first written submission, para. 41 (citing Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.98).

²⁰⁰ United States' Response to Panel question No. 56, para. 20.

²⁰¹ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 829.

contention that Washington State implemented House Bill 2294 alone, or as part of a broader regulatory scheme, to counteract the effects of pyramiding".²⁰²

7.74. In the present dispute, the evidence before the Panel demonstrates that the B&O tax system is organized based on major activity classifications with statutorily prescribed rates of taxation corresponding to each activity. Within the framework of those major activity classifications, the B&O tax system contemplates different rates of taxation for certain businesses.²⁰³ The B&O aerospace tax rate itself is one such case, as it is explicitly framed according to these major activity classifications (i.e. manufacturing, wholesaling, and retailing), and for such aerospace activities it establishes a specific B&O tax rate due to policy reasons tied to the maintenance and growth of Washington State's aerospace industry workforce.²⁰⁴

7.75. In this context, the counteraction of higher effective tax rates from "pyramiding" due to multiple business activities does not appear to amount to an "organizing principle" of the domestic tax regime in question. Other features of the B&O tax system may reflect a concern for preventing double B&O taxation, namely the provision for a Multiple Activities Tax Credit for persons taxable under the B&O tax on making retail and wholesale sales of the items they manufacture, such that taxes paid on manufacturing of products sold in Washington State can be credited against retailing or wholesaling B&O tax liability on the items manufactured.²⁰⁵ However, this feature of the B&O tax system reinforces an understanding of the B&O tax structure built on core activity classifications of manufacturing, wholesaling, and retailing for the purposes of identifying comparably situated taxpayers in Washington State.²⁰⁶ It is these activity classifications, rather than the effective tax rates of specific industries or sectors, that appear to form the "organizing principle" underlying the B&O tax system.

7.76. Finally, the Panel is not persuaded that any possible qualification for pre-existing tax incentives, in particular those established under HB 2294, is relevant to establishing the benchmark in this case. The fact that the applicable tax treatment may have been available previously by virtue of earlier measures does not automatically render that tax treatment its own normative benchmark, particularly as the earlier application of the tax treatment in question may itself be a departure from the organizing principles of the domestic tax regime. The United States has not articulated why a B&O aerospace tax rate of 0.2904% should be understood as a "defined, normative benchmark" reflective of "organizing principles" of the B&O tax regime. The assertion that "[Boeing's] eligibility for that rate during the [period] 2014-2024 does not represent revenue foregone"²⁰⁷ would seem to apply a strict "but for" test, without accounting for the organizing principles of the B&O tax regime described above. Such an approach could amount to "identifying a benchmark solely by reference to historical rates"²⁰⁸, contrary to the reservations expressed by the Appellate Body²⁰⁹ as to the identification of a benchmark without proper regard for the complexities of a Member's domestic rules of taxation.²¹⁰ In this case, the benchmark for comparison is not determined simply by historical tax treatment, but rather is based on the government revenue that would be otherwise due from comparably situated taxpayers in light of the structure and organizing principles of the Washington State B&O tax regime.

7.77. On the basis of the evidence and arguments on the record, the Panel considers that taxpayers in Washington State engaged in the major business activities of manufacturing, wholesaling, and retailing are comparably situated to their counterparts in the aerospace industry engaged in such activities, as "every" taxpayer in the state engaged in those activities is subject to

²⁰² Ibid. para. 830.

²⁰³ For example, the RCW provisions codifying the B&O aerospace tax rate include special B&O tax rates for other businesses, including *inter alia* the manufacturing of seafood and dairy products, as well as the manufacturing and wholesaling of "fruits or vegetables by canning, preserving, freezing, processing, or dehydrating fresh fruits or vegetables". See RCW Section 82.04.260(1) (Exhibit EU-22).

²⁰⁴ ESSB 5952 (Exhibit EU-3), Section 1(3).

²⁰⁵ RCW Section 82.04.440(4) (Exhibit USA-31). See also WAC Section 458-20-19301(3) (Exhibit EU-41) (explaining that "[t]his integrated tax credits system is intended to assure that gross receipts from sales or the value of products determined by such gross receipts are taxed only one time, whether the activities occur entirely within this state or both within and outside this state").

²⁰⁶ See Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 813.

²⁰⁷ United States' second written submission, para. 92.

²⁰⁸ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 815.

²⁰⁹ Appellate Body Report, *US – FSC*, para. 91.

²¹⁰ Appellate Body Report, *US – FSC (Article 21.5 – EC)*, fn 66.

the B&O tax. Accordingly, the appropriate normative benchmarks with regard to the B&O aerospace tax rate are the general B&O tax rates of 0.484% for manufacturing and wholesaling activities, and 0.471% for retailing activities.

7.4.3.1.3 Third step: comparison of applicable tax treatment with benchmark

7.78. Having established the relevant tax treatment provided to alleged beneficiaries of the B&O aerospace tax rate, as well as the reasons for that treatment, the Panel turns to the comparison of the B&O aerospace tax rate with the identified benchmarks.

7.79. For taxpayers engaged in the business of manufacturing commercial airplanes, or manufacturing components of such airplanes, the B&O aerospace tax rate provides for a B&O tax rate of 0.2904%. This is to be compared with the taxation of comparably situated taxpayers, namely the B&O tax rate of 0.484% generally applicable to other entities engaged in manufacturing activities in Washington State. Pursuant to the Washington State tax code, as amended by ESSB 5952, the rate applicable to manufacturing commercial airplanes (or components of such airplanes) is lower than that generally applied to other manufacturing activities. There is no evidence that this difference is reflective of any organizing principle of the B&O tax system. Rather, the difference is for the express reason of incentivizing the maintenance and growth of Washington State's aerospace industry. For these reasons, the Panel finds that the Washington State government is foregoing revenue that is otherwise due in relation to manufacturing beneficiaries of the B&O aerospace tax rate.

7.80. For taxpayers engaged in the business of making sales at wholesale of commercial airplanes, or making sales at wholesale of components of such airplanes, the B&O aerospace tax rate provides for a B&O tax rate of 0.2904%. This is to be compared with the taxation of comparably situated taxpayers, namely the B&O tax rate of 0.484% generally applicable to other entities engaged in wholesaling activities in Washington State. Pursuant to the Washington State tax code, as amended by ESSB 5952, the rate applicable to wholesale sales of commercial airplanes (or components of such airplanes) is lower than that generally applied to wholesaling activities. There is no evidence that this difference is reflective of any organizing principle of the B&O tax system. Rather, the difference is for the express reason of incentivizing the maintenance and growth of Washington State's aerospace industry. For these reasons, the Panel finds that the Washington State government is foregoing revenue that is otherwise due in relation to wholesaling beneficiaries of the B&O aerospace tax rate.

7.81. For taxpayers engaged in the business of making sales at retail of commercial airplanes, or making sales at retail of components of such airplanes, the B&O aerospace tax rate provides for a B&O tax rate of 0.2904%. This is to be compared with the taxation of comparably situated taxpayers, namely the B&O tax rate of 0.471% generally applicable to other entities engaged in retailing activities in Washington State. Pursuant to the Washington State tax code, as amended by ESSB 5952, the rate applicable to retail sales of commercial airplanes (or components of such airplanes) is lower than that generally applied to retailing activities. There is no evidence that this difference is reflective of any organizing principle of the B&O tax system. Rather, the difference is for the express reason of incentivizing the maintenance and growth of Washington State's aerospace industry. For these reasons, the Panel finds that the Washington State government is foregoing revenue that is otherwise due in relation to retailing beneficiaries of the B&O aerospace tax rate.

7.82. Finally, for taxpayers engaged in the manufacture and sales, at both wholesale and retail levels, of *tooling* for use in manufacturing commercial airplanes or components of such airplanes, the B&O aerospace tax rate provides for a B&O tax rate of 0.2904%. This is to be compared with the taxation of comparably situated taxpayers, namely the B&O tax rate of 0.484% generally applicable to other entities engaged in manufacturing and wholesaling activities in Washington State, and the B&O tax rate of 0.471% generally applicable to other entities engaged in retailing activities in Washington State. Pursuant to the Washington State tax code, as amended by ESSB 5952, the rate applicable to manufacturing, wholesaling, and retailing of tooling for use in manufacturing commercial airplanes (or components of such airplanes) is lower than that generally applied to such activities. There is no evidence that this difference is reflective of any organizing principle of the B&O tax system. Rather, the difference is for the express reason of incentivizing the maintenance and growth of Washington State's aerospace industry. For these reasons, the Panel finds that the Washington State government is foregoing revenue that is otherwise due in

relation to tooling beneficiaries (manufacturers, wholesalers, and retailers) of the B&O aerospace tax rate.

7.83. Accordingly, the Panel finds that the B&O aerospace tax rate, in respect of all of the types of activities that it covers, constitutes a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement.

7.4.3.2 B&O tax credit for aerospace product development

7.84. The legislation for the B&O tax credit for aerospace product development provides in relevant part:

(1)(a)(i) In computing the tax imposed under this chapter [the B&O tax], a credit is allowed for each person for qualified aerospace product development. For a person who is a manufacturer or processor for hire of commercial airplanes or components of such airplanes, credit may be earned for expenditures occurring after December 1, 2003. For all other persons, credit may be earned only for expenditures occurring after June 30, 2008.

...

(2) The credit is equal to the amount of qualified aerospace product development expenditures of a person, multiplied by the rate of 1.5 percent.

...

(5) The definitions in this subsection apply throughout this section.

...

(b) "Aerospace product development" means research, design, and engineering activities performed in relation to the development of an aerospace product or of a product line, model, or model derivative of an aerospace product, including prototype development, testing, and certification. ...

(c) "Qualified aerospace product development" means aerospace product development performed within this state.

(d) "Qualified aerospace product development expenditures" means operating expenses, including wages, compensation of a proprietor or a partner in a partnership as determined by the department, benefits, supplies, and computer expenses, directly incurred in qualified aerospace product development by a person claiming the credit provided in this section. ...²¹¹

7.4.3.2.1 First step: applicable tax treatment

7.85. Based on the available evidence, the Panel will first identify the applicable tax treatment under the B&O tax credit for aerospace product development, including consideration of the objective reasons behind that treatment. As provided for in the relevant legislation, Washington State provides a credit against B&O tax liability "equal to the amount of qualified aerospace product development expenditures of a person, multiplied by the rate of 1.5 per cent".²¹² The term "aerospace product development" is defined to include "research, design, and engineering activities performed in relation to the development of an aerospace product or of a product line, model, or model derivative of an aerospace product, including prototype development, testing, and certification".²¹³ In turn, the term "aerospace product" is defined under Washington State law as: "(i) Commercial airplanes and their components; (ii) Machinery and equipment that is designed and used primarily for the maintenance, repair, overhaul, or

²¹¹ RCW Section 82.04.4461 (Exhibit EU-23).

²¹² RCW Section 82.04.4461(2) (Exhibit EU-23).

²¹³ RCW Section 82.04.4461(5)(b) (Exhibit EU-23).

refurbishing of commercial airplanes or their components".²¹⁴ Such "aerospace product development" is only "qualified" – i.e. it only counts towards the tax credit – if it occurs in Washington State²¹⁵, and the relevant expenditures for such development against which the credit is calculated include a variety of "operating expenses" specified in the relevant statute that are "directly incurred in qualified aerospace product development by a person claiming the credit provided in this section".²¹⁶

7.86. Thus, the tax treatment at issue is a credit applied against a taxpayer's B&O tax liability, calculated as 1.5% of expenditures on the development of commercial airplanes and their components, as well as machinery and equipment used in relation to commercial airplanes and their components. As a result of the enactment of ESSB 5952, the B&O tax credit for aerospace product development expires on 1 July 2040.²¹⁷ Thus, the relevant tax treatment for the covered activities, at present and until the 2040 expiry date, is as set forth above.

7.87. This tax treatment forms part of the legislation in ESSB 5952 targeted towards the aerospace industry in Washington State. Its "objective reasons" are the same as discussed in respect of the B&O aerospace tax rate – that is, to provide favourable tax treatment for the aerospace industry in order to encourage the industry to remain in Washington State and to grow its workforce.²¹⁸

7.4.3.2.2 Second step: benchmark for comparison

7.88. Having identified the relevant tax treatment and its objective reasons, the next step of the analysis is the identification of an appropriate "benchmark for comparison" within the Washington State tax regime to determine whether this tax treatment constitutes revenue foregone by the Washington State government that would otherwise be due. This benchmark must be ascertained with regard for "the structure of the domestic tax regime and its organizing principles".²¹⁹

7.89. With regard to the "benchmark for comparison", the European Union submits that the B&O tax credit for aerospace product development reduces the amount of B&O tax liability by the value of the credit, and that "the standard tax treatment of manufacturers, unabated by such tax credits, serves as the normative benchmark".²²⁰ The United States, in addition to its general argument that the European Union has not met its burden to identify the benchmark for each aerospace tax measure, also submits, in respect of tax credits, that the comparable taxable "event" is not an event involving the same taxpayers absent the credit, as this would be the "type of historical comparison for a taxpayer [that] was criticized by the Appellate Body".²²¹

7.90. The Panel considers that, as with the B&O aerospace tax rate, the B&O tax regime (rather than other types of taxation that exist in Washington State) constitutes the part of the Washington State tax regime that is relevant to the appropriate benchmark for the B&O tax credit for aerospace product development. Unlike the B&O aerospace tax rate, the B&O tax credit for aerospace product development does not alter the rate of taxation applicable to a given taxpayer, but rather provides for an amount to be credited or offset against that taxpayer's B&O tax liability. As discussed above, the organizing principles of the B&O tax regime involve the establishment of

²¹⁴ RCW Section 82.08.975(3)(a) (Exhibit EU-25). Under Washington State law, the term "commercial airplane" "has its ordinary meaning, which is an airplane certified by the federal aviation administration for transporting persons or property, and any military derivative of such an airplane". RCW Section 82.32.550(1) (Exhibit EU-82). Further, the term "component" "means a part or system certified by the federal aviation administration for installation or assembly into a commercial airplane". RCW Section 82.32.550(2) (Exhibit EU-82).

²¹⁵ RCW Section 82.04.4461(5)(b) (Exhibit EU-23). United States' first written submission, para. 60.

²¹⁶ RCW Section 82.04.4461(5)(d) (Exhibit EU-23).

²¹⁷ ESSB 5952 (Exhibit EU-3), Section 9.

²¹⁸ See para. 7.65 above.

²¹⁹ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 813.

²²⁰ See European Union's response to Panel question No. 24, para. 48; first written submission, paras. 22-24, 62-63.

²²¹ The United States' response to Panel question No. 57, para. 23 (citing Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 815).

generally applicable rates of taxation according to major activity classifications, across a range of different industries and sectors.²²²

7.91. Based on the evidence on record, the Panel does not consider it to be an "organizing principle" of the B&O tax regime to provide industry-specific credits for designated activities to offset a portion of the tax liability arising from the pertinent B&O tax rates. A taxpayer is normally subject to generally applicable B&O tax rates based on the type of business activity conducted (e.g. manufacturing, wholesaling, or retailing). The taxpayer's B&O tax liability would be calculated by multiplying the applicable tax rate by the taxable amount generated by the business activity.²²³ The "gross" B&O tax liability thus calculated would be the benchmark against which to compare the taxpayer's B&O tax liability net of the amount of the credit. The fact that in every case of such comparison the taxpayer in question is the same does not change this conclusion, because the organizing principle is not that credits are made available, but rather that taxpayers, by virtue of the generally applicable rates of taxation according to major activity classifications, would otherwise expect to have to pay the tax that is being credited. Indeed, given that the form of the measure is a credit, or offset, against a taxpayer's gross B&O tax liability, the Panel considers this approach to identifying the benchmark for a measure of this nature as most reasonable.

7.92. The Panel therefore agrees with the European Union that the relevant normative benchmark is the B&O tax liability that would apply to a given taxpayer in the absence of the credit.

7.4.3.2.3 Third step: comparison of applicable tax treatment with benchmark

7.93. Having established the relevant tax treatment provided to alleged beneficiaries of the B&O tax credit for aerospace product development, as well as the reasons for that treatment, the Panel turns to the comparison of the B&O tax credit for aerospace product development with the identified benchmark.

7.94. As described above, taxpayers engaged in activities subject to B&O taxation in Washington State are subject to B&O tax rates corresponding to the major activity classifications. It is by virtue of the additional provision for a B&O tax credit tied to aerospace product development that this tax liability can be reduced for eligible taxpayers by the amount of the credit. As noted above, this credit is provided within the framework of legislation enacted for the express reason of incentivizing the maintenance and growth of employment in Washington State's aerospace industry.

7.95. In this regard, the Panel is mindful of the Appellate Body's reservation that "an approach that focuses too narrowly on the change effected by a tax measure could result in a finding that government revenue otherwise due is foregone anytime the tax rate applicable to a recipient is lowered."²²⁴ The Appellate Body underscored "the risk in identifying a benchmark solely by reference to historical rates, the very departure from which may reflect evidence of shifting norms within that regime".²²⁵ This is the issue raised by the United States referred to above.²²⁶

7.96. Taking into account the Appellate Body's guidance, the Panel's analysis does not concern "what *previously* applied to commercial aircraft manufacturing activities", but rather "what would *currently* apply to these activities if the conditions for" the tax credit were not met.²²⁷ The Panel has taken into account the structure of the B&O tax system and the reasons for the specific tax treatment at issue. Moreover, the Panel does not consider, nor did the United States provide evidence or argumentation to suggest, that the provision of this tax credit reflects "evidence of shifting norms within" the B&O tax regime.²²⁸ The Panel notes that the measure in question is a

²²² See also Tax Classifications for Common Business Activities, Washington State Department of Revenue (Exhibit EU-62).

²²³ More specifically, the B&O tax liability "is measured by the application of rates against the value of products, gross proceeds of sales, or gross income of the business, as the case may be". RCW Section 82.04.220(1) (Exhibit EU-32).

²²⁴ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 815.

²²⁵ *Ibid.*

²²⁶ See United States' response to Panel question No. 57.

²²⁷ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 823. (emphasis original) See also European Union's comments on the United States' response to Panel question No. 57, para. 15.

²²⁸ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 815. See also United States' response to Panel question No. 57.

tax credit, and thus does not change the applicable tax rates, but rather offsets B&O tax liability that would otherwise be due in the absence of the credit.

7.97. Based on these considerations, the Panel finds that the B&O tax credit for aerospace product development results in the foregoing of government revenue by Washington State with respect to the B&O tax liability that would otherwise be presently incurred by the taxpayers eligible for the credit. In this regard, the Panel considers the illustrative reference in Article 1.1(a)(1)(ii) to "fiscal incentives such as tax credits" to be apposite to the circumstances of the B&O tax credit for aerospace product development as presented to the Panel.

7.98. Accordingly, the Panel finds that the B&O tax credit for aerospace product development constitutes a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement.

7.4.3.3 B&O tax credit for property and leasehold excise taxes

7.99. The legislation for the B&O tax credit for property and leasehold excise taxes provides in relevant part:

(1) In computing the tax imposed under this chapter [the B&O tax], a credit is allowed for property taxes and leasehold excise taxes paid during the calendar year.

(2) The credit is equal to:

(a)(i)(A) Property taxes paid on buildings, and land upon which the buildings are located, constructed after December 1, 2003, and used exclusively in manufacturing commercial airplanes or components of such airplanes; and

(B) Leasehold excise taxes paid with respect to buildings constructed after January 1, 2006, the land upon which the buildings are located, or both, if the buildings are used exclusively in manufacturing commercial airplanes or components of such airplanes; and

(C) Property taxes or leasehold excise taxes paid on, or with respect to, buildings constructed after June 30, 2008, the land upon which the buildings are located, or both, and used exclusively for aerospace product development, manufacturing tooling specifically designed for use in manufacturing commercial airplanes or their components, or in providing aerospace services ... ; or

(ii) Property taxes attributable to an increase in assessed value due to the renovation or expansion, after: (A) December 1, 2003, of a building used exclusively in manufacturing commercial airplanes or components of such airplanes; and (B) June 30, 2008, of buildings used exclusively for aerospace product development, manufacturing tooling specifically designed for use in manufacturing commercial airplanes or their components, or in providing aerospace services, ... ²²⁹

7.4.3.3.1 First step: applicable tax treatment

7.100. Based on the available evidence, the Panel will first identify the applicable tax treatment under the B&O tax credit for property and leasehold excise taxes, including consideration of the objective reasons behind that treatment. As provided for in the relevant legislation, Washington State provides a credit against B&O tax liability "for property taxes and leasehold excise taxes paid during the calendar year".²³⁰ The tax credit applies to property and leasehold excise taxes related to buildings, and/or land upon which the buildings are located, that are: "used

²²⁹ RCW Section 82.04.4463 (Exhibit EU-24). The B&O tax credit for property and leasehold excise taxes contains further provisions on the calculation of the credit for property taxes paid on certain machinery and equipment, as well as certain computer hardware, computer peripherals, and software. See RCW Section 82.04.4463(2)(b) (Exhibit EU-24).

²³⁰ RCW Section 82.04.4463(1) (Exhibit EU-24).

exclusively in manufacturing commercial airplanes or components of such airplanes"²³¹; and "used exclusively for aerospace product development, manufacturing tooling specifically designed for use in manufacturing commercial airplanes or their components, or in providing aerospace services".²³² In addition, this B&O tax credit applies to property taxes "attributable to an increase in assessed value due to renovation or expansion" of such buildings.²³³ As a result of the enactment of ESSB 5952, the B&O tax credit for property and leasehold excise taxes expires on 1 July 2040.²³⁴ Thus, the relevant tax treatment, at present and until the 2040 expiry date, is as set forth above.

7.101. The United States explains that the B&O tax credit for property and leasehold excise taxes enables a taxpayer to claim a credit that is measured according to property taxes and leasehold excise taxes²³⁵ "due on certain types of property with certain types of uses related to commercial airplane, airplane components, aerospace services, and aerospace product development".²³⁶ The tax credit provided for under this aerospace tax measure "offsets the B&O tax that is due in a given year".²³⁷

7.102. This tax treatment forms part of the legislation in ESSB 5952 targeted towards the aerospace industry in Washington State. As such, its "objective reasons" are the same as discussed in respect of the B&O aerospace tax rate – that is, to provide favourable tax treatment for the aerospace industry in order to encourage the industry to remain in Washington State and to grow its workforce.²³⁸

7.4.3.3.2 Second step: benchmark for comparison

7.103. Having identified the relevant tax treatment and its objective reasons, the next step of the analysis is the identification of an appropriate "benchmark for comparison" within the Washington State tax regime to determine whether this tax treatment constitutes revenue foregone by the Washington State government that would otherwise be due. This benchmark must be ascertained with regard for "the structure of the domestic tax regime and its organizing principles".²³⁹

7.104. With regard to the "benchmark for comparison", the European Union submits that the B&O tax credit for property and leasehold excise taxes reduces the amount of B&O tax liability by the value of the credit, and that "the standard tax treatment of manufacturers, unabated by such tax credits, serves as the normative benchmark".²⁴⁰ The United States, in addition to its general argument that the European Union has not met its burden to identify the benchmark for each aerospace tax measure, also submits, in respect of tax credits, that the comparable taxable "event" is not an event involving the same taxpayers absent the credit, as this would be the "type of historical comparison for a taxpayer [that] was criticized by the Appellate Body".²⁴¹

7.105. The Panel considers that, as with the other B&O-related tax measures, the B&O tax regime constitutes the part of the Washington State tax regime that is relevant to the appropriate benchmark for the B&O tax credit for property and leasehold excise taxes. Like the B&O tax credit for aerospace product development, the B&O tax credit for property and leasehold excise taxes does not alter the rate of taxation but rather provides for an amount to be credited against a taxpayer's B&O tax liability. As discussed above, the organizing principles of the B&O tax regime

²³¹ RCW Section 82.04.4463(2)(a)(i)(A) and (B) (Exhibit EU-24). Under Washington State law, the term "commercial airplane" "has its ordinary meaning, which is an airplane certified by the federal aviation administration for transporting persons or property, and any military derivative of such an airplane". RCW Section 82.32.550(1) (Exhibit EU-82). Further, the term "component" "means a part or system certified by the federal aviation administration for installation or assembly into a commercial airplane". RCW Section 82.32.550(2) (Exhibit EU-82).

²³² RCW Section 82.04.4463(2)(a)(i)(C) (Exhibit EU-24).

²³³ RCW Section 82.04.4463(2)(a)(ii) (Exhibit EU-24).

²³⁴ ESSB 5952 (Exhibit EU-3), Section 10.

²³⁵ See description of these taxes in paras. 7.25-7.26 above.

²³⁶ United States' response to Panel question No. 9, para. 18.

²³⁷ Ibid.

²³⁸ See para. 7.65 above.

²³⁹ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 813.

²⁴⁰ See European Union's response to Panel question No. 24, para. 48; first written submission, paras. 22-24, 62-63.

²⁴¹ The United States' response to Panel question No. 57, para. 23 (citing Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 815).

involve the establishment of generally applicable rates of taxation according to major activity classifications, across a range of different industries and sectors.²⁴²

7.106. As also discussed above, and based on the evidence on record, the Panel does not consider it to be an "organizing principle" of the B&O tax regime to provide industry-specific credits for designated activities to offset a portion of the tax liability arising from the pertinent B&O tax rates. The Panel follows the same approach for the B&O tax credit for property and leasehold excise taxes, for the same reasons, as that taken in respect of the B&O tax credit for aerospace product development. The Panel therefore agrees with the European Union that the relevant normative benchmark is the B&O tax liability that would apply in the absence of the credit.

7.4.3.3.3 Third step: comparison of applicable tax treatment with benchmark

7.107. The comparison for the B&O tax credit for property and leasehold excise taxes follows the same reasoning as that set out above for the B&O tax credit for aerospace product development. Thus, taxpayers engaged in activities subject to B&O taxation in Washington State are subject to B&O tax rates corresponding to the major activity classifications. It is by virtue of the additional provision for a B&O tax credit for property and leasehold excise taxes paid in respect of the designated aerospace related activities and properties that this tax liability can be reduced, for eligible taxpayers, by the amount of the credit. As noted above, this credit is provided within the framework of legislation enacted for the express reason of incentivizing the maintenance and growth of employment in Washington State's aerospace industry.

7.108. As with the B&O tax credit for aerospace product development, the Panel is mindful of the Appellate Body's reservation that "an approach that focuses too narrowly on the change effected by a tax measure could result in a finding that government revenue otherwise due is foregone anytime the tax rate applicable to a recipient is lowered."²⁴³ The Appellate Body underscored "the risk in identifying a benchmark solely by reference to historical rates, the very departure from which may reflect evidence of shifting norms within that regime".²⁴⁴

7.109. Taking into account the Appellate Body's guidance, the Panel's analysis does not concern "what *previously* applied to commercial aircraft manufacturing activities", but rather "what would *currently* apply to these activities if the conditions for" the tax credit were not met.²⁴⁵ The Panel has taken into account the structure of the B&O tax system and the reasons for the specific tax treatment at issue. Moreover, the Panel does not consider, nor did the United States provide evidence or argumentation to suggest, that the provision of this tax credit reflects "evidence of shifting norms within" the B&O tax regime.²⁴⁶ The Panel notes that the measure in question is a tax credit, and thus does not change the applicable tax rates, but rather offsets B&O tax liability that would otherwise be due in the absence of the credit.

7.110. Based on these considerations, the Panel finds that the B&O tax credit for property and leasehold excise taxes results in the foregoing of government revenue by Washington State with respect to the B&O tax liability that would otherwise be presently incurred by taxpayers eligible for the credit. In this regard, and as with the B&O tax credit for aerospace product development, the Panel considers the illustrative reference to "fiscal incentives such as tax credits" in Article 1.1(a)(1)(ii) to be apposite to the circumstances of the B&O tax credit for property and leasehold excise taxes as presented to the Panel.

7.111. Accordingly, the Panel finds that the B&O tax credit for property and leasehold excise taxes constitutes a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement.

²⁴² See also Tax Classifications for Common Business Activities, Washington State Department of Revenue (Exhibit EU-62).

²⁴³ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 815.

²⁴⁴ Ibid. See also United States' response to Panel question No. 57.

²⁴⁵ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 823. (emphasis original) See also European Union's comments on the United States' response to Panel question No. 57, para. 15.

²⁴⁶ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 815. See also United States' response to Panel question No. 57.

7.4.3.4 Computer sales and use tax exemptions

7.112. The legislation for the computer sales tax exemption provides in relevant part:

(1) The tax levied by RCW 82.08.020 [the sales tax] does not apply to sales of computer hardware, computer peripherals, or software ... used primarily in the development, design, and engineering of aerospace products or in providing aerospace services, or to sales of or charges made for labor and services rendered in respect to installing the computer hardware, computer peripherals, or software.²⁴⁷

7.113. The computer use tax exemption provides in relevant part:

(1) The provisions of this chapter [the use tax] do not apply in respect to the use of computer hardware, computer peripherals ... used primarily in the development, design, and engineering of aerospace products or in providing aerospace services, or to the use of labor and services rendered in respect to installing the computer hardware, computer peripherals, or software.²⁴⁸

7.4.3.4.1 First step: applicable tax treatment

7.114. Based on the available evidence, the Panel will first identify the applicable tax treatment under the computer sales and use tax exemptions, including consideration of the objective reasons behind that treatment. As provided for in the relevant legislation, Washington State provides an exemption from the retail sales tax²⁴⁹ for "sales of computer hardware, computer peripherals, or software ... used primarily in the development, design, and engineering of aerospace products or in providing aerospace services, or to sales of or charges made for labor and services rendered in respect to installing the computer hardware, computer peripherals, or software".²⁵⁰ Additionally, the use of these items is exempt from the Washington State's "use tax"²⁵¹, which is a tax on the use of goods or certain services in the state of Washington when sales tax has not been paid.²⁵² As a result of ESSB 5952, the computer sales and use tax exemptions expire on 1 July 2040.²⁵³ Thus, the relevant tax treatment for the covered activities and products, at present and until the 2040 expiry date, is as set forth above.

7.115. This tax treatment forms part of the legislation in ESSB 5952 targeted towards the aerospace industry in Washington State. As such, its "objective reasons" are the same as discussed in respect of the B&O aerospace tax rate – that is, to provide favourable tax treatment for the aerospace industry in order to encourage the industry to remain in Washington State and to grow its workforce.²⁵⁴

7.4.3.4.2 Second step: benchmark for comparison

7.116. Having identified the relevant tax treatment and its objective reasons, the next step of the analysis is the identification of an appropriate "benchmark for comparison" within the Washington State tax regime to determine whether this tax treatment constitutes revenue foregone by the Washington State government that would otherwise be due. This benchmark must be ascertained with regard for "the structure of the domestic tax regime and its organizing principles".²⁵⁵

²⁴⁷ RCW Section 82.08.975 (Exhibit EU-25).

²⁴⁸ RCW Section 82.12.975 (Exhibit EU-26).

²⁴⁹ RCW Section 82.08.020 (Exhibit EU-92).

²⁵⁰ RCW Section 82.08.975 (Exhibit EU-25).

²⁵¹ RCW Section 82.12.975 (Exhibit EU-26).

²⁵² Use Tax Explanation, Washington State Department of Revenue (Exhibit USA-19). For example, the use tax is owed if goods are purchased in another state that does not have a sales tax or a state with a sales tax lower than that of the state of Washington. The use tax would also be owed if good are purchased from someone who is not authorized to collect sales tax (e.g. purchases of furniture from an individual through a newspaper classified ad or a purchase of artwork from an individual collector), or if personal property is acquired with the purchase of real property.

²⁵³ ESSB 5952 (Exhibit EU-3), Sections 11-12.

²⁵⁴ See para. 7.65 above.

²⁵⁵ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 813.

7.117. With regard to the "benchmark for comparison", the European Union submits that the computer sales and use tax exemptions "exempt[] the purchase of otherwise taxable goods and services from the retail sales and use taxes", and that "the normative benchmark is the sales and use taxes that would otherwise apply absent these exemptions".²⁵⁶ The United States, in addition to its general argument that the European Union has not met its burden to identify the benchmark for each aerospace tax measure, also submits, in respect of tax exemptions, that the comparable taxable "event" is not an event involving the same taxpayers absent the exemption, as this would be the "type of historical comparison for a taxpayer [that] was criticized by the Appellate Body".²⁵⁷ The United States further submits that "quantitative coverage of various tax regimes could be relevant to determining a financial contribution compared to a normative benchmark"²⁵⁸ and that "Washington provides a large number of exemptions ... suggesting that the sales and use tax rates that are notionally (but not actually) applicable to all purchases by consumers located in Washington are not the appropriate benchmark".²⁵⁹

7.118. As a threshold matter, it is the sales and use tax regime, as distinguished from other types of taxation that exist in Washington State, in which the aerospace tax measure at issue applies and according to which the parties have advanced their arguments on the appropriate benchmark for comparison. Therefore, in order to identify the appropriate benchmark for comparison, the Panel will examine the structure of the sales and use tax regime in Washington State, particularly in respect of its organizing principles and legitimately comparable tax situations.

7.119. Washington State has a retail sales tax, which is its principal source of tax revenue.²⁶⁰ Generally, a retail sale is the sale of tangible personal property, as well as the sale of certain services (including construction services) and sales of digital products to consumers.²⁶¹ The Washington State retail sales tax rate has two components: the state component, which is equal to 6.5%, and the local component, which varies by jurisdiction.²⁶² Local governments within Washington State have the authority to set their own retail sales tax rates within their jurisdictions, but the State administers both components.²⁶³

7.120. The Washington State use tax is complementary to the retail sales tax, in that it is due on the use of goods or services to the extent that the user has not paid the Washington State retail sales tax or "a legally imposed retail sales or use tax ... to any other state, possession, territory, or commonwealth of the United States, any political subdivision thereof, the District of Columbia, and any foreign country or political subdivision thereof".²⁶⁴ Thus, goods in Washington State are subject to either sales or use tax, but not both, and the use tax compensates when the sales tax has not been paid.²⁶⁵ Use tax is determined on the value of the goods (generally the purchase price) when first used in Washington State.²⁶⁶ The use tax rate is the same as the retail sales tax rate.²⁶⁷

7.121. Both parties have noted that there are a number of exemptions from retail sales and use taxes for purchases of specific goods or services. Some of these exemptions are limited to a particular industry or sector, while other exemptions are available for any purchaser or user of the

²⁵⁶ See European Union's comments on the United States' response to Panel question No. 24, para. 50; first written submission, paras. 22-24, 62-63.

²⁵⁷ The United States' response to Panel question No. 57, para. 23 (citing Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 815).

²⁵⁸ United States' response to Panel question No. 60, para. 31.

²⁵⁹ United States' response to Panel question No. 56, para. 21.

²⁶⁰ United States' first written submission, para. 42; Retail Sales Tax Explanation, Washington State Department of Revenue (Exhibit USA-12).

²⁶¹ RCW Section 82.08.020 (Exhibit EU-92); United States' first written submission, para. 42; Retail Sales Tax Explanation, Washington State Department of Revenue (Exhibit USA-12); Services Subject to Sales Tax, Washington State Department of Revenue (Exhibit USA-13); Digital Products including Digital Goods, Washington State Department of Revenue (Exhibit USA-14).

²⁶² See Local Sales, Use Tax Rates and Changes, Washington State Department of Revenue (Exhibit USA-16).

²⁶³ United States' first written submission, para. 43.

²⁶⁴ RCW Section 82.12.020 (Exhibit USA-17); RCW Section 82.12.035 (Exhibit USA-18).

²⁶⁵ Use Tax Explanation, Washington State Department of Revenue (Exhibit USA-19).

²⁶⁶ *Ibid.*

²⁶⁷ *Ibid.*

specified good or service.²⁶⁸ The parties also have advanced arguments based on the quantitative coverage of the exemptions.²⁶⁹

7.122. The parties' arguments on the coverage and exemption of sales and use taxes are primarily based on a 2016 Tax Exemption Study by the Washington State Department of Revenue. The portions of the study submitted to the Panel include an Introduction and Summary of Findings²⁷⁰ as well as an Appendix containing a detailed list of "tax exemptions" examined in the study. The study uses the term "tax exemption" to cover "a variety of preferences that reduce tax liability for taxpayers", including exclusions, deductions, credits, preferential tax rates, and exemptions under a range of different tax regimes, not limited to the retail sales and use taxes.²⁷¹ On the basis of data in this study, both parties have submitted figures on the quantitative coverage of certain exemptions in relation to the underlying tax. The United States refers to the large number of exemptions as "suggesting that the sales and use tax rates that are notionally (but not actually) applicable to all purchases by consumers located in Washington are not the appropriate benchmark".²⁷²

7.123. Having examined the tax study, the Panel finds that it evidences a tax regime structure in which there are specific exemptions targeted at defined beneficiaries.²⁷³ To the extent that the study is submitted as evidence of the factual assertion that exemptions from the tax rules in question (sales and use taxes) are of greater value than government revenue collected under those rules, the parties' arguments based on this study do not clearly establish that this is the case. For example, the parties derive fractions using different figures for the numerator²⁷⁴, and the figures used by both parties fail to adjust for the exemptions in question that are available to the aerospace industry, which could be necessary to assess government revenue that would be "otherwise due" and to guard against the normative benchmark being distorted by alleged subsidies at issue.²⁷⁵

7.124. The Panel considers that the quantitative scope of what may be considered an "exception" could undermine the notion of a "general rule" for a given tax situation. An organizing principle that a government professes in respect of a tax, or that appears to be the principle that is being applied "on the surface", may not represent the "true" organizing principle. The terms and principles employed by the sovereign tax authority in question will be important but in all cases the Panel's decision must be informed by the evidence and by the Panel's interpretation of it. In this respect, the Panel finds relevant the Appellate Body's statement that the benchmark for comparison is normative in nature, and that "the task of the panel is to develop an understanding of the tax structure and principles that best explains that Member's tax regime, and to provide a reasoned basis for identifying what constitutes comparable income of comparably situated taxpayers".²⁷⁶

²⁶⁸ See Table of Contents for RCW Chapter 82.08 (Exhibit USA-64); Retail Sales Tax Explanation, Washington State Department of Revenue (Exhibit USA-12) (listing "common exemptions" that include food, prescription drugs, sales to nonresidents, federal government sales, interstate and foreign sales, manufacturers' machinery and equipment, sales to Indians or Indian tribes, and newspapers); 2016 Tax Exemption Study, Washington State Department of Revenue (Exhibit EU-95), Appendix B; United States' response to Panel question No. 25, para. 55 (providing as examples motor vehicles and brokered natural gas).

²⁶⁹ See parties' responses and comments on each other's responses to Panel question No. 60.

²⁷⁰ 2016 Tax Exemption Study, Washington State Department of Revenue (Exhibit USA-65), Introduction and Summary of Findings.

²⁷¹ Ibid. p. 1-1.

²⁷² United States' response to Panel question No. 56, para. 21.

²⁷³ 2016 Tax Exemption Study, Washington State Department of Revenue (Exhibit EU-95), Appendix B.

²⁷⁴ Specifically, the United States uses a fraction based on "taxpayer savings from exemptions", whereas the European Union uses a fraction based on "state potential revenue gains" – these figures form the numerator of the fraction to represent the value of the exemption, and both parties add "forecasted tax revenues" of the particular tax to the chosen exemption value to form the denominator. The difference between taxpayer savings, on the one hand, and potential revenue gains from a full repeal, on the other hand, is that repeal of a given exemption does not automatically mean the tax can be collected due to other reasons within the Washington State tax system. See 2016 Tax Exemption Study, Washington State Department of Revenue (Exhibit USA-65), Introduction and Summary of Findings, p. 1-3.

²⁷⁵ See Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 824.

²⁷⁶ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 813.

7.125. In this case, the Washington State sales and use taxes are drawn as broadly applicable taxes in a non-exhaustive fashion, and are designed to complement one another through mutually exclusive coverage. This breadth of the sales and use taxes is foundational to the structure of the sales and use tax regime, which set out exemptions in a specific manner. Although the exemptions involve a diversity of goods, services, and sectors, the evidence advanced by the United States is not sufficient to rebut the *prima facie* conclusion that can be drawn from what the European Union has placed before the Panel. The structure of the tax is that of a generally applicable tax that applies by default. As a matter of fact the Panel does not find that structure to have been inverted by the relative coverage of exemptions in quantitative terms. In other words, exempting taxpayers from sales and use taxes does not amount to an "organizing principle" of the Washington State sales and use tax regime (or the Washington State tax regime more generally).

7.126. It is with regard for this basic structure, and on the basis of the rules established by Washington State, that the Panel finds that the generally applicable sales and use taxes serve as the appropriate normative benchmark in respect of the computer sales and use tax exemptions.

7.4.3.4.3 Third step: comparison of applicable tax treatment with benchmark

7.127. In view of the benchmark established above, it follows that the specific exemption from sales and use taxes, which otherwise would apply to the aerospace activities in question, amounts to the foregoing of government revenue by Washington State that would otherwise be due. Accordingly, the Panel finds that the computer sales and use tax exemption constitutes a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement.

7.4.3.5 Construction sales and use tax exemptions

7.128. The legislation for the construction sales tax exemption provides in relevant part:

(1) The tax levied by RCW 82.08.020 does not apply to:

(a) Charges, for labor and services rendered in respect to the constructing of new buildings, made to (i) a manufacturer engaged in the manufacturing of commercial airplanes or the fuselages or wings of commercial airplanes or (ii) a port district, political subdivision, or municipal corporation, to be leased to a manufacturer engaged in the manufacturing of commercial airplanes or the fuselages or wings of commercial airplanes;

(b) Sales of tangible personal property that will be incorporated as an ingredient or component of such buildings during the course of the constructing; or

(c) Charges made for labor and services rendered in respect to installing, during the course of constructing such buildings, building fixtures ...²⁷⁷

7.129. The construction use tax exemption provides in relevant part:

(1) The provisions of this chapter do not apply with respect to the use of:

(a) Tangible personal property that will be incorporated as an ingredient or component in constructing new buildings for (i) a manufacturer engaged in the manufacturing of commercial airplanes or the fuselages or wings of commercial airplanes or (ii) a port district, political subdivision, or municipal corporation, to be leased to a manufacturer engaged in the manufacturing of commercial airplanes or the fuselages or wings of commercial airplanes; or

(b) Labor and services rendered in respect to installing, during the course of constructing such buildings, building fixtures ...²⁷⁸

²⁷⁷ RCW Section 82.08.980 (Exhibit EU-27).

²⁷⁸ RCW Section 82.12.980 (Exhibit EU-28).

7.4.3.5.1 First step: applicable tax treatment

7.130. Based on the available evidence, the Panel will first identify the applicable tax treatment under the construction sales and use tax exemptions, including consideration of the objective reasons behind that treatment. As provided for in the relevant legislation, Washington State provides exemptions from retail sales taxes²⁷⁹ on "[c]harges, for labor and services rendered in respect to the constructing of new buildings, made to a manufacturer engaged in the manufacturing of commercial airplanes or the fuselages or wings of commercial airplanes", as well as taxes on "[s]ales of tangible personal property that will be incorporated as an ingredient or component of such buildings during the course of the constructing".²⁸⁰ Similarly, there is an exemption from use taxes "with respect to the use of [t]angible personal property that will be incorporated as an ingredient or component in constructing new buildings for a manufacturer engaged in the manufacturing of commercial airplanes or the fuselages or wings of commercial airplanes".²⁸¹ As a result of ESSB 5952, the construction sales and use tax exemptions expire on 1 July 2040.²⁸² Thus, the relevant tax treatment for the covered activities and products, at present and until the 2040 expiry date, is as set forth above.

7.131. This tax treatment forms part of the legislation in ESSB 5952 targeted towards the aerospace industry in Washington State. As such, its "objective reasons" are the same as discussed in respect of the B&O aerospace tax rate – that is, to provide favourable tax treatment for the aerospace industry in order to encourage the industry to remain in Washington State and to grow its workforce.²⁸³

7.4.3.5.2 Second step: benchmark for comparison

7.132. The parties have not differentiated between the computer sales and use tax exemptions, on the one hand, and the construction sales and use tax exemptions, on the other, in their arguments regarding the benchmark for comparison.

7.133. The construction sales and use tax exemptions pertain to the same underlying tax obligations as those considered above, namely the Washington State retail sales and use taxes. In the Panel's view, the same considerations apply in determining the appropriate normative benchmark for comparison in relation to the construction sales and use tax exemptions. These exemptions form a targeted tax treatment within a structure organized according to the principle that either sales or use taxes, but not both, are generally due on the sales and use of tangible goods and services. In light of this basic organizing principle, it is the generally applicable sales and use taxes that serve as the appropriate normative benchmark in this case.

7.4.3.5.3 Third step: comparison of applicable tax treatment with benchmark

7.134. In view of the benchmark established above, it follows that the specific exemption from sales and use taxes, which would otherwise apply to the aerospace activities in question, amounts to the foregoing of government revenue by Washington State that would otherwise be due. Accordingly, the Panel finds that the construction sales and use tax exemption constitutes a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement.

7.4.3.6 Leasehold excise tax exemption

7.135. The legislation for the leasehold excise tax exemption provides in relevant part:

²⁷⁹ RCW Section 82.08.020 (Exhibit EU-92).

²⁸⁰ RCW Section 82.08.980 (Exhibit EU-27). A similar exemption is applied for charges, for labor and services for constructing new buildings, made to "a port district, political subdivision, or municipal corporation, to be leased to a manufacturer engaged in the manufacturing of commercial airplanes or the fuselages or wings of commercial airplanes".

²⁸¹ RCW Section 82.12.980 (Exhibit EU-28). A similar exemption is applied to tangible property used in constructing new buildings for "a port district, political subdivision, or municipal corporation, to be leased to a manufacturer engaged in the manufacturing of commercial airplanes or the fuselages or wings of commercial airplanes".

²⁸² ESSB 5952 (Exhibit EU-3), Sections 3-4.

²⁸³ See para. 7.65 above.

(1) All leasehold interests in port district facilities exempt from tax under [the construction sales and use tax exemptions] and used by a manufacturer engaged in the manufacturing of superefficient airplanes ... are exempt from tax under this chapter. A person claiming the credit under [the B&O tax credit for property and leasehold excise taxes] is not eligible for the exemption under this section.²⁸⁴

7.4.3.6.1 First step: applicable tax treatment

7.136. Based on the available evidence, the Panel will first identify the applicable tax treatment under the leasehold excise tax exemption, including consideration of the objective reasons behind that treatment. As provided for in the relevant legislation, Washington State imposes a leasehold excise tax in lieu of a property tax on the use of public property by a private party.²⁸⁵ The relevant regulations explain that "[t]he intent of the law is to ensure that lessees of property owned by public entities bear their fair share of the cost of governmental services when the property is rented to someone who would be subject to property taxes if the lessee were the owner of the property".²⁸⁶ Washington State exempts from this tax leasehold interests in certain facilities "used by a manufacturer engaged in the manufacturing of superefficient airplanes".²⁸⁷ The leasehold excise tax exemption is not available to a person claiming the B&O tax credit for property and leasehold excise taxes.²⁸⁸ ESSB 5952 extended the application of this exemption to 1 July 2040.²⁸⁹ Thus, the relevant tax treatment for the covered activities, at present and until the 2040 expiry date, is as set forth above.

7.137. This tax treatment forms part of the legislation in ESSB 5952 targeted towards the aerospace industry in Washington State. As such, its "objective reasons" are the same as discussed in respect of the B&O aerospace tax rate – that is, to provide favourable tax treatment for the aerospace industry in order to encourage the industry to remain in Washington State and to grow its workforce.²⁹⁰

7.4.3.6.2 Second step: benchmark for comparison

7.138. Having identified the relevant tax treatment and its objective reasons, the next step of the analysis is the identification of an appropriate "benchmark for comparison" within the Washington State tax regime to determine whether this tax treatment constitutes revenue foregone by the Washington State government that would otherwise be due. This benchmark must be ascertained with regard for "the structure of the domestic tax regime and its organizing principles".²⁹¹

7.139. The European Union submits that the appropriate benchmark for comparison for the leasehold excise tax exemption "is the payment of the 12.84 percent leasehold excise tax that would normally apply".²⁹² The United States, in addition to its general argument that the European Union has not met its burden to identify the benchmark for each aerospace tax measure, also submits that, for tax exemptions, the comparable taxable "event" is not an event involving the same taxpayer absent the exemptions, as this would be the "type of historical comparison for a taxpayer [that] was criticized by the Appellate Body".²⁹³ The United States further submits that "quantitative coverage of various tax regimes could be relevant to determining a financial

²⁸⁴ RCW Section 82.29A.137 (Exhibit EU-29).

²⁸⁵ Leasehold Excise Tax, Washington State Department of Revenue (Exhibit EU-49).

²⁸⁶ WAC Section 458-29A-100 (Exhibit EU-50).

²⁸⁷ Under Washington State law, "superefficient airplane" is defined as "a twin aisle airplane that carries between two hundred and three hundred fifty passengers, with a range of more than seven thousand two hundred nautical miles, a cruising speed of approximately mach .85, and that uses fifteen to twenty percent less fuel than other similar airplanes on the market". RCW Section 82.32.550(3) (Exhibit EU-82).

²⁸⁸ RCW Section 82.29A.137 (Exhibit EU-29).

²⁸⁹ ESSB 5952 (Exhibit EU-3), Section 13; RCW Section 82.29A.137 (Exhibit EU-29).

²⁹⁰ See para. 7.65 above.

²⁹¹ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 813.

²⁹² European Union's response to Panel question No. 24, para. 51.

²⁹³ United States' response to Panel question No. 57, para. 23 (citing Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 815).

contribution compared to a normative benchmark"²⁹⁴ and that "tax exemptions far outweighed tax revenues" for state property taxes.²⁹⁵

7.140. The Panel notes that the leasehold excise tax is an excise tax that supplements the Washington State property tax regime. Specifically, the leasehold excise tax applies in lieu of real property tax where a private party uses public property under lease, rather than owning real property. This tax is complementary to real and personal property taxes, which are levied in accordance with the statutory rule of the property tax regime in Washington State that "[a]ll property now existing, or that is hereafter created or brought into this state, shall be subject to assessment and taxation for state, county, and other taxing district purposes".²⁹⁶ Thus, real and personal property is generally subject to taxation, although a number of exemptions to this general rule apply.²⁹⁷ For example, property valued at less than USD 500, churches and cemeteries, business inventory, and property owned by federal, state, and local governments are all exempt from property taxation.²⁹⁸ Although government-owned property as such is not subject to property tax, such property becomes subject to the leasehold excise tax when it is used by a private party. Personal property such as household goods and personal effects are not subject to property tax unless these items are used in a business, and personal property is subject to the same levy rate as real property.²⁹⁹

7.141. Based on the foregoing, the Panel considers that it is the Washington State property tax regime, as distinguished from other types of taxation that exist in Washington State, that is relevant to identifying the appropriate benchmark for the leasehold excise tax exemption. As noted, under this tax regime, real and personal property is subject to taxation unless a specific exemption applies. In this respect, while the Panel takes note of the parties' arguments on the quantitative coverage of property tax exemptions³⁰⁰, the relevant rules established by Washington State authorities suggest that the organizing principle of the tax regime is to create a default rule of property taxation with provision for specific exemptions and the quantitative information does not displace that principle. Exempting taxpayers from property tax liability does not appear to be an "organizing principle" of the Washington State property tax regime. Nor does the structure of the tax regime in question suggest an alternative benchmark apart from the generally defined norm of being subject to property taxation. The particular features of the leasehold excise tax, which is a tax on the use of public property by a private party in lieu of the property tax, reinforces the notion of generally applicable property taxation as the appropriate benchmark for comparison.³⁰¹ In light of this, the applicable leasehold excise tax rate of 12.84% of the rent paid by the lessee for the property represents the taxable situation that is legitimately comparable to that covered by the leasehold excise tax exemption.

7.142. Accordingly, the Panel considers that the benchmark for comparison for the leasehold excise tax exemption is the leasehold excise tax that would ordinarily be imposed on private parties using public property.

7.4.3.6.3 Third step: comparison of applicable tax treatment with benchmark

7.143. Given the benchmark of otherwise applicable leasehold excise taxation within the general regime of property taxation, the specific exemption from leasehold excise taxes, which would otherwise apply to the aerospace activities in question, amounts to the foregoing of government

²⁹⁴ United States' response to Panel question No. 60, para. 31.

²⁹⁵ Ibid. para. 32.

²⁹⁶ RCW Section 84.36.005 (Exhibit USA-20).

²⁹⁷ United States' first written submission, para. 46.

²⁹⁸ RCW Section 84.36.010 (Exhibit USA-21); RCW Section 84.36.020 (Exhibit USA-22); RCW Section 84.36.477 (Exhibit USA-23).

²⁹⁹ Real and personal property are chiefly distinguished by the characteristic of mobility, with the former including "land, structures, improvements to land, and certain equipment affixed to land or structures", and the latter including "machinery, equipment, furniture, and supplies of businesses and farmers". Personal Property Tax, Washington State Department of Revenue (Exhibit EU-51).

³⁰⁰ See parties' responses and comments on each other's responses to Panel question No. 60. See also paras. 7.123-7.125 above. The Panel notes that the parties relied upon the same tax exemption study in respect of exemptions from property taxation as that cited in respect of exemptions from retail sales and use taxes.

³⁰¹ Leasehold Excise Tax Explanation, Washington State Department of Revenue (Exhibit USA-25); WAC Section 458-29A-100 (Exhibit EU-50).

revenue by Washington State that would otherwise be due. Accordingly, the Panel finds that the leasehold excise tax exemption constitutes a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement.

7.4.3.7 Leaseholder property tax exemption

7.144. The legislation for the leaseholder property tax exemption provides in relevant part:

(1) Effective January 1, 2005, all buildings, machinery, equipment, and other personal property of a lessee of a port district eligible under [the construction sales and use tax exemptions], used exclusively in manufacturing superefficient airplanes, are exempt from property taxation. A person taking the credit under [the B&O tax credit for property and leasehold excise taxes] is not eligible for the exemption under this section. ...³⁰²

7.4.3.7.1 First step: applicable tax treatment

7.145. Based on the available evidence, the Panel will first identify the applicable tax treatment under the leaseholder property tax exemption, including consideration of the objective reasons behind that treatment. As provided for in the relevant legislation, Washington State exempts from property taxation "all buildings, machinery, equipment, and other personal property of a lessee of a port district eligible [for construction sales and use tax exemptions], used exclusively in manufacturing superefficient airplanes".³⁰³ The leaseholder property tax exemption is not available to a person claiming the B&O tax credit for property and leasehold excise taxes.³⁰⁴ ESSB 5952 extended the application of this exemption to 1 July 2040.³⁰⁵ Thus, the relevant tax treatment, at present and until the 2040 expiry date, is as set forth above.

7.146. This tax treatment forms part of the legislation in ESSB 5952 targeted towards the aerospace industry in Washington State. As such, its "objective reasons" are the same as discussed in respect of the B&O aerospace tax rate – that is, to provide favourable tax treatment for the aerospace industry in order to encourage the industry to remain in Washington State and to grow its workforce.³⁰⁶

7.4.3.7.2 Second step: benchmark for comparison

7.147. Having identified the relevant tax treatment and its objective reasons, the next step of the analysis is the identification of an appropriate "benchmark for comparison" within the Washington State tax regime to determine whether this tax treatment constitutes revenue foregone by the Washington State government that would otherwise be due. This benchmark must be ascertained with regard for "the structure of the domestic tax regime and its organizing principles".³⁰⁷

7.148. The European Union submits that the leaseholder property tax exemption "exempts certain otherwise taxable business property from the property taxes that would normally apply", and "that otherwise applicable property tax treatment therefore provides the normative benchmark".³⁰⁸ The United States, in addition to its general argument that the European Union has not met its burden to identify the benchmark for each aerospace tax measure, also submits that, for tax exemptions, the comparable taxable "event" is not an event involving the same taxpayer absent the exemptions, as this would be the "type of historical comparison for a taxpayer [that] was criticized by the Appellate Body".³⁰⁹ The United States further submits that "quantitative coverage of various

³⁰² RCW Section 84.36.655 (Exhibit EU-30).

³⁰³ Ibid. Under Washington State law, "superefficient airplane" is defined as "a twin aisle airplane that carries between two hundred and three hundred fifty passengers, with a range of more than seven thousand two hundred nautical miles, a cruising speed of approximately mach .85, and that uses fifteen to twenty percent less fuel than other similar airplanes on the market". RCW Section 82.32.550(3) (Exhibit EU-82).

³⁰⁴ RCW Section 84.36.655 (Exhibit EU-30).

³⁰⁵ ESSB 5952 (Exhibit EU-3), Section 14.

³⁰⁶ See para. 7.65 above.

³⁰⁷ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 813.

³⁰⁸ European Union's response to Panel question No. 24, para. 51.

³⁰⁹ United States' response to Panel question No. 57, para. 23 (citing Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 815).

tax regimes could be relevant to determining a financial contribution compared to a normative benchmark"³¹⁰ and that "tax exemptions far outweighed tax revenues" for state property taxes.³¹¹

7.149. As discussed above, under the relevant statutory rule of the Washington State property tax regime³¹², real and personal property in Washington State is generally subject to taxation, although a number of exemptions from this general rule apply.³¹³ In this respect, the Panel has noted that the relevant rules established by Washington State authorities suggest that the organizing principle of the tax regime is to create a default rule of property taxation with provision for specific exemptions and the quantitative information does not displace that principle. Exempting taxpayers from property tax liability does not appear to be an "organizing principle" of the Washington State property tax regime. Nor does the structure of the tax regime in question suggest an alternative benchmark apart from the generally defined norm of being subject to property taxation. Thus, the generally applicable property tax within the state of Washington corresponds to the taxable situation (namely ownership of personal property by an eligible lessee) that is legitimately comparable to that covered by the leaseholder property tax exemption.

7.150. Accordingly, the Panel considers that the benchmark for comparison is the property tax that would ordinarily be imposed on personal property of lessees of port districts.

7.4.3.7.3 Third step: comparison of applicable tax treatment with benchmark

7.151. Given the benchmark of otherwise applicable property taxation, the specific exemption from property taxes, which would otherwise apply to the aerospace activities in question, amounts to the foregoing of government revenue by Washington State that would otherwise be due. Accordingly, the Panel finds that the leaseholder property tax exemption constitutes a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement.

7.4.3.8 Conclusion on financial contribution

7.152. In concluding, the Panel notes various additional arguments raised by the parties in relation to whether the aerospace tax measures constitute a financial contribution.

7.153. The United States has submitted that aerospace activity until 1 July 2024 would have qualified for certain tax treatment under legislation pre-dating ESSB 5952, and that the extent of any financial contribution in this dispute would be limited to revenue foregone at some point in the future.³¹⁴ In this regard, the Panel recalls its determination that the aerospace tax incentives at issue are those as currently codified and in effect until 2040 by virtue of ESSB 5952.³¹⁵ Thus, the preceding analysis of a financial contribution under each of the aerospace tax measures does not refer to a future window of time during which pre-existing tax treatment was extended. Rather, the analysis of government revenue foregone has been conducted in regard to the currently codified tax provisions, which reflect and incorporate a series of earlier legislative acts, in addition to incorporating new substantive provisions created by ESSB 5952.

7.154. The Panel further notes the European Union's clarification that its claim is directed at the aerospace tax measures "as such", and thus is "not directed against the application of these measures during any given point in time or in any specific instance".³¹⁶ The Panel considers this an important distinction from the claim made in *US – Large Civil Aircraft (2nd complaint)*, in which arguments were presented and assessed in relation to Boeing-specific subsidies and their alleged causation of adverse effects under Part III of the SCM Agreement. Thus, although evidence of actual use of certain fiscal incentives may support or confirm a finding that government revenue is foregone that is otherwise due³¹⁷, the Panel does not consider this to be required for the purposes

³¹⁰ United States' response to Panel question No. 60, para. 31.

³¹¹ Ibid. para. 32.

³¹² RCW Section 84.36.005 (Exhibit USA-20).

³¹³ United States' first written submission, para. 46; RCW Section 84.36.010 (Exhibit USA-21); RCW Section 84.36.020 (Exhibit USA-22); RCW Section 84.36.020 (Exhibit USA-23).

³¹⁴ United States' response to Panel question No. 2.

³¹⁵ See para. 7.42 above.

³¹⁶ European Union's response to Panel question No. 6, para. 7.

³¹⁷ See ESSB 5952 Fiscal Note (Exhibit EU-5); Snohomish County Council Lease Approval (Exhibit EU-44); Paine Field Community Council, Minutes of Meeting of 12 November 2013 (Exhibit EU-45); The Seattle Times, "State gave Boeing a free pass on \$19.5M in sales tax", 30 November 2015

of Article 1.1(a)(1)(ii) of the SCM Agreement, particularly where a claim is made that the challenged measures "as such" make a financial contribution.³¹⁸

7.155. In the same vein, the Panel notes the issue raised by the United States of whether it is possible to establish a financial contribution (and benefit) for tax incentives that legally are mutually exclusive according to their own explicit terms, as is the case for the B&O tax credit for property and leasehold excise taxes on the one hand, and the tax exemptions related to leasehold excise taxes and leaseholder property taxes on the other hand.³¹⁹ The Panel does not consider that any such mutual exclusivity should prevent simultaneous challenge, or a finding that each tax incentive, on its own and "as such", represents the foregoing of revenue otherwise due. The fact that a taxpayer can in the future choose between tax incentives does not render the one that ultimately is not chosen to be less of a foregoing of revenue. Furthermore, for measures such as those at issue where there may be multiple potential recipients of the financial contribution, certain taxpayers may be eligible for, and may use, one incentive, while others may be eligible for, and may use, the other at any given moment during the period of availability of the tax measures (in this case, until the expiration of the aerospace tax measures in 2040).³²⁰

7.156. Finally, the Panel notes the United States' reiteration that the European Union has failed to meet its burden of proof in respect of any financial contribution made by the aerospace tax measures, and that this burden cannot be met by substituting the findings made in the context of *US – Large Civil Aircraft (2nd complaint)* regarding different claims and measures. The Panel agrees that its terms of reference are confined to the aerospace tax measures identified in the European Union's panel request in the present case, which are formally and substantively distinct from those considered in *US – Large Civil Aircraft (2nd complaint)*. The Panel's assessment is based upon arguments and evidence on the record of this dispute, with careful regard for the principle that it is the complaining party's burden to establish a *prima facie* case which, in the absence of adequate refutation, requires the Panel to rule in favour of the complaining party. A significant amount of evidence was placed before the Panel by the European Union, and its submissions led the Panel to various relevant aspects of that evidence. Brevity in the European Union's submissions did not prejudice its satisfaction of the burden of proving facts to establish that the measures involved a foregoing of revenue otherwise due within the terms of Article 1.1(a)(1)(ii) of the SCM Agreement. The case put in rebuttal by the United States did not reverse the European Union's satisfaction of its burden.

7.157. In conclusion, none of these arguments disturbs the Panel's above analysis of the aerospace tax measures. Accordingly, the Panel finds that each aerospace tax measure constitutes a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement because "government revenue that is otherwise due is foregone or not collected".

(Exhibit EU-48); The Seattle Times, "Boeing must disclose tax-break savings, state Department of Revenue rules", 8 January 2016 (Exhibit EU-121).

³¹⁸ In the view of the United States, "where a Member challenges the alleged grant of a subsidy to a particular recipient of an alleged subsidy, that Member normally must establish actual receipt of that subsidy. That may not be the case where a Member asserts 'that a financial contribution exists in the abstract', which the EU has now clarified is its argument in this proceeding." United States' second written submission, para. 85.

³¹⁹ See, e.g. United States' response to Panel question No. 2, para. 4.

³²⁰ In this connection, the Panel's conclusions are not impacted by the fact that the alleged contingency of using domestic over imported goods does not apply to all potential beneficiaries of the subsidies at issue. The provision of subsidies to a range of beneficiaries based on a contingency applicable to only one or some of those beneficiaries may still be found inconsistent with the disciplines of the SCM Agreement, provided that: (i) a subsidy exists within the meaning of Article 1; and (ii) the availability of any such subsidy, to whichever recipient or beneficiary, is contingent in the manner set out in Article 3. These provisions do not require any strict identity of subsidy recipients and entities subject to the contingency in question. The Panel is therefore unpersuaded by the United States' contention that the applicability of ESSB 5952's contingencies to only one potential recipient of subsidies "disproves the EU's claims that the alleged subsidies are 'as such' contingent on the use of domestic over imported fuselages and wings". See United States' response to Panel question No. 59, para. 25. Accordingly, the Panel assesses in this section the criteria for determining the existence of a subsidy, and separately will consider whether, as a condition for access to any such subsidy, there is a requirement to use domestic over imported goods.

7.4.4 Whether a benefit is thereby conferred

7.158. With respect to whether a benefit is conferred under Article 1.1(b) of the SCM Agreement, the Appellate Body emphasized that "a 'financial contribution' and a 'benefit' [are] two separate legal elements in Article 1.1 of the SCM Agreement, which together determine whether a subsidy exists".³²¹

7.159. The ordinary meaning of the term "benefit" has been understood as "clearly encompass[ing] some form of advantage".³²² The Appellate Body further explained that "the word 'benefit', as used in Article 1.1(b), implies some kind of comparison" to determine whether "the 'financial contribution' makes the recipient 'better off' than it would otherwise have been, absent that contribution".³²³ In the Appellate Body's view, "the marketplace provides an appropriate basis for comparison in determining whether a 'benefit' has been 'conferred', because the trade-distorting potential of a 'financial contribution' can be identified by determining whether the recipient has received a 'financial contribution' on terms more favourable than those available to the recipient in the market."³²⁴

7.160. In the case of tax-based financial contributions, while the foregoing of revenue by a government may not be conceptually equivalent to the enjoyment of an advantage by the recipient, as a practical matter the two will often coincide. That is, where the government is found to have foregone revenue, this is because it has departed from the normative benchmark in respect of some particular category or class of taxpayers or activities. By virtue of foregoing revenue, that departure from the norm means that the taxpayers that are subject to the government's normative departure owe less tax than they otherwise would under the "normal" taxation rules.

7.161. It is in this light that the Panel understands the observation of the panel in *US – Large Civil Aircraft (2nd complaint)* that, "[i]n those cases where a financial contribution has been found to exist in the form of the foregoing of revenue otherwise due, the conclusion that a benefit exists has been made with little difficulty".³²⁵ Having reviewed cases in which the existence of a benefit readily followed from a determination of foregone revenue that was otherwise due³²⁶, the panel concluded that "the relevant tax break is essentially a gift from the government, or a waiver of obligations due, and it is clear that the market does not give such gifts".³²⁷ Although the parties disagree as to the extent to which revenue foregone is automatically *determinative* of a benefit, they have not directly called into question the soundness of the approach adopted by the panel in *US – Large Civil Aircraft (2nd complaint)* or its reliance on previous panels.

7.162. For tax-based financial contributions such as the aerospace tax measures, the relief from taxation otherwise due is not generally available to market participants, nor does it exist as a general condition in the marketplace. It is in this sense that the Panel understands the "marketplace" observations made by the Appellate Body in *Canada – Aircraft* as they would apply in the context of Article 1.1(a)(1)(ii).³²⁸ Indeed, the "market conditions" that are relevant as the benchmark in this context are the competitive conditions that exist in the absence of the challenged financial contribution. Judging the conferral of a benefit by reference to such market conditions, it is clear that the financial contributions of foregone government revenue otherwise due from certain Washington State taxpayers – through a reduced tax rate, credits against business taxation, or exemptions from otherwise applicable tax liability – makes the recipients

³²¹ Appellate Body Report, *Brazil – Aircraft*, para. 157. (emphasis omitted)

³²² Appellate Body Report, *Canada – Aircraft*, para. 153 (citing Panel Report, *Canada – Aircraft*, para. 9.112).

³²³ Appellate Body Report, *Canada – Aircraft*, para. 157.

³²⁴ Ibid.

³²⁵ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.169.

³²⁶ See Panel Reports, *US – FSC*, para. 7.103; *US – FSC (Article 21.5 – EC)*, para. 8.46; *Canada – Autos*, para. 10.165.

³²⁷ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.170. Accordingly, the panel found that "for those tax measures that it has found to constitute a financial contribution, a benefit is conferred". Ibid. para. 7.171.

³²⁸ See fn 324 above.

"better off" than they otherwise would have been, in the marketplace, absent those contributions.³²⁹

7.163. While bearing in mind the guidance of the Appellate Body as to the independence of the concepts of financial contribution and benefit³³⁰, the Panel does not consider itself precluded from using the same factual elements from its conclusions as to revenue foregone in its analysis of whether each measure also confers a benefit. By way of reference, financial contributions in the form of "grants" under Article 1.1(a)(1)(i) of the SCM Agreement have been found to confer benefits, "as they place the recipient in a better position than the recipient otherwise would have been in the marketplace", given that no entity acting pursuant to commercial considerations would make such unremunerated payments.³³¹ Similarly, a financial contribution in the form of foregone government revenue that is otherwise due is naturally apt to provide the taxpayers concerned with an "advantage" in comparison to market conditions where such advantages do not otherwise exist.

7.164. Accordingly, the Panel finds that each of the aerospace tax measures at issue confers a benefit within the meaning of Article 1.1(b) of the SCM Agreement.

7.4.5 Conclusion under Article 1 of the SCM Agreement

7.165. Having concluded that there is a financial contribution by the Washington State government under each of the aerospace tax measures at issue, and that a benefit is thereby conferred, the Panel finds that each of the aerospace tax measures at issue constitutes a subsidy within the meaning of Article 1 of the SCM Agreement.

7.5 Whether the challenged measures are prohibited subsidies under Article 3.1(b) of the SCM Agreement

7.166. The Panel has found that the challenged measures are subsidies within the meaning of Article 1 of the SCM Agreement. It will now proceed to consider whether, as alleged by the European Union, the measures are also "contingent ... upon the use of domestic over imported goods" and therefore prohibited subsidies under Article 3.1(b) of the SCM Agreement.

7.167. In this regard, the Panel recalls that, for a subsidy within the meaning of Article 1.1 to be subject to the provisions of Parts II, III, and V of the SCM Agreement (disciplines on prohibited subsidies, actionable subsidies, and countervailing measures, respectively), it must be "specific in accordance with the provisions of Article 2" of that Agreement.³³² The Panel further recalls that, pursuant to Article 2.3 of the SCM Agreement, prohibited subsidies are deemed to be specific. The

³²⁹ See Appellate Body Report, *Canada – Aircraft*, para. 154.

³³⁰ The Appellate Body has stated that "the second element in Article 1.1. is concerned with the 'benefit ... conferred' on the *recipient* by [the] governmental action" of making a financial contribution, and that a "'benefit' does not exist in the abstract, but must be received and enjoyed by a beneficiary or a recipient". The Appellate Body further considered that "[l]ogically, a 'benefit' can be said to arise only if a person, natural or legal, or a group of persons, has in fact received something". Appellate Body Report, *Canada – Aircraft*, paras. 154 and 156. (emphasis original)

The Panel notes that these statements were made in the context of rejecting a specific argument "that 'cost to government' is one way of conceiving of 'benefit'". Ibid. para. 154. The Appellate Body considered this approach to be "at odds with the ordinary meaning of Article 1.1(b), which focuses on the *recipient* and not on the *government* providing the 'financial contribution'". Ibid. (emphasis original) The Appellate Body was not addressing the particular factual circumstance of the actual use of a financial contribution (such as a tax incentive) by particular entities, nor did it address the potential relevance in this regard of alleged subsidies being challenged "as such". Rather, in response to particular arguments before it, the Appellate Body was emphasising the focus on *beneficiaries*, as distinct from the *provider*, of a given financial contribution in the conceptually distinct analysis of whether a benefit is conferred by that financial contribution.

³³¹ Panel Report, *US – Upland Cotton*, paras. 7.1116 and 7.1118. See also Panel Reports, *EC and certain member States – Large Civil Aircraft*, para. 7.1501 (finding that "to the extent that Airbus received a funding grant in the form of an actual 'direct transfer of funds' from the various entities involved, it was automatically placed in a better position than it would otherwise have been in without the grant", and that such funding grants therefore conferred a "benefit"); *US – Large Civil Aircraft (2nd complaint)*, paras. 7.1228-7.1229 (in relation to payments that were not disputed to "constitute a financial contribution in the form of a direct transfer of funds", finding that such payments confer a "benefit" under Article 1.1(b) of the SCM Agreement as such payments would not be made by any "private entity acting pursuant to commercial considerations") and 7.1362-7.1363.

³³² SCM Agreement, Article 1.2.

European Union's claim is that the measures at issue are prohibited subsidies in that they are contingent on the use of domestic over imported goods. Accordingly, no matter what the Panel decides in relation to the alleged contingency, the Panel is not required to conduct a specificity analysis under Article 2 of the SCM Agreement.

7.5.1 Arguments of the parties

7.5.1.1 European Union

7.168. The European Union alleges that the aerospace tax measures at issue are *de jure* and *de facto* contingent upon the use of domestic over imported goods and therefore inconsistent with the United States' obligations under Article 3.1(b) of the SCM Agreement.³³³ In the European Union's view, the challenged aerospace tax measures have been contingent in this manner from the time that ESSB 5952 was enacted.³³⁴

7.169. According to the European Union, its first and principal claim is that the challenged aerospace tax measures are *de jure* contingent upon the use of domestic over imported goods inasmuch as the text of ESSB 5952 clearly sets out the prohibited contingency.³³⁵ The European Union also makes a secondary claim that the aerospace tax measures are *de facto* contingent upon the use of domestic over imported goods.³³⁶

7.170. In the European Union's view, Article 3.1(b) of the SCM Agreement sets out a single standard irrespective of whether the claim is that the measure is *de jure* or *de facto* contingent on the use of domestic over imported goods. The difference would be the evidence necessary to establish each claim. A *de jure* claim would be made on the basis of the express terms of the text of the measure or by necessary implication therefrom, whereas in a *de facto* claim the contingency would have to be inferred "from the total configuration of facts constituting and surrounding the subsidy grant, including the design, structure and modalities of operation set out in the measure".³³⁷

7.171. With respect to its *de jure* claim, the European Union submits that, as clearly set out in the text of ESSB 5952, and as a result of the First Siting Provision and the Second Siting Provision, whether considered individually or together, the challenged aerospace tax measures constitute subsidies that are contingent in law on the use of domestic over imported goods.³³⁸ The prohibited contingency in respect of the use of fuselages as domestic goods would result solely from the First Siting Provision, while the prohibited contingency in respect of the use of wings as domestic goods would result from both the First Siting Provision and the Second Siting Provision.³³⁹

7.172. The European Union argues that, pursuant to the First Siting Provision in Section 2 of ESSB 5952, the challenged aerospace tax measures were contingent on the establishment of a new commercial aircraft manufacturing programme that uses goods (i.e., fuselages and wings) produced in the state of Washington. Under this provision, with respect to all aerospace companies in the state of Washington, if Boeing had decided to use imported wings and fuselages in the

³³³ European Union's second written submission, para. 40.

³³⁴ European Union's response to Panel question No. 6, para. 11.

³³⁵ European Union's second written submission, paras. 1, 2, 41 and 90; closing statement at the first meeting of the Panel, para. 1; opening statement at the second meeting of the Panel, para. 2; response to Panel question Nos. 29 and 46, paras. 67 and 125. See also Request for the Establishment of a Panel by the European Union, WT/DS487/2, 13 February 2015, p. 2.

³³⁶ European Union's second written submission, paras. 1 and 90; opening statement at the second meeting of the Panel, para. 2. See also Request for the Establishment of a Panel by the European Union, WT/DS487/2, 13 February 2015, p. 2.

³³⁷ European Union's first written submission, para. 72; second written submission, para. 44; opening statement at the first meeting of the Panel, para. 47; response to Panel question Nos. 18 and 30, paras. 23-26 and 68-69.

³³⁸ European Union's first written submission, paras. 70 and 73; second written submission, paras. 1, 41 and 60; opening statement at the first meeting of the Panel, para. 6; response to Panel question No. 41, para. 98.

³³⁹ European Union's response to Panel question No. 43, para. 101.

assembly of the 777X (or any other new aircraft programme that it might have decided to site in Washington State), the challenged tax measures would not have been granted.³⁴⁰

7.173. The European Union also argues that, pursuant to the Second Siting Provision, the B&O aerospace tax rate for the 777X (or any other aircraft that Boeing might have sited to satisfy the First Siting Provision) is contingent on Boeing's use of wings produced exclusively in the state of Washington. The European Union contends in particular that, if Boeing were to source even some wings for the sited aircraft programme outside of the United States, it would lose access to the B&O aerospace tax rate in respect of the manufacturing and sale of 777X airplanes.³⁴¹

7.174. The European Union further asserts that the United States' proposed reading of the First Siting Provision and the Second Siting Provision would render meaningless all references contained therein to "wings" and to "fuselages".³⁴² The European Union also argues that the text of ESSB 5952 does not require that the same manufacturer produce both the commercial airplane and the fuselages and wings; to the contrary, nothing in ESSB 5952 would preclude an airplane manufacturer from procuring wings or fuselages from another producer, as long as this other producer is located in the state of Washington.³⁴³ The European Union further contends that the Second Siting Provision in ESSB 5952 would be triggered even by a single instance of final assembly outside the state of Washington of an airplane which was the basis of the original siting decision, or by a single instance of wing assembly for that airplane outside the state of Washington, either by Boeing or by any other entity, and that this would result in precluding the continued availability of the B&O aerospace tax rate.³⁴⁴

7.175. The European Union argues further that any evidence provided by the United States and related to the manner in which Boeing purportedly will produce 777X aircraft is irrelevant to the Panel's consideration of the European Union's *de jure* claim, although some of those facts could be relevant to the European Union's *de facto* claim.³⁴⁵

7.176. With respect to its *de facto* claim, the European Union submits that the First Siting Provision and the Second Siting Provision in ESSB 5952 are each capable of strongly influencing Boeing's choice between imported wings and fuselages, and domestic (United States-produced) wings and fuselages, for the 777X airplanes.³⁴⁶ According to the European Union, ESSB 5952 creates specific penalties for the use of imported wings or fuselages and rewards for the use of domestic wings or fuselages. The First Siting Provision and the Second Siting Provision acting together would maximize trade distortions in favour of domestic goods to the detriment of imported goods, which suggests that the challenged measures are geared to induce the use of domestic over imported goods.³⁴⁷ In the European Union's view, the subsidies at issue exceed the total development cost of the 777X airplanes, and would thereby overshadow any other factors that may favour a decision by Boeing to import wings and fuselages for 777X airplanes.³⁴⁸

³⁴⁰ European Union's first written submission, paras. 44 and 74; second written submission, para. 61; opening statement at the first meeting of the Panel, paras. 53-54; opening statement at the second meeting of the Panel, para. 3.

³⁴¹ European Union's first written submission, paras. 47, 51-52 and 75; second written submission, para. 61; opening statement at the first meeting of the Panel, paras. 55-56; response to Panel question No. 7, para. 12.

³⁴² European Union's second written submission, paras. 65-75.

³⁴³ European Union's second written submission, paras. 65 and 76-81; opening statement at the first meeting of the Panel, paras. 60-61; response to Panel question No. 45, para. 119.

³⁴⁴ European Union's second written submission, paras. 65 and 82-84; opening statement at the first meeting of the Panel, para. 61; response to Panel question No. 7, para. 12.

³⁴⁵ European Union's second written submission, para. 41.

³⁴⁶ European Union's first written submission, para. 77; second written submission, para. 90. See also European Union's second written submission, para. 91; opening statement at the first meeting of the Panel, paras. 72-73; response to Panel question No. 29, paras. 66-67; Reuters, "Boeing seen in advanced talks to make 777X near Seattle", 4 November 2013 (Exhibit EU-65).

³⁴⁷ European Union's first written submission, para. 77; opening statement at the first meeting of the Panel, paras. 6 and 70-74; response to Panel question Nos. 31 and 41, paras. 70-71 and 98.

³⁴⁸ European Union's second written submission, para. 90. See also *ibid*, para. 91; European Union's opening statement at the first meeting of the Panel, para. 73; response to Panel question No. 29, paras. 66-67; Reuters, "Boeing seen in advanced talks to make 777X near Seattle", 4 November 2013 (Exhibit EU-65).

7.5.1.2 United States

7.177. In the United States' view, the main issue before the Panel is whether a subsidy granted for the manufacture of a finished good, including its major structural elements, and which allows the producer to import all the *parts* that are used in the production process, can nonetheless be considered to be a subsidy contingent upon the use of domestic over imported goods.³⁴⁹ The United States argues in this regard that a contingency is only inconsistent with Article 3.1(b) of the SCM Agreement if it requires the use of domestic over imported goods³⁵⁰, and that this determination must take into account all sources that elucidate the meaning of the words used in the measure at issue, including relevant factual information on the application of the measure.³⁵¹ According to the United States, in the analysis of both the *de jure* and the *de facto* claims, the Panel should consider evidence that pertains to the actual operation of the measure, beyond the text of the legal instrument in question.³⁵²

7.178. As a factual matter, the United States asserts that Boeing does not use wings or fuselages, either domestic or imported, to produce 777X airplanes.³⁵³ According to the United States, fuselages and wings are not manufactured as separate products that are subsequently used in the manufacture of a finished 777X airplane.³⁵⁴

7.179. The United States asserts that the European Union has failed to establish that the aerospace tax measures at issue are *de jure* contingent upon the use of domestic over imported goods. According to the United States, if a taxpayer can meet a condition without resorting to the use of domestic over imported goods this would be sufficient to demonstrate that the underlying measure is not an import-substitution subsidy prohibited by Article 3.1(b) of the SCM Agreement.³⁵⁵ The United States argues that "the First Siting Provision has been fulfilled, and the Second Siting Provision has been avoided, without any use of domestic over imported goods".³⁵⁶

7.180. The United States argues that:

The [First] Siting Provision and the [Second] Siting Provision in ESSB 5952 make no mention of *goods*. They make no mention of the *use* of goods. They make no mention of the *domestic nature* of goods. They make no mention of *imported goods*. They contain no text that *requires* the use of domestic over imported goods, nor even *encourages* it. They therefore do not result in any *discrimination* against imported goods.³⁵⁷ (emphasis added)

7.181. According to the United States, the references to the manufacturing and the assembly of fuselages and wings in the First Siting Provision and the Second Siting Provision merely define the scope of the *production activity* required to enjoy the tax treatment covered by ESSB 5952.³⁵⁸ The United States argues that there are several means of satisfying the First Siting Provision and the Second Siting Provision, including one that would not involve the use of fuselages and wings as inputs into the airplane production process, namely the 777X manufacturing programme.³⁵⁹

7.182. The United States argues further that the European Union has failed to demonstrate the existence of a domestic good on which the subsidies are allegedly contingent. According to the United States, ESSB 5952 does not require the use of any domestic *parts* in the assembly of the

³⁴⁹ United States' second written submission, paras. 1-3.

³⁵⁰ United States' first written submission, para. 104; second written submission, paras. 10-14.

³⁵¹ United States' second written submission, paras. 11, 17 and 34.

³⁵² United States' second written submission, paras. 29-34 and 36; response to Panel question No. 18, paras. 37-43.

³⁵³ United States' first written submission, paras. 37 and 105; second written submission, paras. 35 and 54-56; response to Panel question No. 44, para. 104.

³⁵⁴ United States' first written submission, para. 105; response to Panel question Nos. 34, 35 and 42, paras. 79, 81-82, 102 and 110-115.

³⁵⁵ United States' second written submission, paras. 10-11, 15-16, 37 and 51.

³⁵⁶ United States' second written submission, para. 58. See also *ibid.* paras. 60-62; United States' response to Panel question No. 33, para. 74.

³⁵⁷ United States' first written submission, para. 3. See also *ibid.* paras. 73, 101, 105-107 and 109.

³⁵⁸ United States' first written submission, paras. 73 and 101; second written submission, paras. 38-47 and 57.

³⁵⁹ United States' second written submission, para. 51; response to Panel question No. 18, para. 43.

fuselages and the wings; Boeing would be free to import 100% of the parts as long as the assembly takes place in the state of Washington.³⁶⁰

7.183. The United States further asserts that the European Union has failed to establish that the aerospace tax measures at issue are *de facto* contingent upon the use of domestic over imported goods, because it has not demonstrated that the use of domestic goods is required as a condition for eligibility for the subsidy.³⁶¹ According to the United States, none of the factual evidence referred to by the European Union supports its claim that the measures are *de facto* contingent.³⁶²

7.184. The United States also argues that Boeing has complied with the First Siting Provision and has avoided triggering the Second Siting Provision even though it does not use domestic wings and fuselages and instead completes the assembly of wings and fuselages as part of the final assembly of the finished airplane.³⁶³ The United States adds that the measures in ESSB 5952 had no effect on Boeing's make/buy decisions nor on its decision on where to site the assembly of fuselages and wings.³⁶⁴ The United States contends that the European Union has failed to establish that the challenged measures are geared to induce the use of domestic over imported goods.³⁶⁵ The United States submits that, provided it conducts the requisite assembly activity in the state of Washington, Boeing would satisfy the First Siting Provision and avoid triggering the Second Siting Provision even if it imported every part of the 777X airplane; Boeing therefore would be receiving no rewards for increasing the use of domestic inputs on the 777X airplane, nor would it be penalized for increasing the use of imported inputs.³⁶⁶

7.185. The United States rejects the interpretation advanced by the European Union on the meaning of the word "use" in Article 3.1(b) of the SCM Agreement, saying that a broad characterization of the meaning of the word "use", such as that advocated by the European Union, would be subjective in that it is not based on the text of the SCM Agreement.³⁶⁷ According to the United States, the term "use" in Article 3.1(b) refers to the employment of a domestic good as an input or instrumentality in a productive process, or to the enjoyment of a good for its intended purpose by an end user.³⁶⁸ Accordingly, Article 3.1(b) would cover subsidies granted contingent on the employment of a good as an input or instrumentality in a productive process, but not subsidies contingent on the creation of the output of such a productive process.³⁶⁹ In the United States' view, Article 3.1(b) of the SCM Agreement does not prohibit "production subsidies"; in this respect, the United States argues that Article III:8(b) of the GATT 1994 provides relevant context for the interpretation of Article 3.1(b).³⁷⁰

7.5.2 Third-party views

7.186. Australia submits that it is important that a distinction is retained between the permitted payment of a subsidy to domestic producers, including to encourage manufacturing activities, and a prohibited subsidy which is contingent on the use of domestic over imported goods.³⁷¹ Australia notes that it interprets the references to wings and fuselages in the legislation at issue merely as efforts to define the scope of the eligibility to the subsidy. According to Australia, "defining the scope of a subsidy in this manner does not imply that a subsidy is being provided contingent on the use of domestic over imported goods. Rather, it is a practical way of targeting an industry which the Washington State Government has chosen to support."³⁷² In Australia's view, the Panel needs to assess whether the challenged measure can be characterized as providing the scope for

³⁶⁰ United States' second written submission, paras. 24, 48-50, 57, 64, 68 and 84.

³⁶¹ Ibid. para. 58.

³⁶² Ibid. paras. 78-83.

³⁶³ Ibid. paras. 59-63.

³⁶⁴ Ibid. paras. 64-71 and 84.

³⁶⁵ United States' first written submission, paras. 105 and 132-140; second written submission, paras. 72-74; response to Panel question No. 30, paras. 65-67.

³⁶⁶ United States' second written submission, paras. 75-77.

³⁶⁷ Ibid. para. 20.

³⁶⁸ United States' second written submission, para. 52; response to Panel question No. 44, paras. 104-108.

³⁶⁹ United States' second written submission, para. 52.

³⁷⁰ United States' first written submission, paras. 116-124; second written submission, para. 20.

³⁷¹ Australia's third-party submission, paras. 10 and 21; third-party statement, paras. 10-12; response to Panel question No. 5.

³⁷² Australia's response to Panel question No. 5.

the beneficiaries of the subsidy, or whether it can be characterized instead as a requirement to use domestic over imported goods as a condition for the subsidy.³⁷³ Australia argues that it is unclear how the European Union reaches the conclusion that the First and the Second Siting Provisions are expressly conditioned on the use of domestic over imported goods.³⁷⁴ According to Australia, it is doubtful whether the European Union has successfully made a case for a *de jure* breach of Article 3.1(b) of the SCM Agreement; the Panel's determination in the present case may ultimately depend on the finding of facts.³⁷⁵ Australia encourages the Panel to consider whether the references to wings and fuselages in the First and the Second Siting Provisions can be regarded as merely defining the beneficiary of the subsidies, instead of being a requirement to use domestically produced goods.³⁷⁶ In response to a question from the Panel, Australia submits that the Appellate Body's rulings in *US – Softwood Lumber IV* cannot be interpreted as stating that "goods" in Article 3.1(b) of the SCM Agreement must be tradeable or capable of being traded. In Australia's view, such an interpretation would not be practical and would undermine the object and purpose of the SCM Agreement.³⁷⁷

7.187. Brazil argues that Article 3.1(b) of the SCM Agreement does not cover production requirements, as long as these requirements do not constitute requirements to use domestic goods to the detriment of imported goods.³⁷⁸ According to Brazil, the SCM Agreement does not prohibit WTO Members from providing subsidies to producers contingent on the performance of production steps of a certain good in their territories. Such a production requirement could fall upon the production of either a final or an intermediate good.³⁷⁹ In Brazil's view, the expression "use" in Article 3.1(b) means that the goods in question must be "products" that can be "used" in a commercial context.³⁸⁰ Brazil adds that "contingency" under Article 3.1(b) requires concrete evidence of the actual requirement to use domestic products to the detriment of imported products and cannot be based simply on a measure's incidental or indirect impact on domestic production, such as the fact that domestic products may become more attractive to the producer and lead to a larger share of domestic products as inputs.³⁸¹ According to Brazil, a subsidy can be prohibited under Article 3.1(b) because the terms of the subsidy expressly condition its granting on the use of domestic inputs or otherwise the necessary implication of the specific conditions is such that, absent the use of domestic goods, the conditions cannot be met.³⁸² Brazil maintains that, in the latter case, a panel would have to examine the specific requirements imposed as a condition for the granting of the subsidy, based on the text of the subsidy programme and on its necessary implications, and determine whether the conditions can be met without using domestic goods.³⁸³ Brazil asserts that a subsidy on the production of a certain good, with requirements on the performance of production steps along the production chain, would not be considered *de jure* contingent on the use of domestic over imported goods under the purview of Article 3.1(b) of the SCM Agreement.³⁸⁴ Conversely, a subsidy could be found *de facto* to be prohibited under Article 3.1(b) when a condition does not necessarily require the use of domestic goods either directly or by necessary implication, but based on the total configuration of the facts it becomes clear that, in fact, the subsidy recipient is required to use domestic over imported goods in order to receive the subsidy.³⁸⁵ Brazil submits that, in the present case, the Panel will have to assess whether the conditions contained in the challenged measure simply require a domestic production activity by the producer (which would likely not amount to a prohibited conditionality) or if instead: (i) the condition requires *de jure* and by necessary implication the use of domestic over imported goods; or (ii) the condition, in combination with other factual evidence on the record, requires *de facto* the use of domestic over imported inputs.³⁸⁶

³⁷³ Australia's third-party submission, paras. 11-13.

³⁷⁴ Australia's third-party statement, para. 6.

³⁷⁵ Ibid. para. 7.

³⁷⁶ Ibid. para. 13.

³⁷⁷ Australia's response to Panel question No. 4.

³⁷⁸ Brazil's third-party submission, paras. 7-8. See also Brazil's response to Panel question No. 5.

³⁷⁹ Brazil's response to Panel question No. 5.

³⁸⁰ Brazil's third-party submission, para. 9; third-party statement, para. 7.

³⁸¹ Brazil's third-party submission, paras. 10-14; third-party statement, paras. 6 and 9.

³⁸² Brazil's third-party submission, paras. 16; third-party statement, para. 10.

³⁸³ Brazil's third-party submission, para. 17.

³⁸⁴ Brazil's response to Panel question No. 12. See also Brazil's response to Panel question No. 14.

³⁸⁵ Brazil's third-party submission, paras. 18; third-party statement, para. 11.

³⁸⁶ Brazil's third-party submission, para. 19.

7.188. According to Canada, the European Union appears to be arguing that a subsidy is contingent on the use of domestic over imported goods where the producer of a final good is required to produce certain components of that good in order to receive the subsidy.³⁸⁷ In Canada's view, this interpretation of Article 3.1(b) would improperly extend the provision to cover situations where subsidy recipients are required to produce goods.³⁸⁸ According to Canada, under the challenged measure, the beneficiary company is required to manufacture and/or assemble those fuselages and wings itself in order to receive the tax subsidy.³⁸⁹ There is no requirement to purchase in the United States wings, fuselages, or other parts used in the assembly of the final aircraft.³⁹⁰ Canada adds that the European Union did not provide any evidence suggesting that Boeing would *de facto* have to "use" domestic components other than those that the company manufactures itself.³⁹¹ Canada argues that WTO Members are not prohibited from providing subsidies to domestic producers, including where the subsidy to the producer of a final good is contingent on the recipient producing goods in its territory or producing certain intermediate goods by itself.³⁹² Similarly, in Canada's view, neither the GATT 1994 nor the SCM Agreement limits a Member's ability to define the level of production required for subsidy eligibility purposes.³⁹³ Otherwise, production requirements would have to be limited to simple assembly operations, and the right of WTO Members to require subsidy recipients to produce goods, as defined by the granting Member, in order to receive a subsidy would be nullified.³⁹⁴

7.189. China contends that the Panel must examine whether, under the First Siting Provision and the Second Siting Provision, the subsidy is conditional or dependent on the use of domestic over imported goods.³⁹⁵ China disagrees with the United States' assertion that fuselages and wings are not "goods".³⁹⁶ In China's view, custom-tailored goods can also be considered as "goods" within the meaning of Article 3.1(b) of the SCM Agreement. China also disagrees with the notion that Article 3.1(b) requires that the relevant good is traded in practice, as long as the good has "the value of trading".³⁹⁷ According to China, the "use" of intermediate goods in the course of production may meet the condition for being considered a "use" of domestic over imported goods.³⁹⁸ The Panel should consider in this regard whether the conditions imposed by the challenged measure result in a *de facto* situation in which the 777X aircraft programme prefers domestic components or other intermediate goods over imported goods.³⁹⁹ China also argues that Article III:8(b) of the GATT 1994 is not relevant to the present dispute as a legal basis to exclude the challenged measure from examination under Article 3.1(b) of the SCM Agreement.⁴⁰⁰ In China's view, there seems to be insufficient evidence that the First Siting Provision would result *de jure* in a prohibited subsidy under Article 3.1(b) of the SCM Agreement.⁴⁰¹ China argues however that the Panel should examine whether *de facto* the First Siting Provision has created an incentive for the use of domestic components over imported components, taking into account that this provision may make it more favourable to purchase, in the state of Washington, the components for the fuselages and wings to be used in the assembly of 777X aircraft.⁴⁰² Likewise, China suggests that the Panel should assess whether the Second Siting Provision should be considered *de jure* as a prohibited subsidy under Article 3.1(b) of the SCM Agreement or otherwise whether

³⁸⁷ Canada's third-party submission, para. 3.

³⁸⁸ Ibid.

³⁸⁹ Ibid. paras. 4-5.

³⁹⁰ Ibid. para. 5.

³⁹¹ Ibid.

³⁹² Ibid. 6-7.

³⁹³ Ibid. paras. 8-10.

³⁹⁴ Ibid. paras. 8 and 11.

³⁹⁵ China's third-party submission, para. 18.

³⁹⁶ China's third-party statement, para. 3.

³⁹⁷ China's third-party submission, para. 21; third-party statement, para. 3; response to Panel question

No. 4.

³⁹⁸ China's third-party statement, para. 4.

³⁹⁹ China's third-party submission, para. 23.

⁴⁰⁰ China's third-party submission, para. 25; third-party statement, para. 5. See also China's response to Panel question Nos. 5 and 15.

⁴⁰¹ China's third-party submission, para. 28; third-party statement, para. 7; response to Panel question No. 5.

⁴⁰² China's third-party submission, paras. 29-30; third-party statement, para. 8; response to Panel question No. 5.

de facto it may result in an incentive to use more domestic than imported components due to cost savings and efficiencies.⁴⁰³

7.190. Japan argues that the same legal standard should be followed by panels when examining prohibited subsidies under Article 3.1(a) and under Article 3.1(b) of the SCM Agreement, as well as when examining *de jure* and *de facto* contingency.⁴⁰⁴ With respect to the evidentiary standard for the establishment of contingency, Japan states that a *de jure* analysis should be based on the words actually used in the measure at issue and their necessary implications, while a *de facto* analysis should be based on the total configuration of the facts constituting and surrounding the granting of the subsidy in light of the available evidence, rather than on subjective motivations expressed by governmental agencies, officials or legislators.⁴⁰⁵ In Japan's view, a subsidy contingent on the use of domestic goods that is prohibited by Article 3.1(b) of the SCM Agreement cannot be justified by Article III:8(b) of the GATT 1994.⁴⁰⁶ According to Japan, it appears that the European Union has argued that the challenged subsidy is *de jure* contingent on the use of domestic over imported goods, but has based its analysis on "factual scenarios which may or may not have materialized, factual circumstances that may or may not have existed, and choices that private actors may or may not have made", instead of focusing on the actual text of the measure.⁴⁰⁷ With respect to the First Siting Provision, Japan asserts that a law stating that a subsidy is contingent upon the domestic *siting* of a certain programme is different from a law stating that a subsidy is contingent upon the *use of* a domestic product.⁴⁰⁸ With respect to the Second Siting Provision, Japan asserts that the words used in the legislation are not completely clear as to whether, by virtue of the location requirement for the final assembly or wing assembly, the revenue from the 777X will not benefit from the reduced B&O tax rate if these assembling activities take place outside Washington State.⁴⁰⁹ In Japan's view, the European Union's analysis with respect to both the First Siting Provision and the Second Siting Provision may fall short of the standard required to establish "contingency" under Article 3.1(b) of the SCM Agreement.⁴¹⁰

7.5.3 Order of analysis

7.191. As noted above, the European Union has argued that its "first and principal claim in this dispute" is that the challenged aerospace tax measures are *de jure* contingent upon the use of domestic over imported goods.⁴¹¹

7.192. The Panel will start by considering the European Union's *de jure* claim. As explained below, the Panel will assess whether the European Union has made a *prima facie* case that the contingency of the challenged aerospace tax measures upon the use of domestic over imported goods can be demonstrated on the basis of the words of the relevant legislation. This could be either because the conditionality is set out expressly in the legislation or because such conditionality can clearly be derived, by necessary implication, from the words used in the legislation.⁴¹²

7.193. The European Union has also advanced a secondary claim, i.e. that the tax measures at issue are inconsistent with Article 3.1(b) of the SCM Agreement by being *de facto* contingent upon the use of domestic over imported goods. If the Panel were to conclude that the European Union has successfully established that the aerospace tax measures are *de jure* contingent upon the use of domestic over imported goods, and therefore inconsistent with Article 3.1(b) of the SCM Agreement, it would not need also to establish that the same measures are *de facto* contingent. Nonetheless, in that circumstance the Panel will try to ensure that there is a complete factual record on which the Appellate Body may base its rulings in the event of an appeal.

⁴⁰³ China's third-party submission, paras. 32-33.

⁴⁰⁴ Japan's third-party submission, paras. 2-8; third-party statement, paras. 3-5.

⁴⁰⁵ Japan's third-party submission, paras. 2 and 11-21; third-party statement, paras. 6-11.

⁴⁰⁶ Japan's response to Panel question No. 5.

⁴⁰⁷ Japan's third-party submission, para. 12.

⁴⁰⁸ Japan's third-party submission, para. 22; third-party statement, para. 13.

⁴⁰⁹ Japan's third-party statement, para. 14.

⁴¹⁰ Japan's third-party submission, paras. 27-28; third-party statement, para. 12.

⁴¹¹ European Union's second written submission, para. 2. See also *ibid.* paras. 41, 85 and 90; European Union's closing statement at the first meeting of the Panel, paras. 1 and 11; response to Panel question No. 29, para. 67.

⁴¹² See para. 7.274 below.

7.194. Conversely, if the Panel finds that the European Union has not established its *de jure* claim, it will subsequently consider the European Union's *de facto* claim, which the European Union makes on a secondary and alternative basis. In analysing the *de facto* claim, the Panel would consider the total configuration of the facts constituting and surrounding the granting of the subsidy. As explained below⁴¹³, this would include considering (i) the design and structure of the measures granting the subsidies; (ii) the modalities of operation set out in such measures; and (iii) the relevant factual circumstances surrounding the granting of the subsidies that provide the context for understanding the measures' design, structure, and modalities of operation.

7.5.4 Article 3.1(b) of the SCM Agreement

7.5.4.1 Prohibited subsidies

7.195. Article 3.1 of the SCM Agreement reads as follows:

Except as provided in the Agreement on Agriculture, the following subsidies, within the meaning of Article 1, shall be prohibited:

(a) subsidies contingent, in law or in fact⁴, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I⁵;

(b) subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods.

(footnotes original) ⁴ This standard is met when the facts demonstrate that the granting of a subsidy, without having been made legally contingent upon export performance, is in fact tied to actual or anticipated exportation or export earnings. The mere fact that a subsidy is granted to enterprises which export shall not for that reason alone be considered to be an export subsidy within the meaning of this provision.

⁵ Measures referred to in Annex I as not constituting export subsidies shall not be prohibited under this or any other provision of this Agreement.

7.196. Only those subsidies that meet the definition in Article 1 of the SCM Agreement and fall within the description of either Article 3.1(a) or 3.1(b), commonly referred to as "export subsidies" and "import substitution subsidies", respectively, are prohibited by the SCM Agreement. As noted by the Appellate Body:

Only those subsidies that are conditioned on export performance or on import substitution are prohibited *per se* under Article 3 of Part II of the *SCM Agreement*. In contrast, all other subsidies are allowed under the *SCM Agreement*, albeit a Member granting such subsidies should not cause, through the use of the subsidies, adverse effects within the meaning of Article 5 of Part III, in which case it must remove the adverse effects or must withdraw the subsidies themselves.⁴¹⁴ (original italics)

7.197. Pursuant to Article 3.2 of the SCM Agreement, "[a] Member shall neither grant nor maintain [prohibited subsidies]".

7.198. Prohibited subsidies are a special category of subsidies, which Members have deemed to create such trade distortions that they are proscribed without the need for a complaining Member to show any adverse effects.⁴¹⁵ As noted by the panel in *Brazil – Aircraft*, these subsidies "are specifically designed to affect trade".⁴¹⁶

⁴¹³ See para. 7.329 below.

⁴¹⁴ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1054.

⁴¹⁵ The Appellate Body has explained that "the granting of a subsidy is not, in and of itself, prohibited under the *SCM Agreement*. Nor does granting a 'subsidy', without more, constitute an inconsistency with that Agreement. The universe of subsidies is vast. Not all subsidies are inconsistent with the *SCM Agreement*. The

7.5.4.2 Article III:8(b) of the GATT 1994

7.199. The United States has argued that Article III:8(b) of the GATT 1994 provides context for the interpretation of Article 3.1(b) of the SCM Agreement.⁴¹⁷ Article III:8(b) is part of Article III of the GATT 1994, the provision dealing with the obligation of national treatment on internal taxation and regulation. As noted by the Appellate Body:

The broad and fundamental purpose of Article III is to avoid protectionism in the application of internal tax and regulatory measures. More specifically, the purpose of Article III "is to ensure that internal measures 'not be applied to imported or domestic products so as to afford protection to domestic production'".⁴¹⁸ Toward this end, Article III obliges Members of the WTO to provide equality of competitive conditions for imported products in relation to domestic products.^{419, 420}

7.200. Notwithstanding the above, according to Article III:8(b):

The provisions of this Article [Article III of the GATT 1994] shall not prevent the payment of subsidies exclusively to domestic producers, including payments to domestic producers derived from the proceeds of internal taxes or charges applied consistently with the provisions of this Article and subsidies effected through governmental purchases of domestic products.

7.201. By its terms, Article III:8(b) of the GATT 1994 applies to the national treatment disciplines under Article III of the GATT 1994, which are not at issue in this dispute, and clarifies that the provision of subsidies exclusively to domestic producers is not in itself a breach of the national treatment obligation. To the extent that Article III:8(b) provides interpretive guidance in the present case, it is consistent with the principle under the SCM Agreement that subsidization in itself is not prohibited, but only becomes so in two particular situations – one of which is a contingency on the use of domestic over imported goods.⁴²¹

7.5.4.3 Contingency

7.202. Returning to the specific text of Article 3.1(b), the expression "contingent ... upon" is common to Articles 3.1(a) and 3.1(b) of the SCM Agreement. Article 3.1(a) prohibits subsidies that are contingent upon export performance, while Article 3.1(b) prohibits those subsidies that are contingent upon the use of domestic over imported goods.

7.203. The expression "contingent ... upon" is used in both Article 3.1(a) and Article 3.1(b). This expression has been found to have the same meaning in both provisions.⁴²² The expression "contingent ... upon" has been explored in greatest detail in disputes concerning allegations of export subsidies under Article 3.1(a). In this context, the Appellate Body has noted:

In our view, the key word in Article 3.1(a) is "contingent". As the Panel observed, the ordinary connotation of "contingent" is "conditional" or "dependent for its existence on something else". This common understanding of the word "contingent" is borne out by the text of Article 3.1(a), which makes an explicit link between "contingency" and

only 'prohibited' subsidies are those identified in Article 3 of the *SCM Agreement*". Appellate Body Report, *Canada – Aircraft (Article 21.5 – Brazil)*, para. 47.

⁴¹⁶ Panel Report, *Brazil – Aircraft*, para. 7.26.

⁴¹⁷ See, for example, United States' first written submission, paras. 9 and 116-123; second written submission, paras. 9, 20 and 47; opening statement at the first meeting of the Panel, para. 19; opening statement at the second meeting of the Panel, para. 16.

⁴¹⁸ (footnote original) United States – Section 337 of the Tariff Act of 1930, BISD 36S/345, para. 5.10.

⁴¹⁹ (footnote original) United States – Taxes on Petroleum and Certain Imported Substances, BISD 34S/136, para. 5.1.9; Japan – Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages, BISD 34S/83, para. 5.5(b).

⁴²⁰ Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 16, DSR 1996:I, 97, at p. 109.

⁴²¹ See Panel Report, *Indonesia – Autos*, para. 14.33.

⁴²² Appellate Body Report, *Canada – Autos*, para. 123.

"conditionality" in stating that export contingency can be the sole or "one of several other *conditions*".⁴²³ (emphasis original)

7.204. Regarding the interpretation of the term "contingent" in the context of an export subsidy, the Panel in *Australia – Automotive Leather II* referred to a "close connection" between the grant or maintenance of a subsidy and export performance. It added that for a subsidy to be export contingent, it must be "conditioned" upon export performance, stating:

An inquiry into the meaning of the term "contingent..." in Article 3.1(a) must, therefore, begin with an examination of the ordinary meaning of the word "contingent". The ordinary meaning of "contingent" is "dependent for its existence on something else", "conditional; dependent on, upon".⁴²⁴

7.205. In *Canada – Autos*, the Appellate Body referred back to this earlier statement and held that "this legal standard applies not only to 'contingency' under Article 3.1(a), but also to 'contingency' under Article 3.1(b)".⁴²⁵

7.206. The Appellate Body has also clarified that Article 3.1(b) covers not only *de jure* contingency, but also *de facto* contingency. In *Canada – Autos*, the Appellate Body reversed a panel ruling that had limited "contingency" under Article 3.1(b) to *de jure* contingency:

[W]e believe that the Panel erred in finding that Article 3.1(b) does not extend to subsidies contingent "in fact" upon the use of domestic over imported goods. We, therefore, reverse the Panel's broad conclusion that "Article 3.1(b) extends only to contingency in law."⁴²⁶

7.207. In the context of Article 3.1(a), the Appellate Body has noted that contingency "in law" (*de jure*) is demonstrated "on the basis of the words of the relevant legislation, regulation or other legal instrument".⁴²⁷ The Appellate Body has added that "such conditionality can [also] be derived by necessary implication from the words actually used in the measure".⁴²⁸

7.208. Given that "contingent ... upon" has the same meaning in Article 3.1(b) as it does in Article 3.1(a), a conclusion that a subsidy is *de jure* contingent upon the use of domestic over imported goods is to be based on the words of the relevant legislation, as well as their necessary implication. This would require a finding that:

[T]he existence of that condition can be demonstrated on the basis of the very words of the relevant legislation, regulation or other legal instrument constituting the measure. The simplest, and hence, perhaps, the uncommon, case is one in which the condition ... is set out expressly, in so many words, on the face of the law, regulation or other legal instrument. We believe, however, that a subsidy is also properly held to be *de jure* ... contingent where the condition ... is clearly, though implicitly, in the instrument comprising the measure. Thus, for a subsidy to be *de jure* ... contingent, the underlying legal instrument does not always have to provide *expressis verbis* that the subsidy is available only upon fulfillment of the condition ... Such conditionality can also be derived by *necessary implication* from the words actually used in the measure.⁴²⁹ (emphasis added)

7.209. With respect to *de facto* contingency, in the context of Article 3.1(a) of the SCM Agreement, the Appellate Body has stated that "the evidence needed to establish *de facto* ...

⁴²³ Appellate Body Report, *Canada – Aircraft*, para. 166.

⁴²⁴ Panel Report, *Australia – Automotive Leather II*, para. 9.55.

⁴²⁵ Appellate Body Report, *Canada – Autos*, para. 123.

⁴²⁶ *Ibid.* para. 143.

⁴²⁷ Appellate Body Report, *Canada – Aircraft*, para. 167. See also Appellate Body Reports, *Canada – Autos*, para. 123; *EC and certain member States – Large Civil Aircraft*, para. 1038.

⁴²⁸ Appellate Body Report, *Canada – Autos*, para. 123. See also *ibid.* para. 100; and Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1038.

⁴²⁹ Appellate Body Report, *Canada – Autos*, para. 100. See also Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.365 and Panel Report, *US – FSC (Article 21.5 – EC)*, paras. 8.54-8.56.

contingency goes beyond a legal instrument and includes a variety of factual elements concerning the granting of the subsidy in a specific case"⁴³⁰:

Proving *de facto* ... contingency is a much more difficult task. There is no single legal document which will demonstrate, on its face, that a subsidy is "contingent ... in fact...". Instead, the existence of this relationship of contingency, between the subsidy and ... performance, must be *inferred* from the total configuration of the facts constituting and surrounding the granting of the subsidy, none of which on its own is likely to be decisive in any given case.⁴³¹ (emphasis original)

7.210. Still referring to contingency upon export performance under Article 3.1(a), the Appellate Body has stated that "the standard for *de facto* ... contingency ... would be met when the subsidy is granted so as to provide an incentive to the recipient to export in a way that is not simply reflective of the conditions of supply and demand in the domestic and export markets undistorted by the granting of the subsidy."⁴³² The Appellate Body has further noted that:

The existence of *de facto* export contingency, as set out above, "must be *inferred* from the total configuration of the facts constituting and surrounding the granting of the subsidy"⁴³³, which may include the following factors: (i) the design and structure of the measure granting the subsidy; (ii) the modalities of operation set out in such a measure; and (iii) the relevant factual circumstances surrounding the granting of the subsidy that provide the context for understanding the measure's design, structure, and modalities of operation.⁴³⁴ (emphasis original)

7.211. Moreover, the Appellate Body has ruled as follows:

[T]he conditional relationship between the granting of the subsidy and export performance must be objectively observable on the basis of such evidence in order for the subsidy to be geared to induce the promotion of future export performance by the recipient. The standard for *de facto* ... contingency is therefore not satisfied by the subjective motivation of the granting government ... In this respect, we note that the Appellate Body and panels have, on several occasions, cautioned against undue reliance on the intent of a government behind a measure to determine the WTO-consistency of that measure.⁴³⁵ The Appellate Body has found that "the intent, stated or otherwise, of the legislators is *not conclusive*" as to whether a measure is consistent with the covered agreement.⁴³⁶ In our view, the same understanding applies in the context of a determination on ... contingency, where the requisite conditionality ... must be established on the basis of objective evidence, rather than subjective intent. We note, however, that while the standard for *de facto* ... contingency cannot be satisfied by the subjective motivation of the granting government, objectively reviewable expressions of a government's policy objectives for granting a subsidy may, however, constitute relevant evidence in an inquiry into whether a subsidy is *geared to induce* the promotion of future export performance by the recipient.⁴³⁷ (emphasis added)

⁴³⁰ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1038.

⁴³¹ Appellate Body Report, *Canada – Aircraft*, para. 167. See also Appellate Body Reports, *Canada – Autos*, para. 123; *EC and certain member States – Large Civil Aircraft*, para. 1038.

⁴³² Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1045.

⁴³³ (footnote original) Appellate Body Report, *Canada – Aircraft*, para. 167. (original emphasis)

⁴³⁴ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1046.

⁴³⁵ (footnote original) For example, in the context of a discrimination claim under Article III of the GATT 1994, the Appellate Body found that "[i]t is not necessary for a panel to sort through the many reasons legislators and regulators often have for what they do and weigh the relative significance of those reasons to establish legislative or regulatory intent." (Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 27, DSR 1996:I, 97, at 119) Moreover, "there may well be a certain degree of speculation in seeking to establish the intent of a government in the abstract." (Panel Report, *Japan – DRAMs (Korea)*, para. 7.104)

⁴³⁶ (footnote original) Appellate Body Report, *US – Offset Act (Byrd Amendment)*, para. 259. (emphasis added) See also Appellate Body Report, *China – Auto Parts*, para. 178, where the Appellate Body found that the intent, stated or otherwise, of the legislators is not conclusive as to the characterization of a measure.

⁴³⁷ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1050.

7.212. In sum, the Panel takes note of the Appellate Body's findings in prior disputes that "contingency" has the same meaning in Article 3.1(a) and Article 3.1(b) of the SCM Agreement, and that the contingency in Article 3.1(b) can be established on a *de jure* as well as on a *de facto* basis. The Panel shall be guided by these findings in its analysis.

7.5.4.4 Other interpretive issues

7.213. The parties have advanced contrasting arguments regarding the interpretation of certain terms in Article 3.1(b) of the SCM Agreement.

7.5.4.4.1 The term "over"

7.214. Both the European Union and the United States note that the word "over" used in Article 3.1(b) of the SCM Agreement, in the expression "subsidies contingent ... upon the use of domestic *over* imported goods", is defined in the dictionary as "in preference to", "in excess of", or "more than".⁴³⁸

7.215. The United States notes that the expressions equivalent to the word "over" that are used in the French and the Spanish texts of Article 3.1(b) are "*de préférence à*" and "*con preferencia a*", which would be equivalent to the English expression "in preference to" or "instead of".⁴³⁹ Thus, according to the United States:

[A] subsidy that is inconsistent with Article 3.1(b) requires the use of domestic goods "in preference to," *i.e.*, instead of, imported goods. For this reason, Article 3.1(b) is often referred to as relating to "import substitution subsidies."⁴⁴⁰ It does not cover measures simply because they involve some sort of domestic activity, but rather it is focused specifically on subsidies that depend on the substitution of domestic over imported goods.⁴⁴¹

7.216. The European Union argues that, based on its ordinary meaning, the word "over" in Article 3.1(b) should be interpreted as "in excess of".⁴⁴² The European Union recalled that the expression "in excess of" is used in other provisions of the WTO Agreements (such as Articles II:1(b) and III:2 of the GATT 1994) and has been interpreted by previous panels and the Appellate Body as excluding a *de minimis* standard.⁴⁴³ Based on its proposed meaning of the word "over", the European Union argues that there is no *de minimis* standard for discrimination in Article 3.1(b) of the SCM Agreement. According to the European Union, "[a]s soon as a subsidy is contingent upon the use of domestic over imported goods, competitive opportunities between domestic and imported goods are distorted, even if no such goods are currently imported".⁴⁴⁴

7.217. As clarified subsequently, the parties have no real discrepancy with respect to the meaning of the word "over" in Article 3.1(b) for the purpose of this dispute. The European Union has noted that it "does not disagree with the United States' legal interpretation of 'over'".⁴⁴⁵ The United States has noted in turn that none of the parties has argued that there is a *de minimis* exception in Article 3.1(b), so that there is no need for the Panel to address the question of whether such an exception exists.⁴⁴⁶

⁴³⁸ European Union's response to Panel question No. 32, para. 72; United States' second written submission, para. 25; United States' response to Panel question No. 32, para. 68. See also Japan's third-party submission, fn 5; *Shorter Oxford English Dictionary*, 5th edition, Volume 2, p. 2044 (Exhibit USA-15); and *Shorter Oxford English Dictionary*, 6th edition, pp. 2044-2045 (Exhibit USA-51).

⁴³⁹ United States' second written submission, para. 25; response to Panel question No. 32, para. 68. See also European Union's second written submission, para. 52.

⁴⁴⁰ (footnote original) See, e.g., Canada – Renewable Energy (AB), para. 5.6.

⁴⁴¹ United States' response to Panel question No. 32, para. 68. See also United States' second written submission, para. 25.

⁴⁴² European Union's response to Panel question No. 32, para. 77; second written submission, para. 51.

⁴⁴³ European Union's response to Panel question No. 32, paras. 73-76.

⁴⁴⁴ European Union's response to Panel question No. 32, para. 77; second written submission, paras. 50-51.

⁴⁴⁵ European Union's second written submission, para. 52.

⁴⁴⁶ United States' second written submission, para. 28.

7.218. In any event, the Panel notes the ordinary meaning of the word over, namely "[a]bove in degree, quality, or action; in preference to; more than".⁴⁴⁷ In Article 3.1(b), the term "over" appears in the context of a prohibition on subsidies that are conditional upon the use of domestic over imported products. As noted above, the purpose of this provision is to prohibit certain subsidies that have been considered particularly trade-distorting by Members. In this context, the word "over" in Article 3.1(b) can be read in the sense of "in preference to" (or "instead of" or "rather than")⁴⁴⁸, so that this provision prohibits any subsidy that is conditional on the use of domestic goods in preference to (or "instead of" or "rather than") imported goods.

7.5.4.4.2 The term "use"

7.219. Article 3.1(b) refers to subsidies contingent upon the *use* of domestic over imported goods. According to the United States, "[t]he term 'use' [in Article 3.1(b)] refers to either the act of using an input to produce a downstream good, or the use of a finished good by the end-user".⁴⁴⁹ The United States refers to footnote 61 of the SCM Agreement in Annex II ("Guidelines on Consumption of Inputs in the Production Process") as "mak[ing] clear that 'use' means the consumption of goods ... as inputs into a production process".⁴⁵⁰ This is related to the United States' argument that separate wings and fuselages are elements of the finished aircraft and will not be "used" in the production of 777X airplanes.⁴⁵¹

7.220. Conversely, the European Union argues that the term "use" in Article 3.1(b) is broad enough to "encompass situations where the input is 'used' in such a way that it has not been consumed and where it remains a discrete, identifiable part of the whole."⁴⁵² In the European Union's view, the term "use" is not limited to situations where an input is consumed in the production process, or merely attached to a final product.⁴⁵³

7.221. The Appellate Body has examined the ordinary meaning of the term "use" in the context of a different provision of the SCM Agreement, namely Article 2.1(c) ("use of a subsidy programme by a limited number of certain enterprises"). In this respect, the Appellate Body noted that "[t]he word 'use' refers to the action of using or employing something" and cited the following dictionary definition of the term: "the action of using something; the fact or state of being used; application or conversion to some purpose".⁴⁵⁴ The Appellate Body also noted that, in the context of Article 2.1(c), "what is used or employed is 'a subsidy programme'".⁴⁵⁵ The Panel observes that term "use", referring to products, appears in several other provisions in the SCM Agreement and in other covered agreements.⁴⁵⁶

⁴⁴⁷ "Over", 11, *Shorter Oxford English Dictionary*, 6th edition (2007), Vol. 2, p. 2048.

⁴⁴⁸ This is also the meaning that best reconciles the language used in the three authentic versions of the SCM Agreement. The French text of Article 3.1(b) reads: "subventions subordonnées ... à l'utilisation de produits nationaux *de préférence* à des produits importés". The Spanish text reads: "las subvenciones supeditadas al empleo de productos nacionales *con preferencia* a los importados..." (emphasis added)

⁴⁴⁹ United States' response to Panel question No. 44, para. 104.

⁴⁵⁰ Ibid. para. 105. Footnote 61 of the SCM Agreement provides as follows: "Inputs consumed in the production process are inputs physically incorporated, energy, fuels and oil *used* in the production process and catalysts which are consumed in the course of their *use* to obtain the exported product." (emphasis added)

⁴⁵¹ United States' first written submission, paras. 110-115; second written submission, paras. 52-55; opening statement at the first meeting of the Panel, paras. 8-10; United States' response to Panel question No. 44, para. 108.

⁴⁵² European Union's opening statement at the second meeting of the Panel, para. 30.

⁴⁵³ European Union's response to Panel question No. 44, para. 102.

⁴⁵⁴ Appellate Body Report, *US – Carbon Steel (India)*, para. 4.374 and fn 1009. See also European Union's response to Panel question No. 44, paras. 103-105.

⁴⁵⁵ Appellate Body Report, *US – Carbon Steel (India)*, para. 4.374.

⁴⁵⁶ See, for example, fn 29 to Article 8.2 of the SCM Agreement ("the translation of industrial research findings into a plan, blueprint or design for new, modified or improved products, processes or services whether intended for sale or *use*..."); item (d) of Annex I to the SCM Agreement ("[t]he provision by governments or their agencies ... of imported or domestic products or services for *use* in the production of exported goods..."); item (h) of Annex I to the SCM Agreement ("[t]he exemption, remission or deferral of prior-stage cumulative indirect taxes on goods or services *used* in the production of exported products..."); para. II.3 of Annex II to the SCM Agreement ("[i]nvestigating authorities should treat inputs as physically incorporated if such inputs are *used* in the production process and are physically present in the product exported..."); Article III:1 of the GATT 1994 ("internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or *use* of products, and internal quantitative regulations requiring the mixture, processing or *use* of products in specified amounts or

7.222. In Article 3.1(b), the term "use" appears in the context of a prohibition on subsidies that are conditional upon the *use* of domestic over imported goods. The purpose of this provision is to prohibit certain subsidies that have been considered particularly trade-distorting by Members. The Panel finds that the ordinary meaning of the word, namely the action of using or employing something, is apt in the context of Article 3.1(b). Neither the text of Article 3.1(b) nor any relevant context indicates that the term "use" is confined to a particular manner of using or employing a given good, or that the good "used" in this context must possess certain characteristics in order to be capable of being "used" within the meaning of Article 3.1(b). Accordingly, a subsidy conditional on the consumption of domestic goods, rather than or in preference to imported goods, as inputs into a production process would be covered by Article 3.1(b), but so too would a subsidy that is conditional in any other way on the use or employment of domestic goods, rather than or in preference to imported goods.

7.5.4.4.3 The term "goods"

7.223. The United States submits that the word "goods" in Article 3.1(b) of the SCM Agreement, in the expression "subsidies contingent ... upon the use of domestic over imported *goods*", refers to something that is saleable or tradeable.⁴⁵⁷ The United States points to the dictionary definition of "goods" as "saleable commodities, merchandise, wares"⁴⁵⁸ The United States also notes that the words used in the French and the Spanish texts of Article 3.1(b) are "*produits*" and "*productos*", respectively, both of which connote saleable commodities, merchandise, or wares.⁴⁵⁹ The United States further notes that in Article 3.1(b) of the SCM Agreement the word "goods" is qualified by the word "imported" (as well as by the word "domestic") and an imported good would be one that by definition is traded.⁴⁶⁰ The United States concludes that "goods", within the meaning of Article 3.1(b), must be understood as being products that are traded; if they are not, they cannot be imported, which would be inconsistent with the specific reference to "imported goods" in Article 3.1(b).⁴⁶¹

7.224. The European Union agrees with the United States that the French and the Spanish texts confirm the interpretation that the word "goods" in Article 3.1(b) of the SCM Agreement is synonymous with the word "products".⁴⁶² The European Union, however, does not agree that the definition of "goods" should be limited to those products which are actually traded.⁴⁶³ In the European Union's view, the approach advocated by the United States would run against a fundamental principle of the disciplines on trade in goods: that these disciplines protect competitive opportunities (and not just actual trade volumes), including the potential to compete, even absent actual trade in the goods concerned.⁴⁶⁴ According to the European Union, the interpretation advocated by the United States would open up an easy path for circumventing the subsidy disciplines under Article 3.1(b) of the SCM Agreement⁴⁶⁵ and would defeat the purpose of Article 3.1(b) by affording impunity to the most distortive subsidies: those that successfully

proportions..."); para. 1(a) of the Annex to the Agreement on Trade-Related Investment Measures ("the purchase or *use* by an enterprise of products of domestic origin or from any domestic source..."); para. 2 of the Annex to the Agreement on Civil Aircraft ("the products covered by the descriptions listed below ... shall be accorded duty-free or duty-exempt treatment, if such products are for *use* in civil aircraft or ground flying trainers and for incorporation therein, in the course of their manufacture, repair, maintenance, rebuilding, modification or conversion..."). (emphasis added)

⁴⁵⁷ United States' first written submission, paras. 105 and 125-128; second written submission, paras. 22-23.

⁴⁵⁸ United States' first written submission, para. 126 (citing Appellate Body Report, *US – Softwood Lumber IV*, para. 58 & fn 43, which in turn cites *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. I, p. 1116).

⁴⁵⁹ United States' first written submission, para. 126 (citing *Le Nouveau Petit Robert*, 2009, pp. 2034-2035 (Exhibit USA-28) and *Diccionario de la Lengua Española*, 2001, pp. 1839-1840 (Exhibit USA-29)).

⁴⁶⁰ United States' first written submission, para. 126 (citing Appellate Body Report, *US – Softwood Lumber IV*, para. 62). See also United States' second written submission, para. 22.

⁴⁶¹ United States' first written submission, para. 128.

⁴⁶² European Union's second written submission, para. 46.

⁴⁶³ *Ibid.*

⁴⁶⁴ *Ibid.* (citing Panel Reports, *Korea – Alcoholic Beverages*, para. 10.81; *Colombia – Ports of Entry*, para. 7.356; *US – Poultry (China)*, paras. 7.424-7.427 and 7.429; and *Indonesia – Autos*, para. 14.113; and Appellate Body Report, *Canada – Periodicals*, pp. 20-21, DSR 1997:I, 449, 466-467. See also European Union's response to Panel question No. 33, para. 85.

⁴⁶⁵ European Union's second written submission, para. 49 (citing Japan's response to Panel question No. 4, para. 4).

eliminate competing foreign products from the market.⁴⁶⁶ The European Union submits that a challenge under Article 3.1(b) should be evaluated in view of the market situation at the point in time prior to adoption of the challenged measure.⁴⁶⁷

7.225. The Panel agrees with the parties that the term "goods" in Article 3.1(b) can be read as synonymous with "products". This is also the reading that best reconciles the language used in the three authentic versions of the SCM Agreement. In Article 3.1(b), the term "goods" appears in the context of a prohibition on subsidies that are conditional upon the use of domestic over imported *goods*. As noted above, the purpose of this provision is to prohibit certain subsidies that have been considered particularly trade-distorting by Members. Since a main objective of the agreement is to address trade distortions caused by subsidies – in the provision at issue, a subsidized preference for domestic over imported goods –, it follows that the goods in question must be at least potentially tradable. Indeed, the SCM Agreement is part of a set of covered agreements called "Multilateral Agreements on Trade in Goods". There is no requirement under the provision, however, that the goods in question must be actually traded. Following the Appellate Body's guidance with respect to provisions in other covered agreements, it can be said that Article 3.1(b) of the SCM Agreement protects competitive opportunities of imported products, rather than existing trade flows of such products.⁴⁶⁸ In this regard, the fact that a given product may, or may not, be actually traded at present is not dispositive of whether competitive opportunities exist with respect to that product. The Panel therefore considers that there is no need to demonstrate present trade in a specific product as it exists at a given moment in time to establish a prohibited contingency under Article 3.1(b).

7.5.5 Relevant facts for the assessment of the alleged contingency

7.226. The European Union's primary claim is that, as a result of the First Siting Provision and the Second Siting Provision, considered individually or together, the challenged aerospace tax measures constitute subsidies that are *de jure* contingent on the use of domestic over imported goods.⁴⁶⁹

7.227. The European Union also argues that the First Siting Provision and the Second Siting Provision each make the tax measures at issue subsidies that are *de facto* contingent on the use of domestic over imported goods.⁴⁷⁰

7.228. Before assessing the European Union's claims, the Panel will review the texts of the relevant provisions of the measures at issue, as well as the additional factual evidence available.

7.5.5.1 The siting provisions of ESSB 5952

7.229. ESSB 5952 amended and extended the aerospace tax measures, which were originally established in 2003 by HB 2294.⁴⁷¹ The amendment and extension, however, did not take effect immediately upon enactment of ESSB 5952. Instead, the entry into force of the amendment and extension of the aerospace tax measures was contingent upon satisfaction of the First Siting Provision in Section 2 of ESSB 5952, namely "upon the siting of a significant commercial airplane manufacturing program in the state of Washington".⁴⁷² The legislation also provides that, "[i]f a significant commercial airplane manufacturing program is not sited in the state of Washington by June 30, 2017, ... [this act] does not take effect".⁴⁷³

7.230. The First Siting Provision reads:

⁴⁶⁶ European Union's second written submission, para. 46; opening statement at the first meeting of the Panel, paras. 47-48.

⁴⁶⁷ European Union's second written submission, para. 46; closing statement at the first meeting of the Panel, para. 9.

⁴⁶⁸ See, for example, Appellate Body Reports, *Japan – Alcoholic Beverages II*, p. 16, DSR 1996:I, 97, at pp. 109-110; *Korea – Alcoholic Beverages*, paras. 119-120.

⁴⁶⁹ European Union's second written submission, para. 60.

⁴⁷⁰ *Ibid.* 90-91.

⁴⁷¹ See para. 7.39 above.

⁴⁷² ESSB 5952 (Exhibit EU-3), Section 2, codified at RCW Section 82.32.850 (Exhibit EU-58). See also European Union's comments on United States' response to Panel question No. 53, para. 7.

⁴⁷³ ESSB 5952 (Exhibit EU-3), Section 2, codified at RCW Section 82.32.850 (Exhibit EU-58).

NEW SECTION. **Sec. 2.** A new section is added to chapter 82.32 RCW to read as follows:

(1) Chapter ..., Laws of 2013 3rd sp. sess. (this act) takes effect contingent upon the siting of a significant commercial airplane manufacturing program in the state of Washington. If a significant commercial airplane manufacturing program is not sited in the state of Washington by June 30, 2017, chapter ..., Laws of 2013 3rd sp. sess. (this act) does not take effect.

(2) The definitions in this subsection apply throughout this section unless the context clearly requires otherwise.

(a) "Commercial airplane" has the same meaning provided in RCW 82.32.550.

(b) "New model, or any version or variant of an existing model, of a commercial airplane" means a commercial airplane manufactured with a carbon fiber composite fuselage or carbon fiber composite wings or both.

(c) "Significant commercial airplane manufacturing program" means an airplane program in which the following products, including final assembly, will commence manufacture at a new or existing location within Washington state on or after the effective date of this section:

(i) The new model, or any version or variant of an existing model, of a commercial airplane; and

(ii) Fuselages and wings of a new model, or any version or variant of an existing model, of a commercial airplane.

(d) "Siting" means a final decision, made on or after November 1, 2013, by a manufacturer to locate a significant commercial airplane manufacturing program in Washington state.

(3) The department must make a determination regarding whether the contingency in subsection (1) of this section occurs and must provide written notice of the date on which such contingency occurs and chapter ..., Laws of 2013 3rd sp. sess. (this act) takes effect. If the department determines that the contingency in subsection (1) of this section has not occurred by June 30, 2017, the department must provide written notice stating that chapter ..., Laws of 2013 3rd sp. sess. (this act) does not take effect. Written notice under this subsection (3) must be provided to affected parties, the chief clerk of the house of representatives, the secretary of the senate, the office of the code reviser, and others as deemed appropriate by the department.⁴⁷⁴

7.231. Under the terms of the legislation, the First Siting Provision concerns a one-time event. That is, the amendment and extension of the challenged aerospace tax measures would come into effect, for all beneficiaries, upon the siting of a significant commercial airplane manufacturing programme in Washington State. Moreover, if no such siting occurred by the specified date (30 June 2017), the possibility for the amendment and extension of the measures to take effect would lapse.

7.232. The First Siting Provision defines "siting" to mean "a final decision, made on or after November 1, 2013, by a manufacturer to locate a significant commercial airplane manufacturing program in Washington State". In turn, "significant commercial airplane manufacturing program" is defined as:

[A]n airplane program in which the following products, including final assembly, will commence manufacture at a new or existing location within Washington state on or after the effective date of this section:

⁴⁷⁴ ESSB 5952 (Exhibit EU-3).

(i) The new model, or any version or variant of an existing model, of a commercial airplane; and

(ii) Fuselages and wings of a new model, or any version or variant of an existing model, of a commercial airplane.⁴⁷⁵

7.233. The First Siting Provision additionally defines "new model, or any version or variant of an existing model, of a commercial airplane" to mean "a commercial airplane manufactured with a carbon fiber composite fuselage or carbon fiber composite wings or both".⁴⁷⁶

7.234. As to the procedures to verify the satisfaction of the conditions in the First Siting Provision, Section 2 of ESSB 5952 provides that:

The department [of Revenue of the state of Washington] must make a determination regarding whether the contingency in subsection (1) of this section [the siting] occurs and must provide written notice of the date on which such contingency occurs and [this act] takes effect. If the department determines that the contingency in subsection (1) of this section has not occurred by June 30, 2017, the department must provide written notice stating that [this act] does not take effect. Written notice under this subsection (3) must be provided to affected parties, the chief clerk of the house of representatives, the secretary of the senate, the office of the code reviser, and others as deemed appropriate by the department.⁴⁷⁷

7.235. The Second Siting Provision within ESSB 5952 relates to the business and occupation (B&O) aerospace tax rate⁴⁷⁸, and provides as follows:

With respect to the manufacturing of commercial airplanes or making sales, at retail or wholesale, of commercial airplanes, this subsection (11) does not apply on and after July 1st of the year in which the department makes a determination that any final assembly or wing assembly of any version or variant of a commercial airplane that is the basis of a siting of a significant commercial airplane manufacturing program in the state under section 2 of this act has been sited outside the state of Washington. This subsection (11)(e)(ii) only applies to the manufacturing or sale of commercial airplanes that are the basis of a siting of a significant commercial airplane manufacturing program in the state under section 2 of this act.⁴⁷⁹

7.236. The Second Siting Provision concerns the continued availability of the 0.2904% B&O aerospace tax rate for the version or variant of a commercial airplane that is the basis of the First Siting Provision. The Second Siting Provision specifically pertains to the siting of any "final assembly or wing assembly" of such commercial airplane.

7.237. By its own terms, the Second Siting Provision refers to the same significant commercial airplane manufacturing programme (that is, the programme that satisfied the First Siting Provision) in which certain "products, including final *assembly*, will commence *manufacture* at a ... location within Washington state" (emphasis added). The Second Siting Provision "only applies to the manufacturing or sale of commercial airplanes that are the basis of a siting [under the First Siting Provision]".⁴⁸⁰ The relevant "commercial airplanes" in this regard are Boeing 777X aircraft.

⁴⁷⁵ Ibid. Section 2(2)(c) and (d), codified at RCW Section 82.32.850(2)(c) and (d) (Exhibit EU-58).

⁴⁷⁶ ESSB 5952 (Exhibit EU-3), Section 2(2)(b), codified at RCW Section 82.32.850(2)(b) (Exhibit EU-58).

⁴⁷⁷ ESSB 5952 (Exhibit EU-3), Section 2, codified at RCW Section 82.32.850 (Exhibit EU-58).

⁴⁷⁸ The Second Siting Provision concerns paragraph 11 of Sections 5 and 6 of ESSB 5952, which refers to the 0.2904% B&O tax rate applicable to persons "engaging within the [state of Washington] in the business of manufacturing commercial airplanes, or components of such airplanes, or making sales, at retail or wholesale, of commercial airplanes or components of such airplanes, manufactured by the seller". See ESSB 5952 (Exhibit EU-3), Sections 5 and 6. See also United States' first written submission, paras. 79-80; response to Panel question No. 53(b), para. 16.

⁴⁷⁹ ESSB 5952 (Exhibit EU-3), Sections 5 and 6, codified at RCW Section 82.32.850(11)(e)(ii) (Exhibit EU-22).

⁴⁸⁰ ESSB 5952 (Exhibit EU-3), Sections 5 and 6, codified at RCW Section 82.32.850(11)(e)(ii) (Exhibit EU-22).

7.238. ESSB 5952 does not define the term "manufacture".⁴⁸¹ However, Section 82.04.120 of the Revised Code of Washington contains the following definition of "manufacture":

"To manufacture" embraces all activities of a commercial or industrial nature wherein labor or skill is applied, by hand or machinery, to materials so that as a result thereof a new, different or useful substance or article of tangible personal property is produced for sale or industrial use...⁴⁸²

7.239. This definition is part of Chapter 82.04 of the Revised Code of Washington, which governs the application of the B&O tax.⁴⁸³ As stated by the United States, the Department of Revenue of the state of Washington considers that the definition "would apply in the interpretation of ESSB 5952".⁴⁸⁴

7.240. There is no relevant statutory definition of the term "assembly". As noted by the United States, if called to interpret undefined terms, Washington State authorities would consider the common law or ordinary meaning of the word in the context of the statute in which the word appears.⁴⁸⁵ Based on the dictionary meaning of the word, and its consideration of the statute as a whole, the United States notes that "assembly is a subset of manufacturing".⁴⁸⁶

7.5.5.2 Products at issue

7.241. The European Union's claim in this dispute relates to an alleged prohibited contingency based on the use of domestic over imported *wings* and *fuselages*.⁴⁸⁷ It is not in dispute whether the measures at issue place any conditions on the use of any *other* elements or components of commercial airplanes, including sub-components of wings and fuselages.⁴⁸⁸ Accordingly, the products at issue for the Panel's analysis under Article 3.1(b) of the SCM are wings and fuselages of commercial airplanes.

7.242. The parties have presented extensive factual evidence regarding the production of commercial airplanes, particularly with regard to the production of wings and fuselages in the context of commercial airplane assembly. In this section, the Panel will review this evidence, including undisputed aspects of the production and assembly of Boeing's 777X aircraft, as well as other evidence relating to the production and transport of wings and fuselages of other types of commercial airplanes.

7.5.5.2.1 Boeing's 777X aircraft programme

7.243. As noted above, the aerospace tax measures, as amended and extended by ESSB 5952, took effect upon fulfilment of the First Siting Provision, based on Boeing's decision to site its programme for the production of 777X aircraft in the state of Washington.⁴⁸⁹ The United States has provided background explanations as to various aspects of the 777X programme and the production process of 777X aircraft, including information provided in a statement by corporate officers of Boeing (Boeing Expert Statement).⁴⁹⁰

⁴⁸¹ United States' first written submission, para. 78.

⁴⁸² See RCW Section 82.04.120 (Exhibit USA-37). The provision additionally lists activities included in this definition such as *inter alia* "[t]he production or fabrication of special made or custom made articles".

⁴⁸³ United States' response to Panel question No. 14, para. 28.

⁴⁸⁴ Ibid.

⁴⁸⁵ See Supreme Court of Washington, *Citizens Alliance for Property Rights Legal Fund v. San Juan County et al.* (2015) (Exhibit USA-38). United States' response to Panel question No. 14, para. 29.

⁴⁸⁶ United States' response to Panel question No. 14, paras. 29-32.

⁴⁸⁷ See, e.g. European Union's first written submission, paras. 74-75; opening statement at the first meeting of the Panel, para. 4; second written submission, para. 1; opening statement at the second meeting of the Panel, paras. 3, 9, 32-34.

⁴⁸⁸ See e.g. European Union's opening statement at the second meeting of the Panel, paras. 9 and 31-32; United States' response to Panel question No. 64, para. 41.

⁴⁸⁹ European Union's first written submission, para. 45; United States' first written submission, paras. 2 and 78. See also Letter from the Director of the Washington State Department of Revenue to the Code Reviser, 10 July 2014 (Exhibit EU-61).

⁴⁹⁰ Boeing expert statement (Exhibit USA-1) (BCI).

7.244. The 777X is a new aircraft programme developed by Boeing, based on its earlier 777 programme. According to the explanations provided by the United States, many of the 777X production and supplier choices made by Boeing mirror those of the current 777-300ER, which is a twin-aisle aircraft, typically configured for approximately 350-375 passengers (depending on class configuration) with a range of 7,825 nautical miles. The 777-300ER's fuselages and wings, however, are composed primarily of aluminium; by contrast, the 777X's wings will be made primarily of carbon fibre-reinforced plastic.⁴⁹¹

7.245. The United States submits a statement by experts affiliated with Boeing regarding Boeing's production operations and background information on the products at issue. As explained by the Boeing experts:

An aircraft gets its essential structure, its aerodynamic and load-bearing qualities, from its *airframe*. The main airframe structures are the fuselage, wing, and tail.⁴⁹²
(emphasis original)

7.246. In the following sections, the Panel will review evidence and information related to the manufacturing and assembly of the Boeing 777X. The Panel notes that this evidence, including the statement by the Boeing experts, concerns *future* manufacturing operations that have not yet commenced, and that, based on current projections, the first variant of the 777X will enter into service in the year 2020.⁴⁹³

7.5.5.2.2 Fuselage

7.247. As explained by the Boeing experts with respect to the fuselage of the aircraft:

The *fuselage* is the long tube that forms the longitudinal axis of the aircraft, running from nose to tail. It forms the exterior structure that houses the aircraft's interior accommodations and payload – e.g., passengers, crew, flight deck, cargo.⁴⁹⁴
(emphasis original)

7.248. The fuselage's primary elements consist of:

- a. Skins: the panels that form the exterior of the fuselage, with cutouts for windows and doors;
- b. Frames: stronger, hoop-shaped structures positioned perpendicular to the skins at intervals along the length of the fuselage; and
- c. Stringers: long, thin structures running parallel to, and reinforcing, the skins.⁴⁹⁵

7.249. The fuselage also includes floor frames and panels that support passengers, crew, cargo, and interior accommodations.⁴⁹⁶

7.250. The 777X's fuselage comprises eight separate fuselage sections, called Sections 41 to 48. Section 41 is the nose of the plane and Section 48 is the empennage (a tapered end at the tail of the plane).⁴⁹⁷ Like all other Boeing commercial aircraft (with the exception of the 787), the 777X's primary fuselage structures are made from aluminium.⁴⁹⁸ According to the Boeing experts, **[[BCI]]**.⁴⁹⁹

⁴⁹¹ United States' first written submission, paras. 20-24; Boeing expert statement (Exhibit USA-1) (BCI), para. 16; Boeing 777 Backgrounder (Exhibit USA-6).

⁴⁹² See Boeing expert statement (Exhibit USA-1) (BCI), para. 11.

⁴⁹³ See *ibid.* para. 40.

⁴⁹⁴ See *ibid.* para. 12.

⁴⁹⁵ See Boeing expert statement (Exhibit USA-1) (BCI), para. 12.

⁴⁹⁶ See *ibid.*

⁴⁹⁷ See *ibid.* para. 13.

⁴⁹⁸ See *ibid.*

⁴⁹⁹ See *ibid.* para. 42. "Make/buy" refers to the process of determining which aircraft elements Boeing will make, and which to procure from outside suppliers. *Ibid.* fn 1.

7.251. In its initial fuselage manufacturing operations, Boeing receives fuselage structures from its suppliers at the Everett fuselage building, which when completed will be a new facility next to the main factory building where the 777X will undergo final assembly.⁵⁰⁰ For the various fuselage Sections, **[[BCI]]**, these primary fuselage structures **[[BCI]]**.⁵⁰¹ The separate fuselage Sections are then joined into three larger parts of the fuselage, namely the forward (Sections 41 and 43), center (Sections 44 and 11/45), and aft (Sections 46-48). More specifically:

- a. The forward part of the fuselage incorporates Section 41, which is the foremost fuselage section that will eventually house the flight deck, which is joined to Section 43.⁵⁰²
- b. The center part of the fuselage consists of Section 44, which unlike other fuselage sections does not have a keel panel; rather, Section 11/45 forms the bottom of the center part of the fuselage, and is itself constructed from various structures: **[[BCI]]**.⁵⁰³
- c. The aft part of the fuselage is formed by joining three separate fuselage sections (Sections 46-48).⁵⁰⁴

7.5.5.2.3 Wings

7.252. As explained by the Boeing experts with respect to the wings of the aircraft:

The *wings* join the aircraft at roughly the mid-point along the length of the fuselage. In addition to providing lift and flight control surfaces, the wings carry the engine installations and fuel.⁵⁰⁵ (emphasis original)

7.253. The wings have elements that are fixed in flight, and flight control surfaces that move in flight. The 777X's main fixed wing elements consist of:

- a. The main wing box, which forms most of the wing's visible surface area;
- b. The wing tip, which is static in flight but folds at airport gates to meet certain wingspan constraints;
- c. The fixed leading and trailing edges that run most of the span of the visible wing; and
- d. The center wing box, which sits under the fuselage and is not visible on a finished aircraft.⁵⁰⁶

7.254. The visible wing box structures are composed of: (i) the skins, which form the wing exterior; (ii) the ribs, which run perpendicular to the wing span and support the skins; (iii) the spars, which run the length of the wing span and support the ribs; and (iv) the stringers, which are attached to the skins and also run the length of the wing. As for the movable elements of the wings, the primary parts are: (i) the slats on the wing's leading edge; and (ii) the droop panels, spoilers, ailerons and flaps on the trailing edge.⁵⁰⁷

7.255. Some of the main structures of the 777X's wings will be made mostly from carbon fibre-reinforced plastic.⁵⁰⁸ By contrast, both the fuselage and the wing of the 777-300ER are primarily composed of aluminium.⁵⁰⁹ According to the Boeing experts, **[[BCI]]**.⁵¹⁰

⁵⁰⁰ Boeing expert statement (Exhibit USA-1) (BCI), para. 52(a).

⁵⁰¹ Ibid. para. 52(b).

⁵⁰² Ibid. para. 52(c).

⁵⁰³ Ibid. para. 52(e).

⁵⁰⁴ Ibid. para. 52(d).

⁵⁰⁵ See Boeing expert statement (Exhibit USA-1) (BCI), para. 14.

⁵⁰⁶ See *ibid.*

⁵⁰⁷ See *ibid.* para. 15.

⁵⁰⁸ United States' first written submission, para. 22; Boeing expert statement (Exhibit USA-1) (BCI), paras. 16, 39, 43.

⁵⁰⁹ United States' first written submission, para. 21; Boeing 777 Backgrounder (Exhibit USA-6).

⁵¹⁰ See Boeing expert statement (Exhibit USA-1) (BCI), para. 42. See also United States' first written submission, para. 32.

7.256. The initial wing manufacturing operations for the 777X will take place in the Composite Wing Center that is being built close to the main factory building. As explained by the Boeing experts, that center is responsible for fabricating **[[BCI]]** 777X wing structures, **[[BCI]]**.⁵¹¹ Further fabrication takes place in a spar sub-assembly building where **[[BCI]]**.⁵¹²

7.257. The resulting "Section 12" wing structure consists of the main wing box (including spars, ribs, and panels) and the fixed leading and trailing edges, but does not include movable edges or the wingtip.⁵¹³

7.5.5.2.4 Final assembly process

7.258. The United States provided detailed descriptions of the various steps in the assembly of the 777X aircraft. The United States "acknowledges that wing fabrication, wing assembly, and fuselage assembly are all production activities conducted in the manufacture of an airplane"⁵¹⁴, but argues that fuselages and wings are "features or elements of the finished aircraft, which are generated only through the final assembly process of the airplane itself – not inputs into the production process".⁵¹⁵ In other words, and as stated by the Boeing experts, "neither a complete fuselage nor complete wings enter the final assembly process".⁵¹⁶

7.259. The production carried out in the fuselage building, described above, results in three separate sections of the fuselage (forward, center, and aft), which at the time they leave the fuselage building still **[[BCI]]**.⁵¹⁷ The three fuselage sections are then **[[BCI]]**.^{518, 519}

7.260. The Section 12 wing structure, which results from initial wing manufacturing operations described above, undergoes additional operations in the main factory building, namely: **[[BCI]]**.⁵²⁰ These operations result in two "outboard wing structures".⁵²¹

7.261. Having undergone separate fabrication and installation operations⁵²², the center fuselage structure (including the center wing box) and outboard wing structures are at this point brought together in the "wing-body join stage" of the moving assembly line. As explained by the Boeing experts, "[t]his is the first point at which the main wing structures – the two outboard wings and the center wing box – are joined together".⁵²³ At this stage, the outboard wing structures still lack **[[BCI]]**.⁵²⁴

7.262. The final assembly process then moves into "final body join", and the subsequent final assembly position, where, as explained by the Boeing experts, certain operations complete the airframe and install the major remaining systems:

[[BCI]]⁵²⁵

7.5.5.2.5 Production and assembly of other aircraft

7.263. In addition to the Boeing 777X, the parties have presented evidence on the production of other models of aircraft, particularly in respect of the production of wings and fuselages.

⁵¹¹ Boeing expert statement (Exhibit USA-1) (BCI), para. 52(h).

⁵¹² Ibid. para. 52(i)-(k).

⁵¹³ United States' response to Panel question No. 64, para. 40.

⁵¹⁴ United States' response to Panel question No. 66, para. 71.

⁵¹⁵ United States' first written submission, para. 110.

⁵¹⁶ See Boeing expert statement (Exhibit USA-1) (BCI), para. 53.

⁵¹⁷ Ibid. para. 52(f).

⁵¹⁸ Ibid.

⁵¹⁹ Ibid. para. 52(m).

⁵²⁰ Ibid. para. 52(l).

⁵²¹ Ibid.

⁵²² See *ibid.* para. 52(m).

⁵²³ Ibid. para. 52(n).

⁵²⁴ Ibid.

⁵²⁵ Ibid. para. 51(p).

7.264. The parties have referred to another model of aircraft manufactured by Boeing, the 787, in respect of whether Boeing imports 787 wings from a foreign supplier.⁵²⁶ The United States submits that the "787's wings, like those of all Boeing large civil aircraft, consist of numerous individual parts, including those that make up fixed wing structures (e.g., the spars, ribs, and panels that comprise the main wing box; the fixed leading and trailing edges; and the center wing box) and the movable wing elements that enable controlled flight operations (e.g., moveable leading and trailing edges)".⁵²⁷ According to the United States, "Boeing imports multiple wing-related structures from Japan" that require further wing assembly activity in the United States.⁵²⁸ More specifically, Boeing imports a "right-hand and left-hand partial wing structure" that include the constituent parts of the main wing box and the fixed and leading trailing edges⁵²⁹, without **[[BCI]]**.⁵³⁰ The United States clarifies that the imported wing structure for the 787 is referred to as Section 12, discussed above in relation to the 777X, which consists of the main wing box and the fixed leading and trailing edges.⁵³¹ These wing structures are then shipped to a Boeing 787 assembly facility in the United States in Boeing's Dreamlifter aircraft where they undergo assembly operations, including additional elements of the wing itself.⁵³² The European Union has also provided evidence, including descriptions from Boeing, of the production and shipping of the relevant 787 wing structures.⁵³³

7.265. In respect of the fuselages of the Boeing 737, it is not disputed that Boeing sources complete fuselages for the 737NG and 737MAX single-aisle aircraft from a supplier in the state of Kansas, which are then transported by rail to Boeing's 737 manufacturing facility in the state of Washington for final assembly of the aircraft.⁵³⁴

7.266. The parties have also presented evidence of the production and assembly of certain models of Airbus aircraft. The European Union describes the production and transport of Airbus A350 XWB wings, which are structurally assembled at a facility in the United Kingdom, and from there transported by the Airbus Beluga carrier aircraft to a facility in Bremen, Germany where they are "fully equipped with the relevant systems", and then transported on the Airbus Beluga to the final assembly site in Toulouse, France.⁵³⁵ In this regard, the United States contends that "these structures have neither all the fixed nor all the movable parts that the fully assembled A350 XWB wings have, and they must therefore undergo further assembly"⁵³⁶, such that "what leaves the United Kingdom is a **[[BCI]]**".⁵³⁷ The European Union further describes the transport of Airbus A380 wings "across long distances", with wings first produced in the United Kingdom and "then moved by road for a mile, placed on a specially built barge on the river, and finally transported by road to Toulouse".⁵³⁸ The United States submits that, for the A380, what is shipped

⁵²⁶ See, e.g. European Union's first written submission, paras. 74-75; Reuters, "Boeing seen in advanced talks to make 777X near Seattle", 4 November 2013 (Exhibit EU-65).

⁵²⁷ United States' response to Panel question No. 16, para. 34.

⁵²⁸ Ibid.

⁵²⁹ Ibid. para. 35.

⁵³⁰ Boeing expert statement (Exhibit USA-1) (BCI), fn 6.

⁵³¹ United States' response to Panel question No. 64, para. 40; response to Panel question No. 73; Mitsubishi Heavy Industries, Boeing 787 (Exhibit USA-42); Boeing Frontiers, "Wings Around the World", March 2006 (Exhibit USA-68); Boeing 787 customs invoice and related shipment documentation (Exhibit USA-67) (BCI).

⁵³² United States' response to Panel question No. 16, para. 35; Boeing expert statement (Exhibit USA-1) (BCI), para. 43 (explaining that **[[BCI]]** in comparison to 777X wings).

⁵³³ See European Union's response to Panel question No. 33, para. 79; Boeing Presentation, "Introducing the 787", September 2011 (Exhibit EU-78); Boeingblogs, "Randy's Journal: Arrivals", 22 May 2007 (Exhibit EU-79); Boeing Video, "Boeing 747 Dreamlifter", 17 January 2009 (Exhibit EU-97); Boeing Frontiers, "The 747-400 will be transformed into an even larger freighter", June 2005 (Exhibit EU-122).

⁵³⁴ United States' response to Panel question No. 35, para. 80; Spirit AeroSystems, "Spirit celebrates completion of first Boeing 737 MAX fuselage", (Exhibit USA-52); European Union's response to Panel question No. 33, paras. 80-81.

⁵³⁵ See European Union's response to Panel question No. 17, paras. 18-19; Airbus, "How is an aircraft built? Production" (Exhibit EU-84); Airbus Video, "The A350 XWB Final Assembly Line: efficiency in motion", 23 October 2012 (Exhibit EU-87).

⁵³⁶ United States' response to Panel question No. 64, para. 47.

⁵³⁷ Ibid. (citing Email from Erik Zahn, Boeing Commercial Airplanes, 15 April 2016 (Exhibit USA-73) (BCI).

⁵³⁸ See European Union's response to Panel question No. 17, para. 22; BBC Documentary, "How to Build A Super Jumbo Wing", 24 August 2013 (Exhibit EU-91).

to Toulouse are **[[BCI]]**.⁵³⁹ In this connection, the United States considers that "[t]here are at least some complete finished wings for single-aisle aircraft that fit on the transport aircraft [such as an Airbus Beluga or a Boeing Dreamlifter], **[[BCI]]**."⁵⁴⁰ However, the United States contends that the same is not true for completely assembled wings of larger aircraft, including **[[BCI]]**.⁵⁴¹

7.267. In addition, the European Union submits that "[m]anufacturing fuselages as intermediate goods before the final assembly of the aircraft is also the standard practice for Airbus", referring specifically to the production of the A320, the A350 XWB, and the A380.⁵⁴²

7.5.5.3 Other relevant facts on record

7.268. In accordance with the First Siting Provision in ESSB 5952, the availability of the aerospace tax measures at issue was conditional on a determination by the Department of Revenue of the state of Washington that a manufacturer had made a final decision, after 1 November 2013 but before 30 June 2017, to site a significant commercial airplane manufacturing programme in the state of Washington.

7.269. The "significant commercial airplane manufacturing program" necessary for the Department of Revenue's determination is one in which the following products, including final assembly, will commence manufacture: (i) a new model of a commercial airplane, or any version or variant of an existing model; and (ii) fuselages and wings of a new model of a commercial airplane, or of any version or variant of an existing model. The "new model" or "any version or variant of an existing model" of a commercial airplane is defined as "a commercial airplane manufactured with a carbon fiber composite fuselage or carbon fiber composite wings or both".

7.270. Boeing's 777X programme is the "significant commercial airplane manufacturing program", and the 777X is the new model of a commercial airplane, that satisfied the First Siting Provision. On 9 July 2014, Boeing notified the Department of Revenue of the state of Washington in writing that Boeing had made a final decision to manufacture the 777X airplane in the state of Washington. In its letter Boeing stated that this decision satisfied the requirement in ESSB 5952 that a significant commercial airplane manufacturing programme be sited in the state of Washington.⁵⁴³ Three attachments accompanied Boeing's letter, as examples of "actions Boeing has taken consistent with its decision to manufacture the 777X in Washington".⁵⁴⁴ The first attachment was a copy of a Collective Bargaining Agreement between Boeing and the International Association of Machinists and Aerospace Workers, AFL-CIO, containing a Letter of Understanding in which "Boeing 'agrees to locate the 777X wing fabrication and assembly, final assembly, and major components' in Puget Sound" (Washington State).^{545, 546} **[[BCI]]**.^{547, 548, 549}

⁵³⁹ United States' response to Panel question No. 64, para. 48 (citing Email from Erik Zahn, Boeing Commercial Airplanes, 15 April 2016 (Exhibit USA-73) (BCI)).

⁵⁴⁰ United States' response to Panel question No. 64, para. 41 (citing Email from Erik Zahn, Boeing Commercial Airplanes, 15 April 2016 (Exhibit USA-73) (BCI)).

⁵⁴¹ United States' response to Panel question No. 64, paras. 52-53.

⁵⁴² European Union's response to Panel question No. 33, para. 83; Airbus, "How is an aircraft built? Final assembly and tests" (Exhibit EU-86); Airbus Video, "The A350 XWB Final Assembly Line: efficiency in motion", 23 October 2012 (Exhibit EU-87); Airbus Video, "A350 XWB final assembly: a step-by-step overview", 23 October 2012 (Exhibit EU-88); Airbus Video, "A380 from dream to reality: Final assembly", 18 October 2007 (Exhibit EU-104).

⁵⁴³ Boeing letter to the Director of the Washington State Department of Revenue, 9 July 2014 (Exhibit USA-32) (BCI). See also United States' response to Panel question No. 10, paras. 20-21.

⁵⁴⁴ Boeing letter to the Director of the Washington State Department of Revenue, 9 July 2014 (Exhibit USA-32) (BCI).

⁵⁴⁵ Ibid.

⁵⁴⁶ See Letter of Understanding No. 43, Subject: 777X Work Placement, dated 3 January 2014, in Collective Bargaining Agreement between Boeing and the International Association of Machinists and Aerospace Workers, 2 November 2008, including Contract Extension and Modification Agreements, 7 December 2011 and 3 January 2014 (Exhibit USA-33), p. 190.

⁵⁴⁷ Boeing letter to the Director of the Washington State Department of Revenue, 9 July 2014 (Exhibit USA-32) (BCI).

⁵⁴⁸ Addendum No. 14 to the 1991 Boeing Everett Mitigation Decision Document SEPA #14-009, 27 March 2014 (Exhibit USA-34) (BCI).

⁵⁴⁹ Addendum No. 15 to the 1991 Boeing Everett Mitigation Decision Document SEPA #14-011 – Composite Wing Manufacturing Facility, 30 May 2014 (Exhibit USA-35) (BCI).

7.271. The Washington State Department of Revenue accepted Boeing's statement as fulfilling the contingency requirements of the First Siting Provision in ESSB 5952. Subsequent to Boeing's letter, on 10 July 2014, the Department of Revenue issued a formal notification that a manufacturer had made a final decision to site a significant commercial airplane manufacturing programme in the state of Washington; that the contingency requirements in ESSB 5952 had been satisfied; and that the relevant legislation had taken effect on 9 July 2014.⁵⁵⁰ As a result of this determination, the expiration date for the aerospace tax measures at issue was extended until 1 July 2040 for all eligible taxpayers, and the other amendments to those measures took effect.⁵⁵¹ As discussed above, pursuant to ESSB 5952 the Department of Revenue's determination is a one-time decision and there is no legal mechanism under Washington State law that would allow the Department of Revenue to revoke its determination.⁵⁵²

7.5.6 Whether the subsidies are *de jure* contingent upon the use of domestic over imported goods

7.272. The Panel turns to the European Union's principal claim, which is its *de jure* claim. In this regard, the Panel must determine whether the European Union has made a *prima facie* case that the challenged aerospace tax measures are *de jure* contingent upon the use of domestic instead of imported goods, and therefore inconsistent with the United States' obligations under Article 3.1(b) of the SCM Agreement. To prevail on its *de jure* claim, the European Union has the burden of demonstrating that such contingency or conditionality is either set out *expressly* on the face of the legislation or can clearly be derived, *by necessary implication*, from the words actually used in the legislation.⁵⁵³

7.273. In this regard, the Panel understands that a contingency that is not set out expressly in the relevant legislation may nevertheless be derived by necessary implication if such contingency results inevitably from the words actually used in the legislation, or if any other interpretation would be unreasonable.⁵⁵⁴ In other words, the terms used in the legislation must either expressly or by necessary implication demonstrate that the granting of a subsidy is contingent upon the use of domestic instead of imported goods.⁵⁵⁵ For the purpose of the *de jure* determination, including by necessary implication, the relevant facts are therefore the text of the legislation at issue and any additional facts that can assist the Panel in understanding the meaning of the terms as used in that legislation.⁵⁵⁶

7.274. As noted above, the ordinary connotation of the term "contingent" is "conditional" or "dependent for its existence on something else". Therefore, the question before the Panel is whether, on the basis of the words of the relevant legislation, the challenged aerospace tax measures are conditional upon the use of domestic over imported goods. Contingency upon the use of domestic over imported goods need not be the only condition; it can be one of several other

⁵⁵⁰ Letter from the Director of the Washington State Department of Revenue to the Code Reviser, 10 July 2014 (Exhibit EU-61). See also United States' response to Panel question Nos. 10 and 12, paras. 21 and 26.

⁵⁵¹ United States' first written submission, para. 78 (citing letter from the Director of the Washington State Department of Revenue to the Code Reviser, 10 July 2014 (Exhibit EU-61)); response to Panel question No. 12, para. 26.

⁵⁵² See United States' response to Panel question No. 12, para. 26.

⁵⁵³ As noted above (see paragraphs 7.209 and 7.210 above), the Appellate Body has indicated that *de jure* contingency can be established explicitly by a legal instrument and "also be derived by necessary implication from the words actually used in the measure". Appellate Body Report, *Canada – Autos*, para. 100. See also *ibid.* para. 123.

⁵⁵⁴ The meaning of the word "necessary", when referring to a mental concept, a truth, a judgment, etc., can be understood to refer to something "resulting inevitably from the nature of things or of the mind itself". *Shorter Oxford English Dictionary*, 6th edition (2007), Vol. 2, p. 1901. A necessary implication is an implication so strong in its probability that anything to the contrary would be unreasonable. See *Black's Law Dictionary*, 8th edition (2004), p. 770.

⁵⁵⁵ See Appellate Body Report, *Canada – Aircraft*, para. 171. See also European Union's response to Panel question No. 18, paras. 23-26.

⁵⁵⁶ In the context of a *de jure* analysis, such facts could include relevant context within the legislation itself, or other clarifications of legal meaning within the domestic legal system in question (such as the interpretation of pertinent terms by domestic courts, or administrative regulations directly implementing the legislation). However, any such facts would serve to illuminate the meaning of words used in the legislation, and would not extend to other factual circumstances surrounding the granting of the subsidy that provide the context for understanding the measure's design, structure, and modalities of operation.

conditions for benefitting from the tax measures at issue. In order to find contingency in the sense of Article 3.1(b), such contingency must be a necessary condition so that the recipient would not benefit from the subsidy unless domestic goods are used instead of, or in preference to, imported goods.

7.275. The European Union asserts that the prohibited contingency is clearly set out in the text of ESSB 5952 as a result of the First Siting Provision and of the Second Siting Provision, whether considered individually or together.⁵⁵⁷ In the European Union's view, each of these two provisions:⁵⁵⁸

[I]ndependently results in a *de jure* violation of Article 3.1(b).⁵⁵⁹ At the same time, these conditions act *together* to maximize trade distortions in favour of domestic goods, and to the detriment of competitive opportunities for imported goods. While the [First Siting Provision] focuses on component sourcing decisions made at the beginning of a new aircraft programme, the [Second Siting Provision] focuses on later stages.⁵⁶⁰ (emphasis original)

7.276. The European Union adds that a prohibited contingency in respect of *wings* results from both the First Siting Provision and the Second Siting Provision, while a prohibited contingency in respect of *fuselages* would result solely from the First Siting Provision.⁵⁶¹

7.277. With respect to the First Siting Provision, according to the European Union:

[U]nder the [First Siting Provision] established in Section 2 [of ESSB 5952], the aerospace tax incentive extensions and expansion provided for in [ESSB 5952] were made contingent upon Boeing's decision to locate in Washington State both (i) production of the wings and fuselage for the 777X and (ii) final assembly of the 777X.^{562, 563}

7.278. The European Union concludes:

Stated differently, for the extension and expansion of the existing aerospace tax incentives to occur, Boeing was required to commit to use wings and fuselages produced or assembled in Washington State in the final assembly of 777X LCA in Washington State.⁵⁶⁴

7.279. With respect to the Second Siting Provision, the European Union asserts that:

Pursuant to the exclusive-production condition established by [ESSB 5952] ... the reduced [business and occupation] tax rate would not apply to revenue from the 777X *in the event* Boeing were to perform any final assembly, *or any wing assembly*, for the 777X outside of Washington State.⁵⁶⁵ In other words, in order for Boeing to benefit from the [business and occupation] tax rate reduction with respect to the 777X

⁵⁵⁷ European Union's first written submission, paras. 70 and 73; second written submission, paras. 1, 2, 41, 60, and 90; opening statement at the first meeting of the Panel, para. 6; closing statement at the first meeting of the Panel, para. 3; opening statement at the second meeting of the Panel, para. 2; response to Panel question Nos. 29, 41, 46, and 68, paras. 67, 98, 125, and 46.

⁵⁵⁸ European Union's response to Panel question No. 68, para. 46.

⁵⁵⁹ (footnote original) See, European Union's first written submission, para. 73 ("As a result of the programme-siting condition and the exclusive-production condition, *whether considered individually or together*, the Washington State tax incentives, as amended and extended by SSB 5952, constitute subsidies that are contingent on the use of domestic over imported goods, in violation of Articles 3.1(b) and 3.2 of the SCM Agreement". (emphasis added)).

⁵⁶⁰ European Union's opening statement at the first meeting of the Panel, para. 6. See also European Union's response to Panel question No. 41, para. 98.

⁵⁶¹ European Union's response to Panel question No. 43, para. 101.

⁵⁶² (footnote original) See SSB 5952 Bill Report, Exhibit EU-4, p. 3.

⁵⁶³ European Union's first written submission, para. 44.

⁵⁶⁴ Ibid. See also European Union's second written submission, para. 61; opening statement at the first meeting of the Panel, para. 4.

⁵⁶⁵ (footnote original) See SSB 5952 §§ 5-6 (adding new subsection (e)(ii) to RCW 82.04.260(11)), Exhibit EU-3.

(whether prior to or after 2024), Boeing must not conduct any final assembly, or any wing assembly, of that aircraft outside of Washington State ...

Accordingly, under this exclusive-production condition, 777X aircraft benefit from the preferential [business and occupation] tax rate only if Boeing assembles the wings and assembles the aircraft exclusively in Washington State.⁵⁶⁶ (emphasis original)

7.280. The United States has submitted particular facts relating to the production process of the 777X programme as evidence of the meaning of the requirements in the First and Second Siting Provisions.⁵⁶⁷ The factual evidence referred to by the United States does not specifically relate to the meaning of the terms used in the legislation, nor does it concern the necessary implication of those terms. Rather, the evidence concerns the particular manner in which Boeing will produce 777X aircraft in Washington State.⁵⁶⁸ In this regard, the Panel is not persuaded by the United States' argument that those facts relating to the siting of the 777X programme in Washington State are relevant to the *de jure* analysis. To the extent that this evidence sheds light on "the total configuration of the facts constituting and surrounding the granting of the subsidy"⁵⁶⁹, the Panel will consider its relevance in the context of the European Union's *de facto* claim.

7.281. The Panel must decide the European Union's *de jure* claim against the aerospace tax measures on the basis of the text of ESSB 5952. The Panel will start its consideration of this claim by looking separately at the First Siting Provision and the Second Siting Provision to assess whether the European Union has successfully demonstrated the existence of the prohibited contingency in either of the provisions. Subsequently, if necessary, the Panel will consider the two siting provisions acting jointly.

7.5.6.1 The First Siting Provision, considered separately

7.282. The Panel recalls that, according to the First Siting Provision in Section 2 of ESSB 5952, the aerospace tax measures as amended and extended by ESSB 5952 "[take] effect contingent upon the siting of a significant commercial airplane manufacturing program in the state of Washington".⁵⁷⁰ The legislation also provides that, "[i]f a significant commercial airplane manufacturing program is not sited in the state of Washington by June 30, 2017, ... [this act] does not take effect".⁵⁷¹

7.283. The Panel further recalls that the First Siting Provision defines "siting" to mean "a final decision, made on or after November 1, 2013, by a manufacturer to locate a significant commercial airplane manufacturing program in Washington State".⁵⁷² In turn, "significant commercial airplane manufacturing program" is defined as:

⁵⁶⁶ European Union's first written submission, paras. 47 and 52. See also European Union's second written submission, para. 61.

⁵⁶⁷ See, for example, United States' response to Panel question Nos. 18, 39, and 46, paras. 37-43, 93-94, and 121-122.

⁵⁶⁸ The Panel notes the United States' argument that, "even under a *de jure* analysis, a panel must make sufficient findings as to how the alleged contingency operates, which may require findings as to how the contingency applies to actual subsidy recipients." See United States' response to Panel question No. 46, para. 116. The United States seeks support for this statement in the Appellate Body's analysis in *Canada – Autos*. The measures at issue in that case created "value-added requirements" that *de jure* were company-specific and capable of variation across the manufacturer beneficiaries. Thus, according to the explicit terms of "the legal instruments at issue [in that dispute] and their implications for individual manufacturers", there was a "multiplicity of possibilities for compliance" that may have been relevant to an analysis of *de jure* contingency. Appellate Body Report, *Canada – Autos*, paras. 130 and 132. This is distinguishable from the measures at issue in the present case, for which particular production choices by a manufacturer are not part of the *de jure* requirements of the measures, but rather form part of the surrounding factual circumstances of the alleged contingency.

⁵⁶⁹ Appellate Body Report, *Canada – Aircraft*, para. 167.

⁵⁷⁰ ESSB 5952 (Exhibit EU-3), Section 2, codified at RCW Section 82.32.850 (Exhibit EU-58). See also European Union's comments on United States' response to Panel question No. 53, para. 7.

⁵⁷¹ ESSB 5952 (Exhibit EU-3), Section 2, codified at RCW Section 82.32.850 (Exhibit EU-58).

⁵⁷² ESSB 5952 (Exhibit EU-3), Section 2(2)(d), codified at RCW Section 82.32.850(2)(d) (Exhibit EU-58).

[A]n airplane program in which the following products, including final assembly, will commence manufacture at a new or existing location within Washington state on or after the effective date of this section:

- (i) The new model, or any version or variant of an existing model, of a commercial airplane; and
- (ii) Fuselages and wings of a new model, or any version or variant of an existing model, of a commercial airplane.⁵⁷³

7.284. The First Siting Provision additionally defines "new model, or any version or variant of an existing model, of a commercial airplane" to mean "a commercial airplane manufactured with a carbon fiber composite fuselage or carbon fiber composite wings or both".⁵⁷⁴

7.285. As to the procedures involved, according to Section 2 of ESSB 5952:

The department [of Revenue of the state of Washington] must make a determination regarding whether the contingency in subsection (1) of this section occurs and must provide written notice of the date on which such contingency occurs and [this act] takes effect. If the department determines that the contingency in subsection (1) of this section has not occurred by June 30, 2017, the department must provide written notice stating that [this act] does not take effect. Written notice under this subsection (3) must be provided to affected parties, the chief clerk of the house of representatives, the secretary of the senate, the office of the code reviser, and others as deemed appropriate by the department.⁵⁷⁵

7.286. Based on the terms used in the legislation, the Panel understands that, for the aerospace tax measures to take effect, the First Siting Provision requires a determination by the Department of Revenue of the state of Washington that a final decision has been made, on or after 1 November 2013 and by 30 June 2017, to site a "significant commercial airplane manufacturing program" within the state of Washington. The legislation also defines the characteristics that the "significant commercial airplane manufacturing program" would have to fulfil to qualify for the Department of Revenue's positive determination. Those characteristics are, in essence, that the following products will "commence manufacture", "including final assembly", at a new or existing location within Washington State on or after the effective date of the legislation: (i) a new model of a commercial airplane or a version or variant of an existing model; and (ii) fuselages and wings for the new model of a commercial airplane or for the version or variant of an existing model.

7.287. In other words, the amendment and extension by ESSB 5952 of the aerospace tax measures are subject, for their entry into force, to a condition precedent or suspensive condition⁵⁷⁶ – a contingency – contained in the same legislation. That contingency is a positive determination by the Department of Revenue of the state of Washington, that a "significant commercial airplane manufacturing program" had been sited, between 1 November 2013 and 30 June 2017, in the state of Washington. Such a determination in turn requires that a producer commit to *manufacture* within the state of Washington the two following categories of products: (i) a commercial airplane with a carbon fibre composite fuselage, or carbon fibre composite wings, or both; and (ii) fuselages and wings for such commercial airplanes.⁵⁷⁷

⁵⁷³ ESSB 5952 (Exhibit EU-3), Section 2(2)(c), codified at RCW Section 82.32.850(2)(c) (Exhibit EU-58).

⁵⁷⁴ ESSB 5952 (Exhibit EU-3), Section 2(2)(b), codified at RCW Section 82.32.850(2)(b) (Exhibit EU-58).

⁵⁷⁵ ESSB 5952 (Exhibit EU-3), Section 2, codified at RCW Section 82.32.850 (Exhibit EU-58).

⁵⁷⁶ A condition precedent is an act or event, other than a lapse of time, that must exist or occur before a duty to perform something promised arises. See *Black's Law Dictionary*, 8th edition (2004), p. 312. A suspensive condition is one that makes a certain obligation arise only if a specified but uncertain event occurs. See *Black's Law Dictionary*, 8th edition (2004), p. 313.

⁵⁷⁷ A possible reading of the First Siting Provision is that the "significant commercial airplane manufacturing program" could consist of the manufacture (including final assembly) of a model of commercial airplane and the manufacture (including final assembly) of fuselages and wings of a *different* model of commercial airplane. In other words, under this reading, the fuselages and wings referred to in subparagraph (ii) of the provision would not need to correspond to the commercial airplane referred to in subparagraph (i). Neither party has advanced such a reading. Moreover, such a reading would assume that the

7.288. The European Union interprets the terms of the First Siting Provision as requiring Boeing "to commit to use wings and fuselages produced or assembled in Washington State in the final assembly of 777X [large civil aircraft] in Washington State".⁵⁷⁸ According to the European Union, "[i]f Boeing had not committed to using US-made wings and fuselages [it would have] thereby failed to satisfy the [First Siting Provision]".⁵⁷⁹

7.289. The Panel's reading of the text of the First Siting Provision is different. On its face, the First Siting Provision imposes a condition for certain tax benefits to take effect for a range of beneficiaries; namely, that the competent authority (the Washington State Department of Revenue) makes a one-time determination that a manufacturer has made a final decision to site a significant commercial airplane manufacturing programme in the state of Washington.

7.290. Nowhere in the words used in the First Siting Provision does the Panel find a requirement that makes the entry into force of the challenged measures contingent upon a determination that domestic goods will be used instead of imported products. Nor do the terms of the First Siting Provision impose any such requirement in respect of the "significant commercial airplane manufacturing program" that would be the basis for the Department of Revenue's determination. To the contrary, the First Siting Provision is silent as to the use of imported or domestic goods and does not make the receipt of subsidies dependent on refraining from using imported goods.

7.291. Nor can a prohibited import-substitution contingency be derived by necessary implication from the language of the First Siting Provision, in the sense that it would result inevitably from the words actually used in the legislation, or that any other interpretation would be unreasonable. The Panel sees nothing in the language of the siting contingency contained in the First Siting Provision that would *per se* and necessarily exclude the possibility for the airplane manufacturer to use wings or fuselages from outside the state of Washington⁵⁸⁰ (if, for example, it continued manufacturing *some* fuselages and wings in the state of Washington, with the additional use of fuselages and wings that were manufactured separately elsewhere). Moreover, as a condition involving a one-time decision, the First Siting Provision in itself would not prevent the manufacturer over time, and subsequent to the Department of Revenue's determination, terminating all production of wings or fuselages and only using wings and fuselages manufactured outside the state of Washington.

7.292. The Panel is mindful of the strict limitation of a *de jure* analysis to the terms actually used in the measure at issue (and any relevant facts illuminating the meaning of those words), as well as of the specific focus of the contingency that is prohibited under Article 3.1(b), namely the requirement to use domestic goods instead of imported goods. In assessing the meaning of municipal law a panel may be assisted by "evidence of the consistent application of such laws, the pronouncements of domestic courts on the meaning of such laws, the opinions of legal experts and the writings of recognized scholars"⁵⁸¹, as well as the "relevant practices of administering agencies".⁵⁸² In this case, no such evidence has been presented that would alter the Panel's assessment of the First Siting Provision for the purposes of the European Union's *de jure* claim.

7.293. The contingency set out in the terms of the First Siting Provision is not that products manufactured in the state of Washington (wings or fuselages) must be *used* in the manufacturing of commercial airplanes as a condition for receiving the subsidies, but rather that the

references to a "significant commercial airplane manufacturing program" and to a "new model, or any version or variant of an existing model, of a commercial airplane" can include two different commercial airplane models. Despite this theoretical possibility based on the terms of the First Siting Provision, such assumptions do not seem persuasive. The manufacturing activities referred to in the First Siting Provision are part of a single "manufacturing program" that is sited based on a decision taken by "a manufacturer", and there is no compelling evidence in the text of the measure or its context to suggest that this programme could involve more than one model of commercial airplane. Therefore, the Panel proceeds on the basis that the reference to fuselages and wings in subparagraph (ii) is to the same model of commercial airplane contemplated in subparagraph (i).

⁵⁷⁸ European Union's first written submission, para. 44. See also European Union's second written submission, para. 61; opening statement at the first meeting of the Panel, paras. 53-54 and 68; opening statement at the second meeting of the Panel, para. 3.

⁵⁷⁹ European Union's opening statement at the first meeting of the Panel, para. 68. See also *ibid.* para. 4; European Union's second written submission, para. 61.

⁵⁸⁰ Assuming *arguendo* that the manufacturer could use wings or fuselages manufactured separately.

⁵⁸¹ Appellate Body Report, *US – Carbon Steel*, para. 157.

⁵⁸² Appellate Body Report, *US – Countervailing and Anti-Dumping Measures (China)*, para. 4.101.

manufacturing (including by final assembly) of all of these products be *sited* within the state of Washington. The terms actually used in the provision do not preclude a scenario in which separately produced wings and fuselages were "used" in the manner alleged by the European Union, i.e. that wings and fuselages manufactured in the state of Washington were "used" in the final assembly of 777X commercial airplanes in the state of Washington. That such a scenario may be possible on the basis of terms used in the First Siting Provision, however, is not the same as concluding that it is a requirement or condition for the subsidies that necessarily derives from those terms.

7.294. One other possible and equally reasonable reading of the terms of the First Siting Provision would allow the manufacturer to benefit from the subsidies if it used wings and fuselages manufactured outside the state of Washington in the final assembly of 777X commercial airplanes in the state of Washington, so long as it manufactured at least some wings and fuselages in the state of Washington. Another possible and also reasonable reading of the terms of the First Siting Provision, as mentioned above, would allow the manufacturer to benefit from the subsidies even if it stopped manufacturing fuselages, wings, and even commercial airplanes in the state of Washington, as the First Siting Provision involves a one-time decision on the initial establishment, but not the continuation, of certain manufacturing activities.

7.295. Furthermore, and related to the above argument by the European Union, the Panel notes that there is a discrepancy between the parties whether the First Siting Provision requires the same entity to manufacture both the commercial airplane and the fuselages and wings. In particular, the European Union has argued that "the [First Siting Provision] could have been satisfied if Boeing had planned to purchase wings and fuselages produced by another entity in Washington State."⁵⁸³ Conversely, the United States has submitted that "the text of ESSB 5952 clearly contemplates a single manufacturer, and Washington officials have confirmed to the United States that this was the only scenario they contemplated".⁵⁸⁴ The Panel notes that the terms of the First Siting Provision refer to "a significant commercial airplane manufacturing program" in which a commercial airplane, as well as fuselages and wings, are manufactured. The First Siting Provision also refers to "a manufacturer" that would have to decide to locate the significant commercial airplane manufacturing programme in the state of Washington.⁵⁸⁵ Because the "manufacturing program" is the one and same programme, this strongly suggests that the manufacturer involved, namely the "manufacturer" referenced in the First Siting Provision, is the same manufacturer that would decide to site the programme in the state of Washington. In any event, regardless of the number of manufacturers that could satisfy the First Siting Provision, the terms of the provision in no case condition, either explicitly or by necessary implication, the availability of subsidies on the use of domestic over imported goods by the manufacturer or manufacturers involved. Thus, even if the First Siting Provision could have been satisfied by two different entities siting two different operations in the state of Washington, this situation would neither expressly require nor necessarily imply that domestic goods instead of imported goods would have to be used by either entity.

7.296. Accordingly, the Panel finds that a contingency upon the use of domestic over imported products is neither set out expressly in the First Siting Provision, nor can it be derived by necessary implication, in the sense that it results inevitably, from the terms used in this provision.⁵⁸⁶ The contingency on siting certain production activities within the state of Washington does not entail any explicit, or any necessarily implied, requirement to use domestic goods.

7.297. For the reasons explained above, the Panel concludes that the European Union has not demonstrated that, on its own, and based on its express terms, the First Siting Provision makes the challenged aerospace tax measures *de jure* contingent upon the use of domestic over imported goods.

⁵⁸³ European Union's opening statement at the first meeting of the Panel, para. 60.

⁵⁸⁴ United States' response to Panel question No. 62, para. 35. See also United States' response to Panel question Nos. 38, 45, and 70, paras. 91, 111, and 83.

⁵⁸⁵ See also, for example, United States' response to Panel question No. 38, paras. 91-92.

⁵⁸⁶ Whether this contingency is demonstrated by other evidence is something that the Panel will discuss in relation to the European Union's *de facto* claim below.

7.5.6.2 The Second Siting Provision, considered separately

7.298. The Panel recalls that the Second Siting Provision in Sections 5 and 6 of ESSB 5952 relates only to the B&O aerospace tax rate and provides as follows:

With respect to the manufacturing of commercial airplanes or making sales, at retail or wholesale, of commercial airplanes, this subsection (11) does not apply on and after July 1st of the year in which the department [of Revenue of the state of Washington] makes a determination that any final assembly or wing assembly of any version or variant of a commercial airplane that is the basis of a siting of a significant commercial airplane manufacturing program in the state under section 2 of this act has been sited outside the state of Washington. This subsection (11)(e)(ii) only applies to the manufacturing or sale of commercial airplanes that are the basis of a siting of a significant commercial airplane manufacturing program in the state under section 2 of this act.⁵⁸⁷

7.299. In other words, the 0.2904% B&O aerospace tax rate as amended and extended by ESSB 5952 is subject to a condition subsequent or resolutive condition⁵⁸⁸, i.e. this tax rate would cease to apply under certain defined circumstances. In particular, this condition would be activated, and the B&O aerospace tax rate terminated in respect of the manufacturing or sale of airplanes that had satisfied the First Siting Provision, if any final assembly (of an airplane) or wing assembly that was the object of a positive siting determination by the Department of Revenue of the state of Washington under the First Siting Provision, is subsequently sited outside the state of Washington.

7.300. According to the European Union, "under this [Second Siting Provision], 777X aircraft benefit from the preferential B&O tax rate only if Boeing assembles the wings and assembles the aircraft exclusively in Washington State".⁵⁸⁹ The European Union adds that, pursuant to this provision, "if Boeing opts, for example, to purchase any 777X wings from outside Washington State, it will be penalized through loss of the B&O tax rate reduction for all revenue related to sales of the 777X".⁵⁹⁰

7.301. As noted in the text of the Second Siting Provision, this provision "only applies to the manufacturing or sale of commercial airplanes that are the basis of a siting of a significant commercial airplane manufacturing program in the state under section 2 of this act", that is, under the First Siting Provision. Furthermore, by its terms, the Second Siting Provision applies only to the challenged B&O aerospace tax rate, which in turn is one of the seven aerospace tax measures that would take effect upon satisfaction of the First Siting Provision. Because the First Siting Provision defines what is referred to in the Second Siting Provision, the terms used in the Second Siting Provision necessarily draw their meaning from the terms of the First Siting Provision, including the events contemplated therein.

7.302. The Panel notes some variation in the usage of the verb "site" in the First and Second Siting Provisions, as well as potential discrepancies in the "assembly" activities that are the subject of siting in each provision. The term "siting" is defined in the First Siting Provision as "a final decision, made on or after November 1, 2013, by a manufacturer to locate a significant commercial airplane manufacturing program in Washington State". Section 2 of ESSB 5952 notes that the "definitions in this subsection apply throughout [the] section unless the context clearly requires otherwise". In this connection, the context of the First Siting Provision is different to that of the Second Siting Provision as it refers to "the siting of a significant commercial airplane manufacturing program", which in turn is "an airplane program in which" an airplane model,

⁵⁸⁷ ESSB 5952 (exhibit EU-3), Sections 5 and 6, codified at RCW Section 82.04.260(11)(e)(ii) (Exhibit EU-22).

⁵⁸⁸ A condition subsequent is one that, if it occurs, will bring something else to an end; an event the existence of which discharges a duty of performance that has arisen. See *Black's Law Dictionary*, 8th edition (2004), p. 312. A resolutive condition is one that upon fulfilment terminates an already enforceable obligation. See *Black's Law Dictionary*, 8th edition (2004), p. 313.

⁵⁸⁹ European Union's first written submission, para. 52. See also European Union's second written submission, para. 61.

⁵⁹⁰ European Union's first written submission, para. 51. See also European Union's second written submission, para. 61; opening statement at the first meeting of the Panel, paras. 61 and 68; opening statement at the second meeting of the Panel, para. 3.

fuselages, and wings are "products [that], including final assembly, will commence manufacture" in Washington State. By contrast, the Second Siting Provision does not use the term "final assembly" in conjunction with the "manufacture" of the products listed in the First Siting Provision, but rather as a discrete activity along with "wing assembly" that the Department of Revenue may determine "has been sited" outside Washington State. In the context of the Second Siting Provision, the term "final assembly" thus seems to pertain to final *aircraft* assembly, as distinguished from wing assembly, whereas "final assembly" in the First Siting Provision appears to refer to a stage or aspect of the manufacturing process of all "products" listed therein. In any event, and apart from these contextual differences of the term "final assembly", the Panel considers that the expression "has been sited" (used in the Second Siting Provision in the passive tense) is consonant with the definition of "siting" in the First Siting Provision. In particular, the reference in the Second Siting Provision to a programme having been "sited" is related to a manufacturer's decision to locate the relevant manufacturing and assembly activities in or outside Washington State.

7.303. As indicated above, the Second Siting Provision explicitly provides that the B&O aerospace tax rate will cease to apply if an assembly operation that had been sited in the state of Washington is subsequently "sited outside the state of Washington". Under the terms of the relevant legislation, to "site" is related to a manufacturer's decision to locate a manufacturing programme in a particular location.

7.304. The European Union asserts that, under the Second Siting Provision, the B&O aerospace tax rate would only continue in force "if Boeing assembles the wings and assembles the aircraft exclusively in Washington State".⁵⁹¹ The European Union adds that, pursuant to this provision, if Boeing purchases any 777X wings from outside the state of Washington, it would lose the B&O aerospace tax rate for all revenue related to sales of the 777X aircraft.⁵⁹²

7.305. Such conclusions, however, do not result explicitly from the terms of the Second Siting Provision. On its face, the Second Siting Provision is silent as to the use of imported or domestic goods and does not make the receipt or continued enjoyment of subsidies dependent on refraining from using imported products. The Panel finds no express indication in the terms of the provision that the subsidy provided by the B&O aerospace tax rate would be lost by importing wings, as alleged by the European Union. In particular, the contingency contemplated in the Second Siting Provision relates to a determination that "any final assembly or wing assembly of any version or variant of a commercial airplane that is the basis of a siting of a significant commercial airplane manufacturing program in the state under [the First Siting Provision] has been sited outside the state of Washington". Based purely on the wording of this statutory contingency, the terms "any final assembly or wing assembly" are explicitly tied, and arguably limited, to the specific assembly operations that were "the basis of a siting" under the First Siting Provision. Thus, the terms of the Second Siting Provision could rather be understood to address the situation in which production activities that had been previously sited in the state of Washington, and had been the basis of the determination by the Department of Revenue pursuant to the First Siting Provision, were subsequently sited outside the state of Washington. Seen in this light, the words of the Second Siting Provision do not expressly condition the receipt of a subsidy on the use of domestic over imported goods. On its face, the Second Siting Provision, as long as production activities of the defined type continue to take place in the state of Washington, does not require that the goods for that production (whether they be wings or anything else) need to be sourced *only* from within the state of Washington.

7.306. Nor can an import-substitution contingency be derived by necessary implication from the words of the Second Siting Provision, in the sense that such a contingency would result inevitably from the words actually used in the legislation, or that any other interpretation would be unreasonable. That is, the siting contingency contained in the Second Siting Provision would not *per se* and necessarily exclude the possibility for the airplane manufacturer to use wings from outside the state of Washington (assuming *arguendo* that the manufacturer could use wings

⁵⁹¹ European Union's first written submission, para. 52. See also European Union's second written submission, para. 61.

⁵⁹² European Union's first written submission, para. 51. See also European Union's second written submission, para. 61; opening statement at the first meeting of the Panel, paras. 61 and 68; opening statement at the second meeting of the Panel, para. 3.

manufactured separately), as long as it did not relocate the previously sited manufacturing of wings outside the state of Washington.

7.307. The Panel recalls the strict limitation of a *de jure* analysis to the terms actually used in the measure at issue and any relevant facts that illuminate the meaning of those terms in their particular context. The Panel also recalls the specific focus of the contingency that is prohibited under Article 3.1(b), namely a requirement to "use" domestic instead of imported goods. As noted above⁵⁹³, in assessing the meaning of municipal law a panel may also be assisted by evidence of the consistent application of such laws, the pronouncements of domestic courts on the meaning of such laws, the opinions of legal experts, the writings of recognized scholars, as well as the relevant practices of administering agencies. In this case, no such evidence has been presented that would alter the Panel's assessment of the Second Siting Provision for the purposes of the European Union's *de jure* claim.

7.308. The contingency set out in the Second Siting Provision is not that products manufactured in the state of Washington (wings) must be "used" in the manufacturing of commercial airplanes as a condition for the subsidy, but rather that the manufacturing (including by final assembly) of all these products not be sited outside the state of Washington.

7.309. If the Second Siting Provision is construed as relating to the relocation of a manufacturing programme previously sited under the First Siting Provision, it would not inevitably result from the terms of the Second Siting Provision that domestic goods must be used over imports. Another reading of the terms of the Second Siting Provision would allow the manufacturer in question to continue to benefit from the subsidy if it used wings manufactured outside the state of Washington in the final assembly of the commercial airplanes in question in the state of Washington, so long as it maintained final and wing assembly previously sited in the state of Washington.

7.310. In sum, and contrary to what the European Union asserts, the Second Siting Provision does not indicate on its face that the B&O aerospace tax rate would cease to apply if the aircraft manufacturer in question "uses" imported products instead of domestic products. Moreover, it does not inevitably result from the terms of the Second Siting Provision that the importation of wings would amount to the "siting" of production activities outside the state of Washington, even if such an outcome is not excluded by the text of the Second Siting Provision. No express or obvious contingency results from the terms used in the provision, nor can one be derived inevitably from its terms.

7.311. For the reasons explained above, the Panel concludes that the European Union has not demonstrated that the Second Siting Provision, on its own, and based on its express terms, makes the challenged B&O aerospace tax rate *de jure* contingent upon the use of domestic instead of imported goods.

7.5.6.3 The First Siting Provision and the Second Siting Provision, considered jointly

7.312. The European Union asserts that, taken together, the First Siting Provision and the Second Siting Provision expressly condition all of the challenged aerospace tax measures "on the use of domestic over imported goods in the final assembly of the aircraft, in violation of Articles 3.1(b) and 3.2 of the SCM Agreement".⁵⁹⁴ The European Union adds that these siting provisions "act *together* to maximize trade distortions in favour of domestic goods and to the detriment of competitive opportunities for imported goods. While the [First Siting Provision] focuses on component sourcing decisions made at the beginning of a new aircraft programme, the [Second Siting Provision] focuses on later stages".⁵⁹⁵

7.313. As noted above, the First Siting Provision and the Second Siting Provision, respectively, set out a condition for the activation of certain tax measures contained in the legislation, and a condition under which one of those tax measures (i.e. the B&O aerospace tax rate) would cease to apply. More specifically, in accordance with these provisions:

⁵⁹³ See para. 7.294 above.

⁵⁹⁴ European Union's first written submission, para. 76. See also *ibid.* para. 73.

⁵⁹⁵ European Union's opening statement at the first meeting of the Panel, para. 6. (emphasis original)
See also European Union's response to Panel question Nos. 31 and 41, paras. 71 and 98.

- a. the entry into force of the amendments and extensions to the aerospace tax measures requires a determination by the Department of Revenue of the state of Washington that a final decision has been made to site within that state a "significant commercial airplane manufacturing program", which would include the manufacture, including the final assembly of: (i) a new model of a commercial airplane or a version or variant of an existing model; and (ii) fuselages and wings for a new model of a commercial airplane or for a version or variant of an existing model; and
- b. one of the challenged aerospace tax measures (namely the 0.2904% B&O aerospace tax rate) would cease to apply if the Department of Revenue of the state of Washington makes a determination that any final assembly of airplanes or wing assembly that had been sited in the state of Washington, in accordance with the First Siting Provision, has subsequently been "sited outside the state of Washington".

7.314. On their face, the two siting provisions, and the respective conditions contained therein, provide for the "siting" of certain manufacturing activities within the state of Washington as a condition for the enjoyment of a number of tax benefits and seek to prevent certain manufacturing activities that had been sited within the state of Washington being subsequently sited outside the state of Washington. Under the terms of the First Siting Provision, the term "siting" refers to a manufacturer's decision to locate a manufacturing programme (the "significant commercial airplane manufacturing program") in a particular location (in the state of Washington).

7.315. As the Panel has found above, the First Siting Provision and the Second Siting Provision are silent as to the use of imported or domestic goods. On their face, these provisions do not make the receipt or continued enjoyment of subsidies dependent on refraining from using imported products. Such conditionality does not result explicitly from the terms of the provisions, nor can it be derived by necessary implication, in the sense that it results inevitably, from such terms. On a *de jure* basis these provisions do not speak of "component sourcing decisions"⁵⁹⁶, but of the location of certain manufacturing activities.

7.316. Furthermore, while the Second Siting Provision pertains explicitly to the "sited" programme that would have satisfied the First Siting Provision, this textual link between the two siting provisions adds nothing to the *de jure* analysis of each of the provisions separately that the Panel has already conducted. Considering them jointly does not produce any elements that might have been obscured by considering them separately. Therefore, the Panel finds that the terms of the First Siting Provision and the Second Siting Provision, taken together, do not condition the challenged aerospace tax measures on the use of domestic over imported goods. Whether *in practice*, as also argued by the European Union, these two siting provisions act together to create a contingency on the use of domestic goods over imported goods, is something that the Panel will turn to as part of its consideration of the European Union's *de facto* claim against the measures at issue.

7.317. Accordingly, the Panel concludes that the European Union has not demonstrated that, acting together, the First Siting Provision and the Second Siting Provision make the challenged aerospace tax measures *de jure* contingent upon the use of domestic over imported goods.

7.5.7 Whether the subsidies are *de facto* contingent upon the use of domestic over imported goods

7.318. The Panel has found that the European Union has failed to establish that the challenged aerospace tax measures are *de jure* contingent upon the use of domestic over imported goods. The Panel will now consider the European Union's secondary claim, i.e. that the aerospace tax measures at issue are inconsistent with Article 3.1(b) of the SCM Agreement by being *de facto* contingent upon the use of domestic over imported goods. In its assessment of this claim, the Panel will determine whether the contingency or conditionality of the aerospace tax measures on the use of domestic goods instead of imported goods, even if not set out *expressly* in the legislation, including by necessary implication, is demonstrated by the facts of the case.

⁵⁹⁶ See, for example, European Union's opening statement at the first meeting of the Panel, para. 6; response to Panel question Nos. 31 and 41, paras. 71 and 98.

7.5.7.1 Legal standard

7.319. There are no specific precedents on the criteria that would guide the Panel's determination of a *de facto* import substitution contingency under Article 3.1(b). However, as discussed above, the Appellate Body has referred to elements that would be considered for a *de facto* determination of export contingency under Article 3.1(a). For the reasons explained above, these elements are also relevant for a contingency determination under Article 3.1(b).⁵⁹⁷

7.320. In summary, the legal standard expressed by the word "contingent" is the same for both *de jure* or *de facto* contingency.⁵⁹⁸ However, there is a difference in the type of evidence that may be employed to establish *de jure* or *de facto* contingency. *De jure* contingency is demonstrated on the basis of the words of the relevant legislation, regulation or other legal instrument. The evidence needed to establish *de facto* contingency goes beyond the relevant legal instruments and includes a variety of factual elements concerning the granting of the subsidy in a specific case.⁵⁹⁹ *De facto* contingency must be established from the total configuration of the facts constituting and surrounding the granting of the subsidy, including the design, structure, and modalities of operation of the measure granting the subsidy, none of which on its own is likely to be decisive in any given case.⁶⁰⁰ That configuration of the facts may include the following factors: (i) the design and structure of the measure granting the subsidy; (ii) the modalities of operation set out in such a measure; and (iii) the relevant factual circumstances surrounding the granting of the subsidy that provide the context for understanding the measure's design, structure, and modalities of operation.⁶⁰¹ Moreover, the determination of contingency must be based on an assessment of *the subsidy itself*, in the light of the relevant factual circumstances, rather than by reference to the granting authority's subjective motivation for the measure. Reviewable expressions of a government's policy objectives for granting a subsidy may, however, constitute relevant evidence in the inquiry.⁶⁰²

7.321. For the Panel to find a violation of Article 3.1(b) of the SCM Agreement, the European Union will need to make a *prima facie* case that the aerospace tax measures are granted subject to the condition that domestic products must be used instead of, or in preference to, imported products. It would not be sufficient to demonstrate, for example, that a subsidy is being granted to a firm that uses domestic instead of imported goods or even that the subsidy would negatively affect the competitive opportunities of foreign producers. Such facts would not in themselves support a determination that the challenged measures are subject to a prohibited contingency (although they might be relevant in the context of actions pursuant to Parts III and V of the SCM Agreement). Rather, the European Union will need to demonstrate that there is something about the design and structure of the challenged measures and their operation, in the circumstances in which the measures have been introduced and exist, that establishes the contingency, and does so with the requisite standard of certainty. The Panel recalls, in this regard, the Appellate Body's warning against blurring "the line drawn by the [SCM] Agreement between *prohibited ... subsidies and actionable ... subsidies*", in a manner "contrary to the overall design and structure of the Agreement".⁶⁰³

7.5.7.2 The Panel's approach to address the European Union's claim

7.322. The European Union asserts that the text of ESSB 5952, and in particular the language of the First Siting Provision and the Second Siting Provision, is the most important fact on record and the best evidence of the design, structure, and modalities of operation of the challenged subsidies and the associated contingencies.⁶⁰⁴

⁵⁹⁷ See Appellate Body Report, *Canada – Autos*, para. 123. See also paras. 7.211 and 7.212 above.

⁵⁹⁸ Appellate Body Report, *Canada – Aircraft*, para. 167.

⁵⁹⁹ Ibid. and Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1038.

⁶⁰⁰ Appellate Body Reports, *Canada – Aircraft*, para. 167; *EC and certain member States – Large Civil Aircraft*, para. 1051.

⁶⁰¹ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1046.

⁶⁰² Ibid. paras. 1051-1052.

⁶⁰³ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1054. (emphasis original)

⁶⁰⁴ European Union's response to Panel question Nos. 29 and 68, paras. 29 and 45-46. See also European Union's second written submission, paras. 90-91.

7.323. In addition to the text of ESSB 5952, the European Union cited the following four factors in support of its *de facto* claim: first, statements and testimony by the Governor of the state of Washington, referring to the "contingency language" included in the legislation⁶⁰⁵; second, that Boeing imports wings from Japan for its 787 aircraft⁶⁰⁶; third, that, prior to the enactment of ESSB 5952, Boeing would have considered the possibility of importing wings from Japan for its 777X aircraft and decided against that option once ESSB 5952 was enacted⁶⁰⁷; and fourth, that ESSB 5952 "creates specific multi-billion dollar *penalties* for use of imported wings or fuselages, and multi-billion dollar *rewards* for use of domestic wings or fuselages".⁶⁰⁸

7.324. The European Union submits that the First Siting Provision and the Second Siting Provision in ESSB 5952 are each capable of strongly influencing Boeing's choice between imported wings and fuselages, and domestic (United States-produced) wings and fuselages for the 777X airplanes.⁶⁰⁹ The European Union asserts that the amount of the subsidies at issue exceeds the total development cost of the 777X airplanes, and would therefore overshadow any other factors that may favour a decision by Boeing to import wings and fuselages for 777X airplanes.⁶¹⁰ The European Union maintains that the First Siting Provision and the Second Siting Provision acting together would maximize trade distortions in favour of domestic goods and to the detriment of imported goods, which suggests that the challenged measures are geared to induce the use of domestic over imported goods.⁶¹¹

7.325. In response, the United States asserts that the European Union has failed to establish that the aerospace tax measures at issue are *de facto* contingent upon the use of domestic over imported goods, because the European Union has not demonstrated that the use of domestic goods is required as a condition for eligibility for the subsidies.⁶¹² According to the United States, none of the factual evidence referred to by the European Union (the text of ESSB 5952; the statement of the Governor of the state of Washington; Boeing's alleged importation of wings from Japan for its 787 airplanes; Boeing's alleged consideration of importing wings from Japan for its 777X airplanes; and the alleged system of rewards and penalties in ESSB 5952) supports its claim that the measures are *de facto* contingent.⁶¹³

7.326. The United States argues that Boeing has fulfilled the First Siting Provision and has avoided triggering the Second Siting Provision without the use of domestic over imported goods.⁶¹⁴ According to the United States, Boeing does not "use" domestic wings and fuselages and instead completes the assembly of wings and fuselages as part of the final assembly of the finished airplane.⁶¹⁵ The United States adds that the measures in ESSB 5952 have had no effect on Boeing's make/buy decisions nor on its decision on where to site the assembly of fuselages and

⁶⁰⁵ European Union's second written submission, para. 91; response to Panel question Nos. 29 and 68, paras. 67 and 45 and 47. See also Office of Washington Governor, "Legislature approves key elements of 777X incentive package", 10 November 2013 (Exhibit EU-59); and Washington State House Finance Committee, Video, "Testimony of Governor Inslee before House Finance Committee", 7 November 2013 (Exhibit EU-110).

⁶⁰⁶ European Union's first written submission, para. 75; second written submission, paras. 91 and 95-96; opening statement at the first meeting of the Panel, paras. 66-67; response to Panel question Nos. 29 and 68, paras. 67 and 45 and 48.

⁶⁰⁷ European Union's second written submission, para. 91; opening statement at the first meeting of the Panel, para. 73; response to Panel question Nos. 29 and 68, paras. 67 and 45 and 48. See also Reuters, "Boeing hopeful of 777X deal, may build wings in Japan if rejected", 11 November 2013 (Exhibit EU-83).

⁶⁰⁸ European Union's second written submission, para. 91; opening statement at the first meeting of the Panel, para. 74; response to Panel question Nos. 29, 31, and 68, paras. 67, 70, and 45. (emphasis original) See also European Union's second written submission, para. 2; response to Panel question Nos. 33 and 68, paras. 71, 85, and 46.

⁶⁰⁹ European Union's first written submission, para. 77; second written submission, para. 90. See also European Union's second written submission, para. 91; opening statement at the first meeting of the Panel, paras. 67-69 and 72-73; response to Panel question No. 29, paras. 66-67; Reuters, "Boeing seen in advanced talks to make 777X near Seattle", 4 November 2013 (Exhibit EU-65).

⁶¹⁰ European Union's second written submission, para. 90. See also *ibid*, para. 91; opening statement at the first meeting of the Panel, para. 73; response to Panel question No. 29, paras. 66-67; Reuters, "Boeing seen in advanced talks to make 777X near Seattle", 4 November 2013 (Exhibit EU-65).

⁶¹¹ European Union's first written submission, paras. 77-78; opening statement at the first meeting of the Panel, paras. 6 and 70-74; response to Panel question Nos. 30, 31 and 41, paras. 68-71 and 98.

⁶¹² United States' second written submission, para. 58.

⁶¹³ United States' second written submission, paras. 78-83.

⁶¹⁴ *Ibid.* para. 58.

⁶¹⁵ United States' second written submission, paras. 59-63. See also response to Panel question No. 64, para. 56.

wings.⁶¹⁶ The United States contends that the European Union has failed to establish that the challenged measures are geared to induce the use of domestic over imported goods.⁶¹⁷ The United States submits that, provided it conducts the requisite assembly activity in the state of Washington, Boeing would satisfy the First Siting Provision and avoid triggering the Second Siting Provision even if it imported every part of the 777X airplane; Boeing therefore would be receiving no rewards for increasing the use of domestic inputs on the 777X airplane, nor would it be penalized for increasing the use of imported inputs.⁶¹⁸ Finally, the United States argues that, if the challenged measures are not found to be *de jure* contingent upon import substitution, to show that they are *de facto* contingent upon import substitution would typically involve at a minimum showing that the measures are having an import substitution effect.⁶¹⁹

7.327. In its assessment of the European Union's *de facto* claim against the challenged aerospace tax measures, the Panel will consider whether the text of the relevant legislation, the factors cited by the European Union, and other evidence on the record, support the European Union's assertion that the aerospace tax measures are contingent upon the use of domestic over imported goods. The Panel's *de facto* analysis must go beyond the text of the legislation and will be based on a holistic examination of all the available evidence. The Panel will consider in this regard the total configuration of the facts constituting and surrounding the granting of the subsidies, such as: (i) the design and structure of the measures; (ii) the modalities of operation set out in such measures; and (iii) the relevant factual circumstances surrounding the granting of the subsidies that provide the context for understanding the measures' design, structure, and modalities of operation.

7.328. The Panel recalls that, with respect to the European Union's *de jure* claim, the Panel started by analysing the First Siting Provision and the Second Siting Provision, each considered separately, and subsequently considered the two siting provisions acting jointly.⁶²⁰ Because the consideration of the European Union's *de jure* claim focused on the terms of the legislation, the Panel considered it appropriate to look at the siting provisions separately and to look subsequently at both provisions jointly. This approach was consistent with the manner in which the European Union directed its *de jure* claim at the provisions "whether considered individually or together".⁶²¹ The European Union further clarified its argument as follows:

To be clear, the European Union understands that each condition [First Siting Provision and Second Siting Provision] *independently* results in a *de jure* violation of Article 3.1(b). At the same time, these conditions act *together* to maximize trade distortions in favour of domestic goods, and to the detriment of competitive opportunities for imported goods.⁶²² (emphasis original; footnote omitted)

7.329. With respect to its *de facto* claim, the European Union has asserted that the First Siting Provision and the Second Siting Provision in ESSB 5952 "are each capable of strongly influencing Boeing's choice between imported wings and fuselages, and US-produced wings and fuselages, for the 777X [airplanes]".⁶²³ In contrast, in articulating its arguments in support of its *de facto* claim, the European Union has consistently referred to the joint operation of the two siting provisions.⁶²⁴

7.330. For purposes of determining the practical operation of the challenged measures, the Panel considers that it would be artificial to look at the siting provisions separately. Not only are both

⁶¹⁶ United States' second written submission, paras. 64-71 and 84.

⁶¹⁷ United States' first written submission, paras. 105 and 132-140; second written submission, paras. 72-74; response to Panel question No. 30, paras. 65-67.

⁶¹⁸ United States' second written submission, paras. 75-77.

⁶¹⁹ United States' response to Panel question No. 74, para. 111.

⁶²⁰ See para. 7.283 above.

⁶²¹ European Union's first written submission, para. 73; second written submission, para. 60; opening statement at the first meeting of the Panel, para. 6, fn 8.

⁶²² European Union's opening statement at the first meeting of the Panel, para. 6.

⁶²³ European Union's second written submission, para. 90. See also European Union's first written submission, para. 77; second written submission, para. 91; opening statement at the first meeting of the Panel, paras. 72-73; response to Panel question No. 29, paras. 66-67; Reuters, "Boeing seen in advanced talks to make 777X near Seattle", 4 November 2013 (Exhibit EU-65).

⁶²⁴ European Union's second written submission, paras. 91, 98; opening statement at the first meeting of the Panel, paras. 67, 70-74; response to Panel question Nos. 31, 41, 68, and 76, paras. 70-71, 98, 45, and 55.

provisions part of the same legal instrument (ESSB 5952), in practice both operate together in regulating the conditions for obtaining and then maintaining access to the subsidies at issue in this dispute. Recalling the textual linkage in the legislation of the two siting provisions (the reference in the Second Siting Provision to the significant commercial airplane programme that had satisfied the First Siting Provision), the First Siting Provision having been satisfied by Boeing's 777X siting decision, the joint operation in practice of the two siting provisions can be examined and, as a practical matter, their operation cannot at this point be dissociated.

7.331. The Panel will therefore consider the manner in which the measures at issue are structured, designed, and operate, under the terms of ESSB 5952, and as a result of the First Siting Provision and the Second Siting Provision. As noted, this approach is consistent with the manner in which the European Union has articulated its *de facto* claim, namely by reference to the joint operation of the two siting provisions.

7.5.7.3 The First and Second Siting Provisions

7.332. The Panel recalls that, based on the terms used in the legislation, for the aerospace tax measures to take effect, the First Siting Provision requires a determination by Washington State's Department of Revenue that a final decision has been made, on or after 1 November 2013 and no later than 30 June 2017, to site a "significant commercial airplane manufacturing program" within the state of Washington. The legislation also defines the characteristics that the "significant commercial airplane manufacturing program" would have to fulfil to qualify for the Department of Revenue's positive determination. Those characteristics are, in essence, that the following products will "commence manufacture", "including final assembly", at a new or existing location within Washington State on or after the effective date of the legislation: (i) a new model of a commercial airplane or a version or variant of an existing model; and (ii) fuselages and wings for a new model of a commercial airplane or for a version or variant of an existing model.

7.333. In turn, based on the terms used in the legislation, the B&O aerospace tax rate will cease to apply in respect of "the manufacturing or sale of commercial airplanes" that had satisfied the First Siting Provision if Washington State's Department of Revenue makes a determination that any final airplane assembly or wing assembly (that had been the object of a positive siting determination by the Department of Revenue under the First Siting Provision) has subsequently been sited outside the state of Washington.

7.334. The European Union interprets the terms of the First Siting Provision as requiring Boeing "to commit to use wings and fuselages produced or assembled in Washington State in the final assembly of 777X [large civil aircraft] in Washington State".⁶²⁵ According to the European Union, "[i]f Boeing had not committed to using US-made wings and fuselages [it would have] thereby failed to satisfy the [First Siting Provision]".⁶²⁶

7.335. According to the European Union, under the Second Siting Provision, "777X aircraft benefit from the preferential B&O tax rate only if Boeing assembles the wings and assembles the aircraft exclusively in Washington State".⁶²⁷ The European Union adds that, pursuant to this provision, "if Boeing opts, for example, to purchase any 777X wings from outside Washington State, it will be penalized through loss of the B&O tax rate reduction for all revenue related to sales of the 777X".⁶²⁸

⁶²⁵ European Union's first written submission, para. 44. See also European Union's second written submission, para. 61; opening statement at the first meeting of the Panel, paras. 53-54 and 68; opening statement at the second meeting of the Panel, para. 3.

⁶²⁶ European Union's opening statement at the first meeting of the Panel, para. 68. See also *ibid.* para. 4; European Union's second written submission, para. 61.

⁶²⁷ European Union's first written submission, para. 52. See also European Union's second written submission, para. 61.

⁶²⁸ European Union's first written submission, para. 51. See also European Union's second written submission, para. 61; opening statement at the first meeting of the Panel, para. 61; opening statement at the second meeting of the Panel, para. 3.

7.336. The European Union adds that the siting provisions in ESSB 5952 "are geared to induce the use of domestic over imported goods".⁶²⁹ According to the European Union:

[T]hese conditions [the First Siting Provision and the Second Siting Provision] act *together* to maximize trade distortions in favour of domestic goods, and to the detriment of competitive opportunities for imported goods.⁶³⁰ While the [First Siting Provision] focuses on component sourcing decisions made at the beginning of a new aircraft programme, the [Second Siting Provision] focuses on later stages.⁶³¹ (emphasis original)

7.337. The European Union adds that the siting provisions in ESSB 5952 influence the choice by an individual producer on how to produce an aircraft and source its wings and fuselages, as follows:

In the absence of the contingencies, Boeing would have arrived at a decision as a reasonable commercial actor, which may or may not have been to use wings and fuselages produced outside the United States. [ESSB 5952] distorts these choices. First, it takes away the *competitive opportunity* for foreign producers of wings and fuselages, pursuant to the [First Siting Provision]. If Boeing had not committed to using US-made wings and fuselages, and thereby failed to satisfy the [First Siting Provision], that would have led to severe penalties for Boeing, as the entirety of [ESSB 5952] would not have gone into effect. Second, it further takes away the *competitive opportunity* for foreign wing producers, pursuant to the [Second Siting Provision]. If Boeing uses any foreign-made wings for the 777X, and thereby fails to satisfy the [Second Siting Provision], then the 777X-related portion of the B&O tax rate reduction will be eliminated.⁶³²

7.338. The United States asserts that the relevant conditions in ESSB 5952 (namely, the First Siting Provision and the Second Siting Provision) have "nothing whatsoever to do with the use of goods" and instead "address aerospace-related production activities".⁶³³ The United States also argues that "the references to manufacturing or assembly of fuselages and wings in the Siting Provisions ... merely define the scope of production activity required to use the tax treatment covered by ESSB 5952".⁶³⁴

7.339. The Panel has already concluded that, on its face, the First Siting Provision imposes a condition for certain tax benefits to take effect for a range of beneficiaries, namely, that the competent authority (the Washington State Department of Revenue) make a one-time determination that a manufacturer has made a final decision to site a significant commercial airplane manufacturing programme in the state of Washington. The Panel also has concluded that the First Siting Provision does not, either by its express terms or by necessary implication thereof, make the entry into force of the subsidies at issue contingent upon a determination that domestic goods will be used instead of imported goods.⁶³⁵

7.340. The Panel has concluded further that, on its face, the Second Siting Provision is silent as to the use of imported or domestic goods and does not expressly or by necessary implication make the receipt or continued enjoyment of subsidies dependent on refraining from using imported goods. The Panel also found no indication in the terms of the provision that the subsidy provided by the B&O aerospace tax rate would be lost by importing wings, as alleged by the European Union. The Panel concluded that the Second Siting Provision does not, either by its

⁶²⁹ European Union's opening statement at the first meeting of the Panel, para. 70. See also European Union's response to Panel question No. 30, paras. 68-69.

⁶³⁰ (footnote original) European Union's opening oral statement, para. 6.

⁶³¹ European Union's response to Panel question No. 31, para. 71.

⁶³² European Union's opening statement at the first meeting of the Panel, para. 68.

⁶³³ United States' first written submission, paras. 1-2. See also *ibid.* paras. 4, 7, 9, 73, 101, and 106-109; second written submission, paras. 2 and 38; opening statement at the first meeting of the Panel, paras. 4 and 23.

⁶³⁴ United States' second written submission, para. 38.

⁶³⁵ See paras. 7.291 and 7.292 above.

express terms or by necessary implication, condition the receipt of the B&O aerospace tax rate on the use of domestic over imported goods.⁶³⁶

7.341. The Panel recalls the European Union's argument that the siting provisions focus on "component sourcing decisions".⁶³⁷ The Panel has found that the First and Second Siting Provisions *de jure* do not speak of component sourcing decisions, but of the location of certain manufacturing activities.⁶³⁸ However, this does not resolve whether on a *de facto* basis these provisions operate in a manner that conditions the availability of subsidies based on whether certain components are sourced from a foreign or domestic origin. It is in respect of this question of "component sourcing decisions" that the Panel will examine the European Union's claim of *de facto* contingency on the use of domestic over imported goods.

7.342. Turning to the actual operation of the challenged measures, the evidence before the Panel confirms that the First Siting Provision in itself did not and does not make the aerospace tax measures contingent upon the use of domestic goods instead of, or in preference to, imported goods. As noted above⁶³⁹, the First Siting Provision was activated by the Washington State Department of Revenue on 10 July 2014. This activation was a result of a determination by the Department of Revenue that a manufacturer (namely, Boeing) had made a final decision to site a significant commercial airplane manufacturing programme (namely, the 777X programme) in the state of Washington and that the contingency requirements in ESSB 5952 had therefore been satisfied. As a result of this determination, ESSB 5952 was deemed to have taken effect on 9 July 2014.⁶⁴⁰ The Department of Revenue's determination in turn was based on Boeing's notification of 9 July 2014 that it had made a final decision to manufacture the 777X airplane, including its fuselages and wings, in the state of Washington.⁶⁴¹ Boeing's notification was accompanied by three attachments, as examples of "actions Boeing has taken consistent with its decision to manufacture the 777X in Washington".⁶⁴² As a result of the Department of Revenue's determination and the entry into effect of ESSB 5952, the expiration date for the aerospace tax measures at issue was extended until 1 July 2040 for all eligible taxpayers, including but not limited to Boeing.⁶⁴³

7.343. Under the terms of the legislation, and as confirmed by the additional evidence available, the Department of Revenue's determination was based exclusively on Boeing's decision to locate a significant commercial airplane manufacturing programme (as defined by the legislation) in the state of Washington.⁶⁴⁴ There is no indication that the activation of the First Siting Provision was the result of any other factor, such as a commitment by the manufacturer to use domestic over imported goods.

7.344. In particular, the European Union has submitted no evidence, and there is nothing in either Boeing's letter to the Department of Revenue or the Department of Revenue's determination, that indicates that the use of domestic over imported goods – by Boeing or anyone else – was a condition for the Department of Revenue's positive determination in respect of the First Siting Provision. In fact, undisputed evidence submitted by the United States shows that Boeing will source a significant number of the components for the 777X, including wing and fuselage components and subassemblies, outside the United States.⁶⁴⁵ In any event, there is no evidence to

⁶³⁶ See paras. 7.308 and 7.313 above.

⁶³⁷ See, for example, European Union's opening statement at the first meeting of the Panel, para. 6; response to Panel question Nos. 31 and 41, paras. 71 and 98.

⁶³⁸ See para. 7.317 above.

⁶³⁹ See para. 7.40 above.

⁶⁴⁰ Letter from the Director of the Washington State Department of Revenue to the Code Reviser, 10 July 2014 (Exhibit EU-61). See also United States' response to Panel question Nos. 10 and 12, paras. 21 and 26.

⁶⁴¹ Boeing letter to the Director of the Washington State Department of Revenue, 9 July 2014 (Exhibit USA-32) (BCI). See also United States' response to Panel question No. 10, paras. 20-21.

⁶⁴² Boeing letter to the Director of the Washington State Department of Revenue, 9 July 2014 (Exhibit USA-32) (BCI).

⁶⁴³ United States' first written submission, para. 78 (citing letter from the Director of the Washington State Department of Revenue to the Code Reviser, 10 July 2014 (Exhibit EU-61)); response to Panel question No. 12, para. 26.

⁶⁴⁴ See Letter from the Director of the Washington State Department of Revenue to the Code Reviser, 10 July 2014 (Exhibit EU-61). See also para. 7.40 above.

⁶⁴⁵ See, for example, Boeing expert statement (Exhibit USA-1) (BCI), paras. 41-42, 50-52, and 59-60; Boeing, Make/Buy Model 777-300ER, July 2007 (Exhibit USA-2) (BCI); Boeing, 777X Make/Buy, All

indicate that a particular use of goods of specific origins formed part of the Department of Revenue's determination that the First Siting Provision had been fulfilled. The Panel thus sees no factual evidence in the Department of Revenue's determination or in how Boeing will organize the sourcing for the production of the 777X indicating a *de facto* requirement to use any domestic goods, including wings or fuselages as referred to specifically in the European Union's claim of *de facto* contingency.

7.345. With respect to the First Siting Provision, the Panel additionally notes that the Department of Revenue's determination, pursuant to this provision, is a one-time decision and there is no legal mechanism under Washington State law that would allow the Department of Revenue to revoke that determination.⁶⁴⁶ Thus, the First Siting Provision is not a measure whose operation will occur in repeated instances over some (definite or indefinite) period. Pursuant to ESSB 5952, there will be no other instance of this particular legislative provision being activated (again) in respect of another commercial airplane programme. The First Siting Provision established the possibility for a one-time creation of certain tax benefits subject to a certain condition being fulfilled. That condition was in fact fulfilled, such that the tax benefits in fact did take effect, and these events exhausted the operational life of the First Siting Provision. Thus, the evidence regarding the satisfaction, in July 2014, of the First Siting Provision by the Boeing 777X programme constitutes the entire universe of relevant evidence regarding that provision's operation.

7.346. While the operation of the First Siting Provision as such was a one-time event creating extended availability of a package of tax benefits, and while the Panel finds no factual evidence of any requirement to use domestic goods in respect of the triggering of that availability, the Panel recalls that the First Siting Provision does not exist in isolation. To the contrary, the role of the Second Siting Provision is to establish conditions for the airplane manufacturing programme that had activated the First Siting Provision (and thus effected the extended availability of the tax benefits) to maintain that programme's access to one of those tax benefits, namely the B&O aerospace tax rate. To put this more precisely, given that the conditionality in the Second Siting Provision is phrased in the negative, the Panel understands the Second Siting Provision to set forth the factual circumstances that would, if they arose, cause the airplane manufacturing programme that had satisfied the First Siting Provision (namely, the 777X programme) to lose access to the B&O aerospace tax rate. These, then, are the conditions or circumstances that Boeing must avoid in respect of the 777X programme in order not to lose access to that tax rate in respect of that programme.

7.347. The Panel thus will now consider the manner of operation of this second set of conditions attached to the subsidy. In particular, the Panel will examine in detail the facts concerning the manner in which the Second Siting Provision operates in practice in respect of the 777X programme which, having satisfied the First Siting Provision, is the sole and exclusive object of the Second Siting Provision. As its analytical framework, the Panel will consider the design, structure, and operation of the measures granting the subsidies, the modalities of operation as set forth in the measures, and the relevant factual circumstances surrounding the granting of the subsidies at issue, that provide context for understanding the measures' design, structure and operation. In that regard, the additional evidence surrounding the Department of Revenue's determination to activate the First Siting Provision can also serve to inform the factual circumstances in which the Second Siting Provision now operates. The Panel notes in particular the following facts in this regard.

7.348. First, the relevant legislation grants discretion to the Department of Revenue to determine both: (i) that a manufacturer made a final decision to site a significant commercial airplane manufacturing programme in the state of Washington; and (ii) that any final airplane assembly or wing assembly previously sited in the state of Washington, and which was the subject of the Department of Revenue's determination as described in (i) above, has subsequently been sited outside the state of Washington. To recall, the Department of Revenue's determination of the original siting decision, under the First Siting Provision, was designed to be, and in fact operated, as a one-time determination, and there is no legal mechanism under Washington State law that would allow the Department of Revenue to revoke that determination once made.⁶⁴⁷ That said,

Commodities, Status as of 17 December 2014 (Exhibit USA-8) (BCI); Boeing, 777X Content Sources, Major Structures & Propulsion, Status as of 27 October 2015 (Exhibit USA-30) (BCI).

⁶⁴⁶ See United States' response to Panel question No. 12, para. 26.

⁶⁴⁷ See paras. 7.273 and 7.347 above.

under the Second Siting Provision, the Department of Revenue could exercise its discretion to make a determination as described in (ii) above at any point in the period during which the B&O aerospace tax rate is in effect under ESSB 5952. Such a determination would lead to the termination of this subsidy for the previously sited airplane programme as of 1 July of the year in which that second determination was made. A determination as described in (ii) above would only affect the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under the airplane manufacturing programme in question. It would not affect any of the other subsidies to the manufacturer in question, nor would it affect any of the subsidies (including the B&O aerospace tax rate) for any of the other beneficiaries in respect of other activities.

7.349. Second, the condition contained in the First Siting Provision is to site the manufacture of certain "products" in Washington State, namely: (i) a new model, or a version or variant of an existing model, of a commercial airplane manufactured with a carbon fibre composite fuselage or carbon fibre composite wings or both; and (ii) fuselages and wings for a new model of a commercial airplane, or a version or variant of an existing model. In contrast, the condition contained in the Second Siting Provision is to refrain from siting outside of Washington State any final assembly or wing assembly of a manufacturing programme that had previously been sited under the First Siting Provision. The Panel notes that it is the Second Siting Provision's reference to wing assembly, rather than final assembly, that is relevant to the European Union's claim of *de facto* contingency to use domestic over imported wings.⁶⁴⁸ This condition of the Second Siting Provision with respect to the siting of any wing assembly is in force for the entirety of the period during which the B&O aerospace tax rate is in effect under ESSB 5952.⁶⁴⁹ Accordingly, the Panel understands that, under the Second Siting Provision, if the manufacturer were to relocate outside Washington State the wing assembly of the "significant commercial airplane manufacturing program" that had been previously sited in Washington State in accordance with the First Siting Provision (namely, the 777X programme), the legal consequence would be the termination of the availability of the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under that programme.

7.350. Third, the parties have discussed extensively the process of producing wings for large civil aircraft and, specifically, the incorporation of wings into the final production or final assembly of large civil aircraft. The evidence before the Panel reflects a variety of aircraft manufacturing processes, as well as continuing innovation within the aerospace industry, including for the development of the 777X itself.⁶⁵⁰ The Panel notes in this regard the United States' observation that there is great variation in the process of producing large commercial airplanes.⁶⁵¹ Accordingly, the available evidence suggests that manufacturers can decide on specific processes for producing wings, including by assembly, and for incorporating wings into the final production or final assembly of large civil aircraft based on a number of factors, including economic, business, logistical, and technological considerations.

7.351. Fourth, as part of their discussion on the process of producing wings for large civil aircraft, the parties advanced different definitions of what can be considered as a "wing" for a large civil aircraft. Different large civil aircraft models have wings with different designs, sizes, and technical characteristics. As is clear from the available evidence, some large aircraft models have been produced using wing components or wing structures in different stages of completion that were

⁶⁴⁸ See, for example, European Union's response to Panel question No. 50, paras. 132-133; comments on United States' response to Panel question Nos. 69 and 77, paras. 63 and 85-89.

⁶⁴⁹ In this respect, the Panel notes the United States' argument that there is no prohibited contingency in this case based on the fact that Boeing's 777X programme has satisfied the First Siting Provision and has not triggered the Second Siting Provision. See, for example, United States' opening statement at the second meeting of the Panel, paras. 46-47. Although this argument rests on particular aspects of 777X production in relation to the United States' interpretation of the terms "use" and "goods" in Article 3.1(b), it also raises an important aspect of the combined operation of the First and Second Siting Provisions. Necessarily, by the terms of the legislation, a programme that satisfies the First Siting Provision would not at that moment trigger the Second Siting Provision. The latter would only be triggered at a later point in time, if the circumstances underlying the original siting determination by the Department of Revenue have changed in the manner specified in the Second Siting Provision.

⁶⁵⁰ See, e.g. Boeing expert statement (Exhibit USA-1) (BCI), para. 39 ("The 777X is designed to be the largest and most efficient twin-engine commercial aircraft in aerospace history"). See also United States' response to Panel question No. 64, para. 57; European Union's response to Panel question No. 64, paras. 37-39; Boeing Frontiers, "The 747-700 will be transformed into an even larger freighter", June 2005 (Exhibit EU-122).

⁶⁵¹ United States' response to Panel question No. 64, para. 57.

produced separately from the rest of the airplane and, in some cases, transported to the site of the final airplane assembly.⁶⁵² In any event, an examination of the available evidence suggests that manufacturers of large civil aircraft can incorporate wing structures into the process of final assembly at different levels of completion based on a number of factors, including economic, business, logistical, and technological considerations.

7.352. More generally, regarding the diversity of ways in which manufacturers may assemble large civil aircraft, the United States noted that "[i]n fact, the evidence shows that what these [aircraft manufacturing] programs really have in common is that they all end up with fuselages and wings on the finished airplanes, which is not surprising because they are the main structural elements of the airframe."⁶⁵³ Thus, whatever manufacturing and assembly process is chosen by a particular manufacturer, the result of that process will be a finished aircraft and the result of wing assembly, however performed, will be a finished wing. Notably, the Second Siting Provision refers to the location of "wing assembly" as the subject of a possible determination by the Department of Revenue, and the text of ESSB 5952 uses the word "products" when referring to commercial airplanes, fuselages, and wings that would have to be manufactured within Washington State as part of the "significant commercial airplane manufacturing program" under the First Siting Provision.⁶⁵⁴

7.353. Fifth, the Panel notes the United States' argument that Boeing does not use fuselages or wings, and has no plans to use fuselages or wings, since the wings for 777X aircraft "are only completed as part of the output of the process of producing the aircraft itself".⁶⁵⁵ The Panel understands from this argument that Boeing is expected to assemble the wings of the 777X itself, rather than sourcing wings from another entity, domestic or foreign. In this connection, the United States clarified that "its argument is not that, as a general matter, it is impossible to assemble any aircraft wings separate from the final assembly of any aircraft".⁶⁵⁶ **[[BCI]]**.⁶⁵⁷

7.354. In any event, the particular production process selected by Boeing for the 777X airplane is not in itself dispositive of whether the legislation creates *de facto* a prohibited contingency on Boeing to use domestic goods. The fact that a manufacturer has chosen a particular production process in the past or operates that process in the present, including because of economic, business, logistical, or technological factors, does not mean that alternative processes may not be available now or in the future. In this respect, it is relevant that ESSB 5952 extends the subsidies provided pursuant to the aerospace tax measures until 2040. During the entirety of this period, the conditions in the Second Siting Provision govern the availability of the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under the 777X programme.

7.355. Furthermore, the Panel recognizes that neither the First Siting Provision nor the Second Siting Provision, either explicitly or in their operation, binds Boeing to a specific process for manufacturing 777X aircraft, either at the time of the 2014 siting determination or in respect of its future activities through 2040. Thus Boeing is not legally constrained by the measures at issue from adopting new processes or adapting existing processes in the future in respect of the 777X. The Panel notes in this regard the United States' argument that "ESSB 5952 does not require any production process in particular".⁶⁵⁸ The focus of the Panel's analysis, for the purpose of the current dispute, is not on the production processes for the 777X, in general or at any point in time,

⁶⁵² See paras. 7.266 and 7.268 above.

⁶⁵³ United States' response to Panel question No. 64, para. 57, fn 71.

⁶⁵⁴ "'Significant commercial airplane manufacturing program' means an airplane program in which the following products, including final assembly, will commence manufacture at a new or existing location within Washington state on or after the effective date of this section: (i) The new model, or any version or variant of an existing model, of a commercial airplane; and (ii) Fuselages and wings of a new model, or any version or variant of an existing model, of a commercial airplane." ESSB 5952 (Exhibit EU-3).

⁶⁵⁵ United States' response to Panel question No. 42, para. 102. Further, in the United States' view, the fact that "complete finished wings for some smaller commercial airplanes can be transported in a large transport airplane ... simply means that, for some airplanes, it is theoretically possible to fully assemble the wings in a location far from where any further assembly of the airplane will take place". United States' response to Panel question No. 64, para. 55. See also United States' second written submission, para. 60.

⁶⁵⁶ United States' response to Panel question No. 42, para. 102.

⁶⁵⁷ See United States' first written submission, paras. 25 and 130, and fn 45; opening statement at the first meeting of the Panel, para. 11; closing statement at the first meeting of the Panel, para. 6; response to Panel question Nos. 35 and 64, paras. 82, 52-54 and 56; Boeing expert statement (Exhibit USA-1) (BCI), para. 43.

⁶⁵⁸ United States' response to Panel question No. 64, para. 57.

but rather on whether the measures at issue, in their design, structure, and modalities of operation, would limit access to existing subsidies if imported goods were to be used in any such processes.

7.356. Sixth, the significant commercial airplane manufacturing programme announced by the manufacturer, which is the basis of the First Siting Provision, in fact entails the production by Boeing and in Washington State of wing structures that, for other aircraft models, had been previously produced outside of Washington State and in some cases imported from outside the United States.⁶⁵⁹ Notwithstanding the fact that "ESSB 5952 does not require any production process in particular"⁶⁶⁰, the fact remains that following the passage of ESSB 5952 the manufacturer made a final decision, for the 777X manufacturing programme, to produce domestically certain wing structures (i.e. "Section 12" wing structures⁶⁶¹) that the same manufacturer had previously imported for another commercial airplane manufacturing programme.⁶⁶²

7.357. Considering all these facts, in the light of the European Union's *de facto* contingency claim, the Panel notes first that the provision of subsidies exclusively to domestic producers, without more, is not in itself a breach of the obligations under the covered agreements. In the context of the GATT 1994, this principle is reflected in Article III:8(b) of the GATT 1994, which clarifies that the provision of subsidies exclusively to domestic producers is not in itself a breach of the national treatment obligation under that agreement. By contrast, subsidies of a particular character can be in breach of the SCM Agreement. The focus of the Panel's assessment is not whether the measures at issue have had an import substitution effect or a detrimental impact on imports, as this would require the Panel to trespass into an adverse effects analysis of the type that is not contemplated by Article 3.1. Rather, the precise question before the Panel is whether the subsidies at issue have been granted to domestic producers (i.e. Boeing) contingent, in fact, upon the use of domestic goods.

7.358. The specific nature and operating mechanism of the Second Siting Provision becomes relevant to this question. We recall, in particular, that the Second Siting Provision provides that the "siting" of "wing assembly" of the airplane model in question (the 777X) outside Washington State would result in the loss of the B&O aerospace tax rate for the manufacturing or sale of that airplane.⁶⁶³ It thus is clear that so long as this "siting" does not happen, the Second Siting Provision remains dormant, operating passively as a deterrent to safeguard the *status quo* (or at least particular aspects thereof) that satisfied the First Siting Provision. This particular passive, deterrent nature of the measure in turn raises the question as to what sorts of factual evidence could inform the analysis of whether ongoing access to the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under the 777X programme is contingent *de facto* on the use of domestic over imported 777X wings. In particular, at the time of the Panel's assessment of this claim, the Second Siting Provision has not been triggered, and therefore no evidence exists as to the actual operation (the triggering) of the Second Siting Provision.

7.359. The Panel thus is confronted by the counterfactual question of what would trigger the Second Siting Provision, that is, what action by Boeing would result in the Department of Revenue determining that 777X wing assembly "has been sited" outside Washington State. We note in this regard the argument of the European Union that if Boeing were to use even a single imported 777X wing, the Second Siting Provision would be triggered and Boeing would lose the B&O aerospace tax rate in respect of the 777X.⁶⁶⁴ The evidence cited by the European Union consists of

⁶⁵⁹ See, for example, Office of Washington Governor, "Legislature approves key elements of 777X incentive package", 10 November 2013 (Exhibit EU-59); Washington State House Finance Committee, Video, "Testimony of Governor Inslee before House Finance Committee", 7 November 2013 (Exhibit EU-110); Collective Bargaining Agreement between Boeing and the International Association of Machinists and Aerospace Workers, 2 November 2008, including Contract Extension and Modification Agreements, 7 December 2011 and 3 January 2014 (Exhibit USA-33), p. 190; Addendum No. 14 to the 1991 Boeing Everett Mitigation Decision Document SEPA #14-009, 27 March 2014 (Exhibit USA-34) (BCI).

⁶⁶⁰ United States' response to Panel question No. 64, para. 57.

⁶⁶¹ See paras. 7.259 and 7.266 above.

⁶⁶² See, for example, United States' first written submission, paras. 18, 24, 25, 28-29, and 31-32.

⁶⁶³ The Panel recalls that the expression "has been sited" (used in the Second Siting Provision in the passive tense) is related to a manufacturer locating a manufacturing programme in a particular place, which is consonant with the definition of "siting" in the First Siting Provision. See para. 7.304 above.

⁶⁶⁴ See European Union's opening statement at the first meeting of the Panel, paras. 5 and 48.

the word "any" in the Second Siting Provision, which it argues means that that provision would be triggered by the use of any quantity, no matter how small, of imported 777X wings.⁶⁶⁵ The United States for its part argued that the purpose of the Second Siting Provision is to prevent Boeing from relocating, or duplicating, 777X production outside Washington State.⁶⁶⁶

7.360. With regard to the question of what would trigger the Second Siting Provision, the Panel finds particularly relevant the discretion granted by ESSB 5952, and specifically by the Second Siting Provision, to the Department of Revenue to terminate the availability of the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under the 777X programme if it determines that Boeing has "sited" assembly of wings for that model outside of Washington State. In particular, the exercise of the Department of Revenue's discretion would be inconsistent with Article 3.1(b) of the SCM Agreement if, in practice, it resulted in the termination of the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under the 777X programme on the basis of a determination that Boeing, by virtue of using imported 777X wings, had "sited" 777X wing assembly outside Washington State.

7.361. To elucidate the issue of what would trigger the Second Siting Provision, and more specifically, whether a use by Boeing of imported 777X wings would do so, the Panel posed a series of questions to the United States in respect of certain counterfactual scenarios, other than the existing *status quo* that satisfied the First Siting Provision (and that thus by definition does not trigger the Second Siting Provision). That existing *status quo* is that Boeing will itself assemble the wings and fuselages, and conduct the final assembly of the 777X, in Washington State. The Panel questions specifically went to whether the Second Siting Provision would be triggered if:

- a. Boeing continued manufacturing, *inter alia*, wings itself in Washington State and in addition purchased wings (assuming *arguendo* that it were possible to do so) from another manufacturer in Washington State⁶⁶⁷;
- b. Boeing continued manufacturing, *inter alia*, wings itself in Washington State and also, (assuming *arguendo* that it were possible to do so), imported some wings from a different producer (i.e., other than Boeing itself).⁶⁶⁸

7.362. The essence of the Panel's questions thus was what would happen pursuant to the Second Siting Provision if Boeing in the future sourced some 777X wings from other entities, including foreign producers, rather than assembling all of them itself.⁶⁶⁹ The specific focus of these questions was the geographic location of other hypothetical suppliers. In response to the first question above, the United States indicated (assuming *arguendo* that it were possible for 777X wings to be completed and transported as separate articles), that the Department of Revenue likely would not determine that any wing assembly had been sited outside Washington State, and thus the Second Siting Provision would not be triggered.⁶⁷⁰ In response to the Panel's other question, however, the United States indicated that if completed wings were produced outside of the United States and then imported, the Department of Revenue likely would determine that some wing assembly had been sited outside Washington State, meaning that the Second Siting Provision would be triggered.⁶⁷¹

⁶⁶⁵ See European Union's response to Panel question No. 7, para. 12; comments on United States' response to Panel question No. 77, paras. 85-89.

⁶⁶⁶ See United States' response to Panel question Nos. 43 and 80, paras. 103 and 118-120.

⁶⁶⁷ See Panel question No. 40.

⁶⁶⁸ See Panel question No. 80.

⁶⁶⁹ The Panel recalls its assessment in the context of the European Union's *de jure* claim that, on its face, the Second Siting Provision did not condition the availability of the subsidy on use of domestic over imported goods. Based strictly on the terms of the Second Siting Provision, a possible reading of the conditionality set out therein would allow the manufacturer in question to continue to benefit from the subsidy if it used wings manufactured outside the state of Washington in the final assembly of the commercial airplanes in question in the state of Washington, so long as it maintained final and wing assembly previously sited in the state of Washington. See above, para. 7.311. As noted, in the context of its *de facto* analysis the Panel considers not only the text of the measure, but also additional factual evidence relevant to understanding the design, structure, and modalities of operation of the contingency in question.

⁶⁷⁰ See United States' response to Panel question No. 40, para. 97.

⁶⁷¹ See United States' response to Panel question No. 39, paras. 93-95; response to Panel question No. 80, paras. 118-120. See also United States' response to Panel question No. 7, paras. 15-16.

7.363. Thus, as explained in the United States' responses in this regard, if the manufacturer were to use wings produced outside of Washington State (including in particular wings imported from other countries) in the production of 777X aircraft⁶⁷², the Department of Revenue would likely consider this to mean that some wing assembly had been sited outside of Washington State and this would activate the Second Siting Provision.⁶⁷³ This would be the case even if the manufacturer imported some wings, while continuing to produce wings in Washington State, effectively duplicating wing manufacturing or assembly.⁶⁷⁴ In such cases, as indicated by the United States, the Department of Revenue would likely determine that at least some wing assembly had been sited outside of Washington, which would activate the Second Siting Provision. As a consequence, the use of imported wings would lead to the loss of the B&O aerospace tax rate. In contrast, if the manufacturer were to use wings made in Washington State by another producer, this would not activate the Second Siting Provision.⁶⁷⁵

7.364. The United States' responses clarify that the Second Siting Provision is not only aimed at ensuring that a manufacturer (namely Boeing) itself assemble the 777X wings or conduct the final assembly of the 777X. This is notwithstanding the United States' arguments that the measures at issue (to the extent they are subsidies) would be production subsidies (to Boeing), rather than subsidies contingent on the use of any particular goods, and that the First Siting Provision and the Second Siting Provision contemplated a single entity performing all of the operations referred to in those provisions. In particular, the United States' responses indicate that the Second Siting Provision would not be triggered simply by a decision by Boeing to source 777X wings from another entity rather than assembling them itself. Rather, in such a scenario, whether or not the Second Siting Provision would be triggered would be determined exclusively by where the wings in question were assembled. In particular, the *only* decision by Boeing to source wings which it would then "use" in producing the 777X that *would not* trigger the Second Siting Provision would be to source such wings within Washington State, which by definition would be domestic wings.

7.365. The Panel considers that these descriptions are significant in understanding the modalities of operation of the conditions of the Second Siting Provision, which as noted are subject to administrative discretion vested in the Department of Revenue. As explained by the United States, within the Washington State domestic legal system, courts would accord "substantial weight to the agency's interpretation of the governing statutes and legislative intent" and "substantial deference to agency views when it bases its determination on factual matters".⁶⁷⁶ The United States' clarifications as to how the Department of Revenue would likely exercise discretion shed light on the requirements imposed by the Second Siting Provision, which applies prospectively to the 777X manufacturing operations that are still being commenced and that may evolve over time. Under such circumstances, the likely actions of the relevant administrative agency in response to possible factual scenarios are indicative of whether, in practice, a subsidy would remain available so long as a manufacturer used domestic goods, while that same subsidy would be terminated if a manufacturer used those same goods from a foreign source.

7.366. In light of the foregoing, the Panel is not persuaded that the Second Siting Provision is only aimed at preventing Boeing from relocating the 777X entirely outside Washington State or from establishing a parallel 777X production program outside Washington State. The Second Siting Provision does not only concern the production of airplanes. It also concerns the "use" of certain goods, and specifically the origin of those goods that enter into the production process for the 777X as a condition for the continued availability of a subsidy. The Panel notes in particular the use of the word "or" in the Second Siting Provision. That is, that provision would be triggered if wing assembly "or" final assembly of the 777X were "sited" outside Washington State.⁶⁷⁷ The United States' responses as to how the Department of Revenue would likely exercise its discretion, in interpreting the Second Siting Provision, demonstrate that the expression "or" in that Provision

⁶⁷² Assuming *arguendo* that the manufacturer could use wings or fuselages manufactured separately.

⁶⁷³ See United States' response to Panel question Nos. 39 and 80, paras. 93-95 and 118-120. See also United States' response to Panel question No. 7, paras. 15-16.

⁶⁷⁴ See United States' response to Panel question No. 80, paras. 118-120. See also United States' response to Panel question No. 42, para. 103; European Union's comments on United States' response to Panel question No. 80, para. 91.

⁶⁷⁵ See United States' response to Panel question No. 40, para. 97.

⁶⁷⁶ See Washington Court of Appeals, *Nationscapital Mortgage Corporation et al. v. Department of Financial Institutions*, June 2006 (Exhibit USA-84); United States' response to Panel question No. 79, para. 117, fn 146.

⁶⁷⁷ See para. 7.304 above.

contemplates, and seeks to prevent *inter alia*, any wings (of the airplane model that satisfied the First Siting Provision) from being produced as separate products outside Washington State (including overseas), that would then be shipped to Washington State for incorporation in the final assembly process. Statements made by the Governor of Washington about the goal of keeping 777X wing production in Washington, seen in the light of the United States' responses, are consistent with this conclusion and are considered by the Panel to be relevant evidence in this *de facto* analysis.⁶⁷⁸

7.367. The loss of the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under the 777X programme if Boeing used 777X wings produced outside of Washington State, even if it maintained production of such wings in Washington State, makes the B&O aerospace tax rate for that programme contingent upon the use of wings made in Washington State. This is confirmed by the 777X programme retaining access to the B&O aerospace tax rate if Boeing used 777X wings made in Washington State by another producer. Accordingly, pursuant to ESSB 5952, and as a result of the Second Siting Provision, the B&O aerospace tax rate subsidy for the manufacturing or sale of commercial airplanes under the 777X programme is contingent *de facto* not only on the production of that aircraft and its wings in Washington State, but additionally on not using 777X wings other than those made in Washington State. Since wings made in Washington State are domestic goods and any imported wings would by definition be made outside of Washington State, it follows that the Second Siting Provision makes the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under the 777X programme contingent upon the use of domestic wings over imported wings.

7.368. Lastly, and for completeness, the Panel returns to the contention by the United States that wings are not used in the production of the 777X, in the sense that separate, identifiable and complete "wings" never come into existence in the production process of the 777X. In this regard we observe that Article 3.1(b) does not require the identification of a specific good in order that it can be applied to a particular situation. In the case before us, it is the output or outputs of a wing assembly process that the evidence establishes must not be sourced by Boeing from overseas, because of the implications of doing so. Regardless of precisely what these outputs are, and regardless of the reference to "wing" and to "wing assembly" in the siting provisions, there can be no doubt that goods, which together make up a wing to the factual satisfaction of the Department of Revenue, cannot be sourced by Boeing from outside the state of Washington without the consequence of activating the Second Siting Provision. The Panel's references to wings should be understood in this context.

7.369. For the reasons explained above, the Panel concludes that the siting provisions in ESSB 5952, and in particular the prospective modalities of operation of the Department of Revenue's discretion under the Second Siting Provision, make the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under the 777X programme *de facto* contingent upon the use of domestic over imported goods within the meaning of Article 3.1(b) of the SCM Agreement.

8 CONCLUSIONS AND RECOMMENDATION

8.1 Conclusions

8.1. In light of the findings in the foregoing sections of the Report, and with respect to the aerospace tax measures at issue, as amended and extended through Washington State's Engrossed Substitute Senate Bill (ESSB 5952), the Panel concludes that:

⁶⁷⁸ Upon the passage of ESSB 5952, the Washington State Governor issued a press release indicating that ESSB 5952 "includes strong contingency language to ensure that all of the 777X assembly and wing assembly remains in Washington. Specifically, the bill includes a provision that says the company will lose its preferential B&O tax rate for the 777X if any of that work is moved out of state." Office of Washington Governor, "Legislature approves key elements of 777X incentive package", 10 November 2013 (Exhibit EU-59). The Governor additionally provided testimony to the Washington State legislature prior to the passage of ESSB 5952 regarding House Bill 2089, a companion bill to a previous version of ESSB 5952, which had similar siting provisions referring to wing assembly and final assembly (in addition to "wing fabrication", which does not appear in ESSB 5952). In that testimony, the Governor expresses the aim of maintaining employment in the aerospace industry by retaining production of the 777X carbon fibre wing in Washington State. See Washington State House Finance Committee, Video, "Testimony of Governor Inslee before House Finance Committee", 7 November 2013 (Exhibit EU-110).

- a. Each of the seven aerospace tax measures at issue in the present case constitutes a subsidy within the meaning of Article 1 of the SCM Agreement;
- b. Regarding the European Union's claim that the aerospace tax measures at issue are subsidies *de jure* contingent upon the use of domestic over imported goods within the meaning of Article 3.1(b) of the SCM Agreement:
 - i. The European Union has not demonstrated that the aerospace tax measures are *de jure* contingent upon the use of domestic over imported goods with respect to the First Siting Provision in ESSB 5952 considered separately;
 - ii. The European Union has not demonstrated that the reduced business and occupation (B&O) tax rate for the manufacture and sale of commercial airplanes (B&O aerospace tax rate) is *de jure* contingent upon the use of domestic over imported goods with respect to the Second Siting Provision in ESSB 5952 considered separately;
 - iii. The European Union has not demonstrated that the aerospace tax measures are *de jure* contingent upon the use of domestic over imported goods with respect to the First Siting Provision and the Second Siting Provision considered jointly;
- c. With respect to the First Siting Provision and the Second Siting Provision in ESSB 5952, considered jointly, the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under the 777X programme is a subsidy *de facto* contingent upon the use of domestic over imported goods within the meaning of Article 3.1(b) of the SCM Agreement.

8.2. Having found that the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under the 777X programme is inconsistent with Article 3.1(b) of the SCM Agreement, the Panel also finds that the United States has acted inconsistently with Article 3.2 of the SCM Agreement.

8.3. Under Article 3.8 of the DSU, in cases where there is an infringement of the obligations assumed under a covered agreement, the action is considered *prima facie* to constitute a case of nullification or impairment. We conclude that, to the extent that the United States has acted inconsistently with the SCM Agreement, it has nullified or impaired benefits accruing to the European Union under that Agreement.

8.2 Recommendation

8.4. Article 4.7 of the SCM Agreement provides that, having found a measure in dispute to be a prohibited subsidy:

[T]he panel shall recommend that the subsidizing Member withdraw the subsidy without delay. In this regard, the panel shall specify in its recommendation the time period within which the measure must be withdrawn.

8.5. The Panel has found that the European Union has demonstrated that the B&O aerospace tax rate for the manufacturing or sale of commercial airplanes under the 777X programme, pursuant to ESSB 5952, is a subsidy contingent upon the use of domestic over imported goods, prohibited under Articles 3.1(b) and 3.2 of the SCM Agreement.

8.6. Accordingly, taking into account the nature of the prohibited subsidy found in this dispute, the Panel recommends that the United States withdraw it without delay and within 90 days.

8.7. Finally, the Panel notes that the rules contained in Part II of the SCM Agreement do not require a panel to specify how the implementation of recommendations under Article 4.7 should be effected by the subsidizing Member. In this context, the second sentence of Article 19.1 of the DSU provides that a panel *may* suggest ways in which a recommendation could be implemented. Assuming that this provision also applies to recommendations under Article 4.7 of the SCM Agreement, the Panel notes that, pursuant to Article 21.3 of the DSU, the means of

implementation is in the first instance for the Member concerned.⁶⁷⁹ Further, the Appellate Body has made clear that the second sentence of Article 19.1 "does not oblige panels to make ... a suggestion".⁶⁸⁰ In this case, in the absence of any request from the parties, the Panel refrains from making any suggestions concerning steps that might be taken to implement its recommendation.

⁶⁷⁹ Panel Report, *US – Hot-Rolled Steel*, para. 8.11.

⁶⁸⁰ Appellate Body Report, *US – Anti-Dumping Measures on Oil Country Tubular Goods*, para. 189.