

## 2. Brief Overview of WTO Rules affecting Taxation

The relation between international trade law and taxation has traditionally focused on internal tax obstacles to trade in goods and trade-distorting subsidies, but with the new rules on services, there are now three main clusters of WTO provisions that are relevant in the tax area. First, and probably best known, is the non-discrimination principle laid down in Articles I and III GATT which prohibits Members to impose higher internal taxes or more burdensome regulation on products imported from one Member than on similar imports from other Members (most-favoured-nation obligation) or on similar domestic products (national treatment obligation). These Articles mainly relate to indirect taxes but may also have relevance for income tax measures as will be further explored in part II of this General Report.

Second, the very wide definition of prohibited or actionable subsidies, under Article XVI GATT and the Agreement on subsidies and countervailing duties (SCM), covers any financial contribution by a government which confers a benefit, including tax incentives, by means of which the government foregoes revenue that it would otherwise have collected. No surprise, therefore, that the SCM Agreement, in its illustrative list of prohibited export subsidies, refers explicitly to both direct and indirect tax incentives. The possible impact of WTO subsidy rules in the income tax area will be further discussed in part III of this General Report.

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<sup>2</sup> Footnote 58 of the SCM Agreement defines direct taxes as taxes on wages, profits, interests, rents, royalties, and all other forms of income, and taxes on the ownership of real property. Indirect taxes are defined as sales, excise, turnover, value added, franchise, stamp, transfer, inventory and equipment taxes, border taxes and all taxes other than direct taxes and import charges.



Third, the General Agreement on Trade in Services (GATS) applies to all measures that may affect services or service suppliers and may therefore also apply to income taxes, in particular where services are supplied by means of cross border establishment in the form of a branch or a subsidiary (mode 3), or by means of the cross border movement of economically active professionals (mode 4). In fact there are explicit references to income tax measures in the GATS, which, however, essentially seek to carve out tax treaties from the most-favoured-nation obligation and income taxes from the national treatment obligation. The possible impact in the income tax area of the GATS non-discrimination principle will be further explored in part IV of this General Report.

In addition to these three main clusters there are some further WTO provisions that may have an impact on taxes. Well known are the interpretative notes to articles III GATT and Article XVI GATT which clarify that non-excessive border tax adjustments within a destination type tax are not GATT incompatible.<sup>3</sup> Moreover, the commitments under the Agreement on Agriculture (AA) to reduce domestic support cover monetary transfers to the beneficiaries as well as revenue foregone by the Member concerned. Furthermore, it is possible to interpret the TRIPS provisions as prohibiting discriminatory taxation of intellectual property (see *Yariv Brauner* in this volume). Finally, there are many transparency obligations scattered throughout the WTO Agreements, some of which may oblige WTO Members to notify income tax legislation to the WTO.

## II. International Trade in Goods, the GATT and Income Taxes

### 1. Summary of WTO Rules on Trade in Goods

International trade in goods is covered by a large number of WTO Agreements which all seek to gradually eliminate barriers to cross border trade. Though there is no general definition of goods or products, a fairly precise idea exists on what supplies are covered by the rules on trade in goods (as opposed to trade in services) because WTO Members agreed on a harmonised system of customs classification in which all goods are listed under a large number of harmonised tariff headings.<sup>4</sup>

GATT makes a broad distinction between trade barriers of a quantitative nature, which it essentially prohibits or seeks to phase out, and measures of a

<sup>3</sup> "Border tax adjustments", Report of the Working Party adopted on 2 December 1970, L/3464, BISD 18 S at 97 to 109. A consolidated document on existing practices of tax adjustments was drawn up by the Secretariat, L/3389.

<sup>4</sup> The distinction between goods and services was also touched on by the Appellate Body in its Report on *Canada – periodicals* (AB Report, *Canada – certain measures concerning periodicals*, WT/DS31/AB/R of 30 June 1997, part IV).