Tax Protectionism and Tax Discrimination: Relevance of Multilateral and Bilateral Trade and Investment Agreements

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Abstract

This paper addresses three questions. First, what is a trade agreement in the contemporary world? Second, should trade agreements affect tax law, particularly direct tax law? Third, how do trade and investment agreements affect tax law? In answering the first question attention is paid to multilateral agreements, such as GATT 94 and GATS, bilateral trade and investment agreements, such as the proposed agreement between the EU and Singapore, and agreements which contain provisions affecting trade but which seek to create high levels of economic, social and political integration between the parties whether in Europe, Africa or elsewhere. In answering the second question it is suggested that care should be taken to ensure that tax law does not undermine the aims of these treaties. Protectionism and discrimination are not justified because tax law is used as the means of achieving them. In addressing the third question, examples are given of how trade agreements have affected tax law. It is suggested that the experience of the EU demonstrates that although the impact of trade agreements may at first appear disruptive to tax systems, in the longer term it may provide significant benefits.

Introduction

Tax law, particularly direct tax law on which this paper focuses, is not infrequently thought of as operating in a world of its own. It is drafted using specialised concepts which in some important respects poorly reflect commercial reality.[2] It is administered using specialist officials. Often, it is disputed in front of

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[2] See for a discussion of this: *Ectopia, tax Law and international taxation* [1997] BTR 383, J. Prebble. He says: '"Ectopia' is used here as a label for a characteristic of income tax law that distinguishes it from most other forms of law. This characteristic is that income tax law is, in a fundamental sense, dislocated from the facts to

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specialist judges, at least until it reaches the higher appellate courts. Internationally, it is governed to a great extent by its own system of bilateral treaties. These, in turn, are frequently negotiated by reference to specialist model tax treaties including, of course, the OECD Model. All this may suggest that tax law in all its forms is law for specialists. No doubt specialists are essential. Yet, increasingly, tax law and administration are being placed in a much broader commercial context and it is not uncommon to find detailed references to them in trade and investment agreements.

The need to place tax law in a broader context is acknowledged by the title of this session and, in particular, by the use of the terms protectionism and discrimination. These are concepts which are by no means confined to the world of taxation.[3] When used in relation to companies and business activity they are inextricably associated with matters of trade, commercial freedom and globalisation. In the context of trade, tax law is merely one of many tools which may be used to achieve discrimination or protectionism and so reduce the benefits of international trade. The OECD's Commentary on the OECD Model Treaty recognises in its first paragraph that trade is a proper context in which to consider tax. Referring to double taxation it says:

> "Its harmful effects on the exchange of goods and services and movements of capital, technology, and persons are so well known that it is scarcely necessary to stress the importance of removing the obstacles that double taxation presents to the development of economic relations between countries."

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which it relates." (p383). Later, he comments: "...ectopia has special and marked effects on tax law as it applies to international trade and investment." (p397).

[3] Some caution is needed in relation to the use of trade terms in the field of tax law. The most favoured nation ("MFN") principle, for example, is sometimes used in relation to intra-EU or intra-OECD affairs. In the EU context Case C-376/03 *D* [2005] ECR I-5821 generated discussion about an EU MFN principle (see "Critical notes on the European Court of Justice's *D* Case decision on most-favoured-nation treatment under tax treaties" EC Tax Review [2006] 6, J Schuch.). An OECD MFN principle is sometimes associated with provisions in double tax treaties giving all OECD members the benefit obtained by one (see, e.g., (6) of the Protocol of 3rd January 1996 to the UK/Argentina treaty). The trade law concept of MFN, however, spreads benefits among the global trading community of 159 WTO members. It does not merely extend benefits to a relatively small group of states with similar interests such as in the EU or the OECD.

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In this session I explore some elements of the relationship between tax law and trade law by asking three questions. First of all, what is a trade agreement in the contemporary world? Second, should trade agreements affect tax law? Third, how do trade and investment agreements affect tax law?

Part One : What is a trade agreement?

It is impossible to isolate trading activity from other elements of national and international activity. A trade agreement is not now and never was an agreement solely about the commercial activities of trading entities and states. Today trade between states has implications for a wide variety of issues affecting the activities of the state. Employment law and worker's rights, health and safety regulation, product regulation, environmental protection, social, commercial and economic policy generally including, of course, taxation are all affected. Even in the nineteenth century bilateral trading agreements between many countries commenced with an express acknowledgement of the broader context essential to their existence. They were treaties of friendship or amity, commerce and navigation. It is not possible here to review their history. That has been done elsewhere. As one of very many examples, however, one may take the treaty between the USA and Argentina of 1853. Its foundation is an expression of "perpetual amity" in article I. That political relationship was the foundation of everything that followed including an article containing the most-favoured nation principle and provisions limiting duties on import, export and tonnage .[4] The state's willingness to place a limit on sources of revenue, especially at a time when income tax was not levied, is noteworthy.

In the contemporary world, in which the taxation of incomes of individuals and corporations is commonplace, it is no surprise to see that free trade agreements may contain complex provisions affecting income taxation. The new draft agreement between the EU and Singapore, released on 20th September 2013, is a good example

[4] See http://avalon.law.yale.edu/subject_menus/19th.asp

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of how extensive a modern bilateral free trade agreement may be. It has chapters on services, establishment and electronic commerce, intellectual property, and competition and subsidies as well as goods and customs duties. It also deals specifically with the relationship between tax law and trade law in Article 17, specifying that: "This Agreement shall only apply to taxation measures insofar as such application is necessary to give effect to the provisions of this Agreement."[5] That, of course, means that the trade agreement does apply to taxation and is intended to do so although subject to significant qualifications.[6] In particular, Article 17 protects tax systems by, amongst other things, preserving tax agreements and their primacy and permitting tax measures differentiating between taxpayers on the basis of rational criteria such as the place of residence or the location in which capital is invested. [7]

Tax may also be affected by the provisions of the North American Free Trade Area Agreement although, again, the extent to which it may be affected is limited. The approach of the agreement is somewhat different to that taken in the EU/Singapore agreement. It provides, somewhat less expansively, that: "Except as set out in this Article, nothing in this Agreement shall apply to taxation measures." [8] There then follow a number of provisions protecting tax systems and double tax agreements. The article on national treatment in the Agreement is said to apply to taxation to the same extent as article III of GATT[9]. The Agreement's provisions on export taxes are also said to apply to taxation. In addition, the purchase or consumption of services may be affected by provisions on income tax, and certain other direct taxes.[10]

[5] See article 17.6.1. The draft is available at http://trade.ec.europa.eu/doclib/press/index.cfm?id=961. See to similar effect the concluded treaty between the EU and Korea at article 15.7 [2011] OJ L 127/33, 14.5.2011.
[6] See also Understanding 1 in relation to Article 17.6 (taxation).
[7] See Articles 17.6.2 and 17.6.3
[8] Article 2013(1) https://www.nafta-sec-alena.org/Default.aspx?tabid=97&language=en-US.
[9] See Article 2103(3)
[10] See Article 2103(4) which contains other provisions on tax in relation to services and certain exceptions for taxation.

If bilateral trading agreements may affect taxation in certain respects it is no surprise that so too do multilateral trading agreements. As is well known, the WTO, now with 159 members, was established pursuant to the Marrakesh Agreement and Ministers affirmed that its establishment:

> "ushers in a new era of global economic cooperation, reflecting the widespread desire to operate in a fairer and more open multilateral trading system for the benefit and welfare of their peoples. Ministers express their determination to resist protectionist pressures of all kinds."[11]

There seems to be no reason to think that the reference to "all kinds" of protectionist pressures excludes those deriving from taxation. GATT 94 contains, of course, a number of provisions concerned with duties, charges and taxation. Article I setting out the MFN principle makes frequent reference to duties and charges. The other fundamental pillar of the global trading order, the principle of national treatment, is dealt with in Article III headed: *National Treatment on Internal Taxation and Regulation*. Other articles of GATT 94, such as Article XVI.4 prohibiting export subsidies, also encompass direct taxation as we shall see.

Among the other agreements of the Marrakesh Round which may have an impact on taxation one may refer to the Agriculture Agreement, the Agreement on Trade Related Investment Measures, the Agreement on Subsidies and Countervailing Measures and the General Agreement on Trade in Services. This last agreement provides that measures inconsistent with the national treatment principle are permitted where they are aimed at ensuring the equitable or effective imposition or collection of direct taxes in respect of services or service suppliers.[12] Measures inconsistent with the MFN principle are permitted provided that the difference in treatment is the result of a double tax treaty or provisions on the avoidance on double taxation in other agreements, or arrangements, binding a Member. It

[11] See point 2 of the Marrakesh Declaration of 15th April 1994: *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts* WTO (1995).
[12] GATS Article XIV (d).

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follows, of course, that direct tax measures which are not covered by these derogations are not permitted and that direct tax may be affected by the provisions of the Agreement.

The broadness of the scope of bilateral and multilateral trading agreements and their ability to affect taxation are easily surpassed by many other agreements which contain provisions on trade but which have altogether more ambitious aims. These are the agreements which aim to achieve extensive economic integration between member states and in some cases social and political integration as well. Perhaps the best known of these is the agreement establishing the European Union.

In some of the discussion on the interaction of trade and taxation, the requirements of the EU internal market and its commercial policy are sometimes treated as matters of trade law.[13] That is understandable. The internal market, with its customs union and common commercial policy, now including foreign direct investment,[14] all under the exclusive competence of the EU, undoubtedly affects trade. But it does so much more than that. The relevant legal provisions, including those concerning trade, do not simply describe the parameters of new trading relationships. They constitute some of the fundamental elements of a new legal, economic, social and political order which also contains, for example, an area of freedom, security and justice and confers EU citizenship on individuals.

Undeniably, in addition to the provisions on the taxation of products,[15] turnover taxes and excise duties,[16] it is the fundamental freedoms of the internal market that have proved highly significant for lawyers dealing with tax and duties, as is noted

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[13] See e.g.: *Impact of Trade Agreements on Tax Systems* (2002) 30 Intertax 166, P. R. McDaniel.
[14] See Treaty on the Functioning of the EU ("TFEU") articles 30 and 207.1 and 4 and Regulation (EU) No 1219/2012 of the European parliament and of the Council of 12th December 2012 establishing transitional arrangements for bilateral investment agreements between Member States and third countries. OJ L 351/40, 20.12.2012.
[15] TFEU, article 110.
[16] TFEU, article 113.

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briefly in Part Three below. Within the internal market the fundamental freedoms of movement of goods, persons, services and capital[17] are to operate without discrimination on grounds of nationality: a concept largely understood as ensuring the absence of impediments to free movement. The freedoms are not, however, even where they affect tax, interpreted as part of trade law, but as much broader general concepts. This was made abundantly clear when an Advocate General of the Court of Justice of the EU ("CJEU") relied on cases involving systems of financing health care in proposing a solution to a case on the availability of cross-border tax losses.[18] The broad nature of the internal market is also expressly recognised in the provisions of the TFEU governing state aid which expressly refers to broader economic, social and cultural considerations.[19]

Staying within Europe but moving outside the EU, the fundamental freedoms operate also in relation to the European Economic Area which covers the EU, Iceland, Liechtenstein and Norway. The EEA Agreement seeks "to promote a continuous and balanced strengthening of trade and economic relations between the Contracting Parties with equal conditions of competition, and the respect of the same rules, with a view to creating a homogenous European Economic Area…".[20] It too has had an impact on taxation[21] although it has not, apparently, been as extensively relied on by taxpayers as the TFEU.

There is, of course, nothing exclusively European about the aim of a common market, or some form of economic union or integration. What follows is not intended to be comprehensive. It is, nevertheless, worth noting that in Latin America, the Treaty of Asunción creating MERCOSUR states, in Article 1, that the common market

[17] The treaty is available at http://eur-lex.europa.eu/en/index.htm.
[18] See the Opinion of Poiares Maduro in Case C-446/03 *Marks & Spencer Ltd* [2005] ECR I-10837 at 10862, paragraph 77, where the Advocate General relies on Case C-56/01 *Inizan* [2003] ECR I-12403 and Case C-157/99 Smits *and Peerbooms* [2001] ECR I-5473.
[19] TFEU, article 107.3.
[20] Article 1 of the European Economic Area treaty [1994] OJ L1/3; 3.1.1994.
[21] A case dealing with the taxation of dividends and the fundamental freedoms in the EEA is E-1/04 *Fokus Bank ASA* 23.11.2004. The EEA treaty is available at http://www.efta.int/legal-texts/eea.
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at which it aims shall involve “the free movement of goods, services and factors of production between countries”.[22] A common external tariff is required, along with the elimination of non-tariff restrictions and equivalent measures. There is a specific article concerned with taxes which requires products originating in one state to be treated in the other states as domestic products.[23] Staying in America, the Organisation of Central American States[24] seeks to establish an economic and political community while elsewhere in the continent the Andean Community pursues its goals.[25]

In the Caribbean the revised treaty of Chaguaramas, establishes the Caribbean Community, including the CARICOM single market and economy. It prohibits discrimination on grounds of nationality, provides for the operation of the most favoured nation principle,[26] a Community trade policy,[27] an external tariff,[28] prohibits state assistance for the export of goods[29] and, among other things, requires the harmonisation of national laws on dumping, subsidies and countervailing measures.[30]

Africa has a number of supra-national organisations aiming at some form of integration or a common market. There is the West African Economic and Monetary Union of eight states.[31] The Revised Treaty of the Economic Community of West African States seeks “the removal between Member States, of obstacles to the free movement of persons, goods, services and capital, and to the right of residence and

[22]Available at http://www.sice.oas.org. Mercosur consists of Argentina, Brasil, Paraguay, Uruguay and Venezuela, with Bolivia in the process of joining.
[23] Articles 1 and 7.
[24] Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua and Panama: http://www.sice.oas.org
[25] Bolivia, Colombia, Ecuador, Peru, and Venezuela were parties to the Cartagena Agreement of 2003 which describes itself as a “subregional integration agreement”, and is available at http://www.sice.oas.org.
[26] Articles 7 and 8: http://www.caricom.org. CARICOM has 15 Caribbean Members, including the Bahamas, Jamaica and Trinidad and Tobago.
[27] Article 78.
[28] Article 82.
[29] Article 93.
[30] Article 74.2.
[31] Consisting of Bénin, Burkina Faso, Côte d’Ivoire, Guinée-Bissau, Mali, Niger, Sénégal and Togo.

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establishment;".[32] Then there is the East African Community which aims at a customs union, a common market, a monetary union and a political federation.[33] Two of the states involved, Kenya and Uganda, are members of the larger Common Market for Eastern and Southern Africa. This aims to create a common market in which its aims and objectives shall be to "remove obstacles to the free movement of persons, labour and services, right of establishment for investors and right of residence within the Common Market;".[34] Both the treaty establishing the East African Community and the treaty establishing the COMESA provide that the law of the organisation shall take precedence over national law.[35]

Elsewhere in the world, the Eurasian Economic Community has as its purpose to promote effectively the process of formation of the Customs Union and the Single Economic Space.[36] There is the Gulf Cooperation Council to be taken into account as well.[37] Finally it should be noted that the ASEAN states aim to achieve economic integration by 2020 in an ASEAN Economic Community.[38]

It is impossible for the purposes of this paper to analyse the different impact of each of these treaties in the field of taxation. That must be left for another day. It is clear, however, that the trade provisions in treaties which seek fundamental

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[32] Article 3.2.d).iii). The treaty is available at: http://www.refworld.org. The Community has 15 members including Nigeria and Ghana.
[33] Article 5.2 of the Treaty for the Establishment of the East African Community, available at http://www.eac.int/
[34] Article 4.6(e) of the COMESA Treaty. There are 19 member states of COMESA including Egypt, Kenya, Libya, Swaziland, Uganda and Zambia.
[35] Article 8.4 of the Treaty for the Establishment of the East African Community available at http://www.eac.int/, establishes that community law takes precedence over national law. The provisions of the COMESA Treaty (http://www.comesa.int) are similar in certain respects but do not contain the same statement as to precedence: see Article 5.
[36] Article 2. The treaty is available at http://www.wipo.int/wipolex/en. The Eurasian Economic Community, was created between The Republic of Belarus, the Republic of Kazakhstan, the Kyrgyz Republic, the Russian Federation, and the Republics of Tajikistan and Uzbekistan. It is to be distinguished from the customs union, and the proposed Eurasian Economic Union, between the Russian Federation, the Republic of Belarus and the Republic of Kazakhstan.
[37] Article 3, which goes on to state "especially the following...1 Movement and residence... 5. Engagement in all economic, investment and service activities... 7. Capital movement 8. Tax treatment..." The treaty is available at http://sites.gcc-sg.org. The GCC consists of Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, the UAE.
[38] See Roadmap for an ASEAN Community 2009-2015 available at http://www.aseansec.org/overview/.

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change in the nature of the economic, social and political situation of the contracting states are very likely to affect tax law. Increasingly, a trade agreement is not just about trade.

Part Two

Should trade law affect tax law?

There is no doubt that trade law, particularly trade law which is found in treaties aiming at high levels of economic, social and political integration, can be disruptive to established tax systems. Some have questioned whether trade law should affect tax law and, if it does, under what conditions. In a thoughtful article by J Slemrod and R S Avi-Yonah the authors have suggested that trade agreements should accept bilateral tax agreements designed to generate and allocate a single layer of taxation between the taxing jurisdictions, accept statutorily uniform source-based factor taxes even if a higher burden is imposed on import intensive sectors and accept anti-evasion provisions dealing with predatory tax protectionism, even if they violate non-discrimination, as long as they do not effectively levy more than a single layer of taxation. On the other hand, the authors recommend that a trade agreement should not accept situations in which the direct tax system is merely a vehicle for otherwise proscribed actions.[39]

Some elements of this approach, at least, are adopted in some of the agreements establishing free trade areas referred to in Part One. The EU/Singapore draft agreement states, for example, that it shall not prevent the adoption or maintenance of any measure aimed at preventing the avoidance or evasion of taxes pursuant to double tax agreements or other tax arrangements or domestic fiscal legislation.[40] Article 17.6.1 also states, as was noted above, that the agreement only applies to taxation so far as it is necessary to give effect to its provisions. The broader the aims of an agreement, however, the less appropriate it is for tax law to be given

[39] *(How) Should Trade Agreements deal with Income Tax Issues* (2001-2002) 55 Tax Law Review 533, J Slemrod and R.S. Avi-Yonah, at pp353-4.
[40] Article 17.6.4.

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special treatment and protected from the impact of the provisions in question. Agreements aiming to facilitate economic integration involve a substantial realignment in the affairs of the contracting parties concerned. Taxation will be as much a part of that realignment as anything else. As Willem Molle has pointed out, economic integration is about much more than pure trade regulation. In his words:

> Internally, the abolishing of many non-tariff barriers ... implies the harmonisation of many regulations in such widely divergent fields as taxation and safety. For the internal market to function properly, measures are also needed to prevent competition distortion. Hence the need for a common competition policy...[41] (emphasis added)

In the context of state aid law, which is so important for the internal market, it has been said that:

> "…failure to place special tax provisions under the state aid structure would create an enormous loophole in the state aid regime."[42]

It is not just in relation to the state aid regime that one wants to avoid the creation of loopholes. They have to be avoided in all the areas which the treaties aim to cover.

It is, of course, true that tax law uses many concepts to tax individuals and businesses which are very different from those which trade law uses to regulate trade. Law governing international trading relationships does not necessarily demand that those concepts be changed. It does demand, though, that the use to which those tax concepts are put is controlled. Tax law is not the master of international trade and investment, particularly in the context of regional economic integration. It is to some extent its servant.[43]

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[41] *The Economics of European Integration: Theory, Practice, Policy* Willem Molle, 5th ed, p23 (Ashgate Publishing Ltd, Aldershot, 2006).
[42] *Impact of Trade Agreements on Tax Systems* (2002) 30 Intertax 166, P. R. McDaniel at p170.
[43] On the relationship between tax and trade law see further, for example, *Panel IV: The Pursuit of National Tax Policies in a Globalized Environment, Principal Papers, Trade and Taxation* (2000-2001) 26 Brooklyn Journal of International Law 1621, P.R.McDaniel; *Treating Tax Issues through Trade Regimes* (2000-2001) 26 Brooklyn Journal of International Law 1683, R. S. Avi-Yonah; *(How) Should Trade Agreements deal with Income Tax Issues* (2001-2002) 55 Tax Law Review 533, J Slemrod and R.S. Avi-Yonah; *Impact of Trade Agreements on Tax*

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Treaties which seek economic integration and the treaties established in the Uruguay round, for example, focus on the economic effects of action by contracting states. Tax protectionism and tax discrimination are phrases which combine means, *i.e.* tax, and ends, *i.e.* protectionism and discrimination. Contracting states determined to abolish the latter will be forced to consider the former.

The experience of the EU following the *Avoir Fiscal* case,[44] when fundamental freedoms were first applied to direct taxation by the CJEU, suggests that some level of disturbance results from the application to tax of treaties aiming at economic integration. Nevertheless, predictions that EU tax systems, or EU states' involvement in the international tax system, would be badly damaged if the logic of some early decisions were followed have been shown to be unfounded, not least by the *D* Case referred to above. Pure logic in EU law has been tempered by an awareness of political reality and mandatory requirements in the public interest. The result of what has happened is that member states now take account of the EU internal market in formulating their tax laws, for example the availability of tax reliefs, to a much greater extent than once they did, but that they have retained more control over their tax systems than has sometimes been anticipated. In this respect, the truth of the famous observations of Oliver Wendell Holmes, Jr., has been demonstrated. He said:

> "It is something to show that the consistency of a system requires a particular result, but it is not all. The life of the law has not been logic: it has been experience. The felt necessities of the time, the prevalent moral and political theories, intuitions of public policy, avowed or unconscious, even the prejudices which judges share with their fellow-men, have had a good deal more to do than the syllogism in determining the rules by which men should be governed." [45]

Systems (2002) 30 Intertax 166, P. R. McDaniel; *Trade Agreements and Income Taxation, Interactions Conflicts and Resolutions* 57 Tax Law Review 275, P R McDaniel.

[44] Case 270/83 *Commission v France* [1986] ECR 273.

[45] Oliver Wendell Holmes Jr. in *The Common Law* p1, available as a Project Gutenberg Ebook at http://www.gutenberg.org, produced by Stuart E. Thiel and David Widger.

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The quotation above is also highly relevant when considering contentions as to the impact of WTO law on taxation. It may be contended, for example, that as a matter of logic the prohibition of export subsidies in GATT 94 would lead to the prohibition of the exemption method of avoiding double taxation under double tax treaties. That is not the same as saying that a WTO panel would, inevitably, come to that decision in any given case. Systems of law which are governed by the decisions of judges or adjudicators must proceed one case at a time and rely on those judges and adjudicators to exercise more than logic in deciding them.

Part Three

How do trade and investment agreements affect tax law?

In this section I propose, very briefly, to highlight some examples of the various ways in which tax has been affected by trade law and to make one or two general comments on the relationship between bilateral trade and investment treaties on the one hand and taxation on the other.

Effects of trade law on taxation: GATT/WTO[46]

The law of the WTO is dealt with in this session by Professor Luiz Olavo Baptista whose great experience in this field is well-known. It is, however, worth noting briefly some relevant cases. In 1981, the tax regimes of the USA,[47] France,[48] Belgium[49] and the Netherlands[50] were held to infringe the provisions on export subsidies in GATT Article XVI.4.[51] The USA law concerned Domestic International Sales Corporations. The legislation cannot be reviewed here, but it may be noted that

[46] For a fuller consideration of direct tax and the WTO agreements see e.g.: *WTO Report*, IFA Cahiers de droit fiscal international, 2008, Vol. 93a. p73, Daly.
[47] Panel Report, *Tax Legislation - United States Tax Legislation (DISC),* L/4422*,* adopted 7-8 December 1981, BISD 23S/98.
[48] Panel Report, *Tax Legislation - Income Tax Practices Maintained By France,* L/4423, adopted 7-8 December 1981, BISD 23S/114
[49] Panel Report, *Tax Legislation - Income Tax Practices Maintained By Belgium,* L/4424, adopted 7-8 December 1981, BISD 23S/127.
[50] Panel Report, *Tax Legislation - Income Tax Practices Maintained By The Netherlands, L/4425,* adopted 7-8 December 1981, BISD 23S/137.
[51] The cases are considered in *G.A.T.T. and Company Taxation* [1977] BTR 201, A.R. Prest.

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affected companies were not subject to federal income tax on current or retained export earnings. One half of the earnings was taxable as a deemed distribution to shareholders. Tax was paid on the happening of certain events. The Panel considered that the legislation gave rise to an export subsidy contrary to Article XVI.4 of GATT.

More recently, the USA law on foreign sales corporations which concerned export-related foreign source income was held, amongst other things, to infringe the Agreement on Subsidies and Countervailing Measures as a prohibited export subsidy, and the Agreement on Agriculture.[52] The USA reacted to the decision by passing the FSC Repeal and Extraterritorial Income Exclusion Act of 2000. This in turn was held to provide subsidies. [53] The USA then passed the American Jobs Creation Act 2004 which still did not provide full compliance.[54] Finally, a mutually acceptable solution was notified on 17th May 2006.

At the present time there is a further dispute before the WTO concerning taxation. Panama alleges that certain provisions of Argentine tax law[55] are inconsistent with GATT 94 and GATS. So far as GATT 94 is concerned it is alleged there are infringements of the most favoured nation rule (article I), the article on national treatment on internal taxation and regulation (article III) and the general elimination of quantitative restrictions (article XI). So far as GATS is concerned, it is alleged that there are infringements of the most favoured nation obligation (article II), the provisions on payments and transfers (article XI) and the provisions on market access (article XVI) and national treatment (article XVII). The case appears, therefore, to be likely to be much more wide-ranging than the case concerning foreign sales corporations in the USA and the other cases in the 1980's involving taxation. On 25th

[52] *US Tax Treatment for "Foreign Sales Corporation"* DS108/AB/R, FSC, 24.2.2000.
[53] See DS108/AB/RW *"Tax Treatment for "Foreign Sales Corporations"* - Recourse to Article 21.5 of the DSU by the European Communities, 14.1.2002.
[54] See DS108/AB/RW *"Tax Treatment for "Foreign Sales Corporations"* – Second Recourse to Article 21.5 of the DSU by the European Communities, 13.2.2006.
[55] See DS 453 in which complaint is made about the Argentine Decree 1344/987 as amended by Decree 1037/00.

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June 2013 a panel was established and several countries, including China, Brazil, the EU, the USA and Singapore, have reserved their third party rights.

Bilateral trade and investment treaties, e.g., Switzerland/EEC Agreement 1972

In Europe, the agreement of 1972 on trade matters between Switzerland and the EEC, as it then was, had a profound impact on the Swiss taxation of companies about 35 years later. Article 23.1(ii) of the agreement of 1972 prohibits "any public aid which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods".[56] The EU authorities, somewhat to the surprise of some in Switzerland, subsequently held that the taxation of management, mixed and holding companies infringed this article.[57] Perhaps this was not what a free trade agreement was thought to cover, at least by the Swiss. The case on the EEC law of state aid which is frequently said to show that state aid encompasses fiscal aid is *Commission v Italy* in 1973.[58] The decision was not, however, entirely unexpected, at least within the EU. By the time of the decision of the European Commission in 2007, however, the position was beyond doubt.

Doubt, however, cannot so easily be dispelled in relation to other bilateral trade treaties in relation to which, as we have seen, the articles limiting the application of the treaties to tax will clearly be of great importance. The same will be true of the articles limiting the application of bilateral investment treaties to tax. The UK model bilateral investment treaty contains an article declaring that, in relation to the application of the most favoured nation principle and the national treatment rule, the treaty is not to be construed so as to oblige one contracting party to extend to the other contracting party the benefits of a customs union or

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[56] OJ L300/189, 31.12.1972.

[57] See Commission Decision of 13 February 2007 on the incompatibility of certain Swiss company tax regimes with the Agreement between the EEC and the Swiss Confederation of 22nd July 1972, C(2007) 411 final.

[58] Case 173/73 *Commission v Italy* [1974] ECR 709 para.13, where the Court noted that EEC law did not distinguished between State measures by reference to their effects not their causes or aims. "Consequently, the alleged fiscal nature or social aim of the measure in issue cannot suffice to shield it..."

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> "any international agreement or arrangement relating wholly or mainly to taxation or any domestic legislation relating wholly or mainly to taxation."[59]

An example of a treaty which contains such a provision is the UK/India treaty (1994).[60] Some treaties though, such as the UK/Indonesia treaty (1976),[61] do not have such a provision. In relation to such treaties, the issue arises as to whether and in what circumstances tax may be affected by their provisions. That in turn involves the proper approach to the construction of, for example, most favoured nation clauses in bilateral investment treaties generally and justifications for limitations to them on public policy or other grounds. The matter is open to dispute and is beyond the scope of this paper. It is clear, though, that such provisions will be construed on a case by case basis and in the light of a number of arbitration decisions. [62]

TFEU

So far, the agreements we have looked at have not aimed at establishing an economic or socio-economic community. Clearly, one example of a treaty which does that is the TFEU. Plainly state aid law affects tax as we have already noted. Particularly since the *Avoir Fiscal* decision in 1986[63], the provisions on the free movement of goods, persons, services and capital have also had a profound impact on direct taxation of both individuals and businesses.

It is now very well-established, in a formula frequently repeated by the CJEU, that tax is subject to the constraints of EU law:

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[59] See Article 7 of the UK's model bilateral investment treaty, available in *Principles of International Investment Law* R. Dolzer and C. Schreuer, 2nd ed, OUP (2012) at p370.

[60] TS No 27 (1995), article 4(3). Cm 2797.

[61] TS No. 62 (1977). Cmnd. 6858.

[62] Two of these may be *National Grid v Argentina* Decision on Jurisdiction, 20th June 2006, para. 82 (UNCITRAL rules: decision available at http://italaw.com) and *Plama Consortium Ltd v Bulgaria* ICSID Case No. ARB/03/24, available on the web-site of the International Centre for Settlement of Investment Disputes: https://icsid.worldbank.org/ICSID/Index.jsp.

[63] C-270/83 *Commission v France* ECR [1986] 273.

"...it must be borne in mind that, according to settled case-law, although direct taxation falls within their competence, Member States must none the less exercise that competence consistently with Community law..."[64]

It could not be otherwise without the supremacy of EU law being compromised. Indeed the position is now so well established that the formula has not always been repeated in recent cases concerned with direct taxation.[65]

This is not the place to review the extensive case-law of the CJEU relating to the tax regimes of Member States. The web-site of TAXUD (European Commission) contains some useful materials for those who wish to do that.[66] Suffice it to say that there are cases dealing with income tax, corporation tax, capital gains tax, and inheritance tax, as well as other taxes. The availability of tax reliefs and deductions under domestic tax law, the treatment of inbound and outbound dividends, the imposition of tax on foreign controlled companies, thin capitalisation rules, the availability of benefits under double tax agreements and the scope of anti-avoidance provisions are all matters which have needed amendment in the light of EU law. Of course, in addition to the impact of the fundamental freedoms, there are many other developments affecting taxation within the EU. These do not derive from trade law elements of the EU although they may have a profound impact, for example, on the terms of double tax treaties.[67]

[64] Case C-446/03 *Marks & Spencer plc* [2005] ECR I-10837, para. 29.
[65] See, for example, Case C-350/11 *Argenta Spaarbank NV*, 4th July 2013, in which the freedom of establishment was applied to corporation tax in the context of double tax treaties and Case C- 380/11 *DI. VI. Finanziaria di Diego della Valle & C. SapA*, 6.9.2012, in which the freedom of establishment was applied to capital tax on corporations without the use of the formula quoted above.
[66] See, e.g., "CJEU cases in the area of, or of particular interest for, direct taxation": http://ec.europa.eu/taxation_customs/resources/documents/common/infringements/case_law/court_cases_direct_taxation_en.pdf and *Direct Taxation in the Case-Law of the European Court of Justice* 1st ed Malherbe, Malherbe, Michelle, Traversa (Larcier) 2008.
[67] See the Commission Recommendation on aggressive tax planning of 6.12.2012 C(2012) 8806 final, para.3.2 and the Commission Recommendation on tax havens of 6.12.2012 C(2012) 8805 final, para. 4.3 and 5.3.

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Conclusion

Clearly, there are a wide variety of international agreements governing trade and investment. Some are concerned exclusively with trade or investment. Many place trade and investment in the context of an economic or socio-economic community. To the extent that the contracting parties do not expressly exclude taxation from their remit there is no reason in principle why tax law should not be affected by their terms. Indeed, if the agreements are to have their proper effect there is every reason why tax should fall within the scope of their application. The first paragraph of the OECD's Commentary on the OECD Model Treaty, referred to in the introduction of this paper, in focusing on the removal of obstacles to the development of economic relations between countries, puts tax law at the service of trade. That is how it should be. The example of the EU demonstrates that, when taxation is governed by the requirements of law relating to trade, what may at first appear disruptive can, in the longer term, prove beneficial.

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