

GENERAL AGREEMENT ON  
TARIFFS AND TRADE

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UNITED STATES TAX LEGISLATION (DISC)

Attached is the full transcript of the European Communities representative's statement before the GATT Council regarding the DISC legislation.

1. The United States stated at the Council meeting of 7 May that it believed that the DISC is in conformity with its GATT obligations. But it also recognised that the DISC could be "appropriately challenged" in GATT.

The Community fully intends to make this challenge. In the first place, the Panel report at paragraph 74 found quite plainly "that the DISC legislation in some cases had effects which were not in accordance with ... Article XVI:4".

This Panel finding has not, in our view, been altered in any respect by the Council decision of last December. The Council Chairman noted then that the decision did not modify existing GATT rules in Article XVI:4 as they relate to the taxation of exported goods: consequently, the Panel finding must still be valid. The United States in December made a unilateral declaration on their interpretation of these GATT rules, which was contested by my delegation and by Canada. I will revert to this point: but clearly it does not affect the validity of the Panel finding.

Mr. Chairman, the United States view has not always been that the DISC is consistent with GATT. Let me cite to the Council a few examples:

- (i) in six meetings of the Council in late 1976 and in 1977 the United States delegation did not on any single occasion contest the Panel findings on DISC;
- (ii) in MTN negotiations on the Subsidy Countervailing Measure Code in 1978/79, the United States accepted a change in item (d) of the 1960 Illustrative List which had the effect of specifically prohibiting tax deferral systems such as DISC. Furthermore a footnote to the new List was included specifically to cover the United States situation on DISC and to permit their signature of the code: this footnote envisaged a special procedure for the elimination of "measures incompatible" with this new text;
- (iii) in mid-1979 a bilateral agreement between the EEC and the United States explicitly recognized that "DISC, as presently conceived in the statute, was not consistent with the provisions of item (e) of the Illustrative List" annexed to the MTN Code;

Mr. Chairman, my delegation is prepared to make this text available to other delegations who wish to see it.

Prior to the adoption of the Council decision last December informal discussions had taken place with the United States in the second half of 1980 and throughout 1981. At no time in that period had the United States argued that the DISC was consistent with GATT, indeed in mid-1981 they had been willing to envisage a scenario under which the matter would have been referred to the SCM Committee which would then confirm that DISC was incompatible with the Code and would invite the United States to modify their legislation as necessary.

The final arrangement, adopted last December was on somewhat different lines; but it was clear that nothing in the bilateral or multilateral discussions preceding that meeting justify the claim that DISC is now to be considered as in conformity with the GATT obligations of the United States.

My delegation has examined the record of the 8 December 1981 meeting with some care. At no time did the United States delegation state that DISC was in conformity with the GATT; nor did it contest declarations by other delegations that it was a prohibited export subsidy, that the Council decision did not modify in substance the Panel report on DISC, and that the United States was expected to take the necessary action to meet its GATT obligations.

2. The United States also stated on 7 May that it cannot be claimed "that only one of the tax practices is guilty or that the December decision applies to all but one of the Panel reports".

In support of this they have argued that "the economic approach on which the Panel based its conclusions" has now been altered by the legal interpretation in the Council decision of last December; and that "the Panel reports, because they analyzed the (DISC and other tax practices) on an incorrect juridical basis, came to flawed conclusions under GATT".

We have examined these contentions. In our view the United States continues to argue as if the DISC system was no different in form from the other practices examined by the panel. In fact they are substantially different; and the impact of the December decision will vary, depending on the relevance of its content to the different practices concerned. One important difference is that the Panel report on DISC does not mention the taxation of "export activities" outside the United States whereas this is crucial in the other cases examined.

The Community submits that the essential qualification adopted by the Council last December - relating to export activities outside the territory of the exporting country - has no significance when applied to the DISC case. Its clear intent was to establish that the activities of foreign located branches or subsidiaries or other foreign located establishments in

connection with the export of goods were not within the terms of Article XVI:4.

The DISC system does not, according to our information, apply to export activities outside the territory of the United State. Unless the United States contests this, it is clear that the effect of the December decisions is to remove the basis upon which certain European tax practices were found by the panels to be, in some cases, not in accordance with Article XVI:4 - and it was for this reason that the EEC and member States had proposed the formula; it does not in any way modify the essential basis for the Panel's finding in relation to the DISC.

To conclude on this point: the Panel report on DISC is not based on an incorrect juridical basis. It is based on the provisions of Article XVI:4 - which we are all agreed have not been modified. The legal interpretation of last December has not vitiated the Panel's approach, since it applies to a situation which does not occur in the DISC case. Consequently it is our view that DISC is the only practice which remains inconsistent with GATT.

3. Mr. Chairman, let me remind the Council of another essential point. The DISC was introduced specifically to give United States exporters a tax advantage: in the minds of its authors, to offset a handicap they faced because the United States does not have a territorial tax system.

Its purpose was clear, and it was clearly designed to test Article XVI of GATT. Whatever the indirect effects of European tax systems, it is clear that they were not designed nor introduced for this purpose.

The DISC can no longer be maintained, in violation of the GATT, simply because the United States does not like the tax systems of European countries. The Panel made a finding on this point, and I quote from paragraph 79 of the report:

"The Panel did not accept that one distortion could be justified by the existence of another one; if the United States considered other CPs were violating the GATT, it could have had recourse to the remedies offered by GATT."

This is still true today. If the United States wishes to attack the practices of others, it is free to do so through GATT procedures. It is not free to continue to maintain a system which has been found to be contrary to Article XVI.

- Last December the Council decided that economic processes located outside the territory of the exporting country need not be subject to taxation by that country.

- This does not say: a country that nevertheless imposes taxes on such activities is free to do so regardless of GATT provisions.
- Nor does it say: where a country decides to tax such activities, it may do so provided the level of taxation on exported products is at least equal to the level that would apply if it had chosen a territorial tax system.
- On the contrary Article XVI:4 applies; and requires a comparison between taxation on exported products and on domestically sold products. By this test the DISC is clearly illegal. The Council should endorse this view, today, and in the strongest possible terms.