international taxation

Customs & Trade

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The International Trading System: Fundamental Principles

This monthly column is an ongoing journey into customs and trade laws at the domestic level in the United States, with some occasional discussions of the domestic law in other jurisdictions, as well as at the international level as embodied by the World Trade Organization (WTO) in Geneva and the World Customs Organization (WCO) in Brussels.

No matter what the topic in international trade laws, or administration of those laws, some fundamental principles are consistent guides. But for an international trade transaction that is beyond the familiar reach of those trade law principles, there may be an unreconciled conflict between those principles and principles that derive their force from disciplines outside the trade laws. Two examples of unresolved conflict are the open questions around the trade laws and international worker rights, and between the trade laws and environmental and wildlife protections. For all of the praise heaped on the WTO system as a comprehensive corpus of normative rules governing international trade in goods, this is a significant failing.[1] If that is not the case, and a given transaction is subject to the international trade laws, a WTO member government must ensure that its laws and their administrative actions comport with those principles.

For all trading nations that have signed on to the General Agreement on Tariffs and Trade (GATT), beginning with its inception in 1948 and later in its renewed format in 1994, these guiding principles serve as the benchmarks whereby adherence to the international community of trading nations is gauged. The GATT 1994 principles are discussed below.

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MFN

The first obligation that GATT 1994 imposes (Article I.1) is to provide most favored nation (MFN) treatment. Members are to treat all other members equally without playing favorites among imported articles in respect of any advantage, favor, privilege, or immunity granted to "like products." This is to prevent a member from discriminating against other international traders, or at least against other GATT members. For example, if the United States were to levy a duty of 10% against all imports of widgets but exceptionally levy a 15% duty against widgets from France, France would have the right to challenge the United States measure in the WTO's dispute settlement system.

An actual example is the case that Argentina recently brought to the WTO against alleged U.S. restrictions on the importation of fresh lemons from the Northwest region of Argentina.[2] One of the crucial issues turns on whether the French widgets—or Argentine lemons—are "like" the widgets or lemons from other countries. If not, or if there is some justification for discriminatory treatment against those specific imports, such as legitimate health or safety issues, there is no GATT violation. The deviation from this universal principle that is characterized by the proliferation of free trade agreements (FTAs), with benefits extended reciprocally by trading partners on a selective basis, is one of the primary objections raised against FTAs by free trade *philosophes*.

National Treatment

The proscription against discrimination among imported

goods would be a hollow remedy without a parallel prohibition against discrimination in favor of locally produced goods viz. imported goods regarding the imposition of domestic taxes and other regulations. GATT Article III.4 provides this standard, whereby imported goods are accorded the same treatment as "like product" goods of national origin. A prior column discussed this restriction in connection with the WTO case against the Thailand government's discriminatory treatment accorded to Philippine cigarettes.[3] Article III contains other anti-discriminatory provisions, especially regarding imposition of internal taxes.

Quantitative Restrictions

One of the other principal goals of GATT was to outlaw the use of quantitative restrictions (quotas). Instead of the distortions caused by quota regimes, GATT (Article XI) posits that countries should rely exclusively on the use of duties, taxes, and other charges. There are exceptions to this general prohibition, e.g., allowing for temporary quotas in response to food shortages.

A good example of this replacement of quotas with customs duties, "tariffication," is the current embodiment in the Harmonized Tariff Schedule of the United States of the tariff treatment of agricultural products. Another recent example is the replacement in 2005 of the use of quotas for regulating the import volumes of textiles and apparel products. This substitution had been agreed as part of GATT and the general move to eliminate quotas.[4]

Customs Formalities

Perhaps the most direct (or at least most common) application of the laws for trade in goods is the customs clearance process and the assessment of customs duties. The tariff classification of imported goods is accomplished through application of the Harmonized Tariff System.[5]

GATT Article VII establishes the basic premise that there should be agreed rules for the customs valuation of imported goods. The actual formal name for what is commonly termed the Valuation Agreement, which provides these formal rules, is the Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994. This agreement, and especially its focus on related-party pricing, is of primary importance for international tax specialists.

One of the primary advantages for private-sector trading is the degree of transparency in the trade law system in the United States. Most of the information that the trading community may need in dealing with the U.S. agencies is readily available online, including matters as diverse as the complete Focused Assessment audit program to be applied by Customs and Border Protection, or the regulations on the Iran sanctions administered by the Office of Foreign Assets Control.

It may be possible to overstate the value of the transparency of an already very complicated system. From experience, this degree of transparency in the U.S. system is very much an exception. The private sector looking for information on the laws and administration of imports in other jurisdiction will generally be frustrated. This issue can be viewed against the GATT Article X requirement for GATT members to publish their body of laws, regulations, judicial decisions, and administrative rulings.

Special Regimes

There are also separate agreements under which GATT members have committed to follow specific rules for the imposition of trade remedies for unfair competition, dumping, and unfair subsidies,[6] as well as for the use of safeguard relief from disruptions caused by increased import volumes (GATT Article XIX). Traders can take some comfort in that any GATT member's attempt to apply trade remedies must follow the strictures of these agreements and that such trade remedy laws and their administration are subject to challenge at the WTO. Thus, the review is not only of the substance of the laws but also their administration, so that the discriminatory administration of a facially neutral statute is actionable.

Conclusion

The international trading system is founded on a solid principle of nondiscrimination, as manifested in the twin bases mandating MFN treatment and national treatment. The use of quotas has been singled out as particularly distorting. Other guiding principles ensure a degree of predictability and procedural fairness and transparency.

Exporters of products to other GATT members should be mindful of the protections that they receive as a result of the commitments that those members make to the United States and its fellow participants. It is also important that importers into the United States and others understand that the United States has made parallel commitments, and that a failure to honor those commitments (as when the United States chooses to apply certain antidumping law methodologies developed by the Department of Commerce) may lead to WTO challenges against the United States. ●

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1 The opportunity to reconcile these issues that was lost with the ill-advised demise almost 65 years ago of the Havana Charter of the International Trade Organization is an enduring failure of tragic proportions. See the discussion on trade and social policy in Neville, *International Trade Laws of the United States: Statutes and Strategies* (Thomson Reuters/WG&L, 2012), ch. 3.

2 United States—Measures Affecting the Importation of Fresh Lemons, DS 448, request for consultations (September 3, 2012).

3 See Neville, "The Next Frontier: Border Taxes in Emerging Markets," 22 JOIT 17 (September 2011).

4 Textiles and apparel had been the subject of a network of bilateral agreements that imposed quantitative restraints on imports into developed textile-consuming countries, including the United States and the EU, from textile-producing developing countries dating to the 1960s. The bilateral agreements were negotiated within the context of three multilateral agreements. The last such agreement was the Agreement on Textiles and Clothing (ATC) (1995-2005), which replaced the Multi-Fiber Arrangement (1974-1995). Under the ATC, quotas were to be gradually eliminated. The last remaining quotas dropped off at the end of 2005, replaced by a tariff-based system. It was the end of the quota system that resulted in significant shifts in textile and apparel production and trade.

5 For more on tariff classification, see Neville, *supra* note 1, ch. 4.

6 Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994; Agreement on Subsidies and Countervailing Measures.