ANNEX E

Oral Statements of the Third Parties

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ANNEX E-1

ORAL STATEMENT BY CANADA

(14 March 2001)

Mr. Chairman, Members of the Panel.

Thank you for the opportunity to provide Canada's views in this proceeding. We would take this opportunity to highlight briefly some of the key points made in our written submission.

As we stated in our submission, we agree with the EC that the *FSC Repeal and Extraterritorial Income Exclusion Act of 2000* does not bring the United States into compliance with the DSB recommendations and rulings in this dispute.

In support of this position, we would advance two principal arguments.

First, in our view, the FSC replacement scheme provides a "subsidy" to US-based enterprises within the meaning of Article 1.1 of the SCM Agreement.

Second, the subsidy provided under the FSC replacement scheme to US-based enterprises is contingent upon export performance, in violation of SCM Article 3.1(a).

Turning briefly to the first argument:

In our view, there is a "financial contribution" to US-based enterprises within the meaning of Article 1.1(a)(ii) of the SCM Agreement. The FSC replacement scheme continues to provide a financial contribution to US-based enterprises by excluding from taxation domestic income that they earn from export transactions.

as noted in our submission, since income earned from export transactions cannot by definition face double taxation, the exclusion from taxation provided for this income under the FSC replacement scheme can only reduce US tax otherwise payable.

In addition, the financial contribution clearly confers a “benefit” to US-based enterprises earning domestic income from export transactions.

ANNEX E-2

THIRD PARTY STATEMENT BY INDIA

(14 March 2001)

India is appreciative of this opportunity to present its views on this dispute.

The issue before this Panel is whether the FSC Repeal and Extraterritorial Exclusion Act of 2000 (hereinafter "FSC Replacement Act") is consistent with the recommendations and rulings of the DSB to withdraw the FSC measure found to be a prohibited export subsidy and thus inconsistent with

Body agreed that the FSC measure represented a "subsidy" within the meaning of Article 1.1 of the SCM Agreement. Finally, the Appellate Body upheld the Panel's finding that the "subsidy" was

that these words are sufficient to make the subsidy de jure export contingent. As stated by the Appellate Body in Canada – Certain Measures Affecting the Automotive Industry (DS139-142):

> "a subsidy is … properly held to be de jure export contingent where the condition to export is clearly, though implicitly, in the instrument comprising the measure. Thus, for a subsidy to be de jure export contingent, the underlying legal instrument does not always have to provide *expressis verbis* that the subsidy is available only upon fulfilment of the condition of export performance. Such conditionality can also be derived by necessary implication from the words actually used in the measure." (para 100 of the AB Report)

ANNEX E-3

ORAL STATEMENT BY JAPAN

(14 March 2001)

I. INTRODUCTION

1.

income from taxation, but only a part, then it is within the category of foreign trade income to which the "otherwise due" criteria must be applied. Therefore, the question is whether tax is "otherwise due" in connection with foreign trade income under the US system.

6. Under the FSC Replacement Scheme, within the category of foreign trade income, the majority of foreign trade income is taxable. Thus, the taxation of most foreign trade income establishes that, from a normative standpoint, income tax on foreign trade income is "otherwise due" under the US tax system. It is only by virtue of the FSC Replacement Scheme that a small portion of that income (i.e., "qualifying foreign trade income") is excluded.

7. In this regard, Japan would like to draw the Panel's attention to the submission of Canada. As Canada correctly points out in footnote 19 of Canada's submission, "the foreign tax credit provisions of the US Internal Revenue Code have not been repealed by the FSC Replacement Act and still provide the basic approach used by the United States to relieve double taxation with respect to income subject to tax in other countries."[2]

8. Being a third party, Japan has not received a copy of rebuttal submission of the United States. So Japan has not learned of the US rebuttal on this point. But based on the materials and argument disclosed to Japan so far, the United States is yet to establish that the Act provides a new benchmark for the taxation of foreign income in the United States in place of the old one. Unless proven otherwise by the United States, Japan believes that the Act still confers a subsidy within the meaning of SCM Agreement Article 1.1(a)(1)(ii), and the "exclusion" from the Gross Income provided under the Act does not create a new benchmark as the United States alleges, but instead closely emulate the tax exemption that was available to FSCs under the previous scheme.

B. THE US DEFENCE BASED ON FOOTNOTE 59 LEAVES MANY ELEMENTS OF THE REPLACEMENT SCHEME UNACCOUNTED FOR

9. Now I would like to address the argument of the United States based on Footnote 59. As I mentioned at the outset of this statement, Japan fully respects the sovereign authority of Members to administer their respective system of taxation. In the following, I would therefore only like to point

absence of clear linkage between its claim under Footnote 59 and what it claims in its own submission.

12. Finally, while Footnote 59 does sanction "measures to avoid the double taxation," this Footnote does not confer upon Members *carte blanche* to introduce any measure under the name of "a measure to avoid double taxation" As is the case with any exception permitted under the WTO Agreement, exceptions are permitted only to the extent necessary so as not to deviate from the generally binding principles applicable to all Members, which in this case includes, prohibition of export subsidies.

13. If the United States is to invoke Footnote 59 in justifying the Act as a measure to avoid double taxation, it must be demonstrated that the measures introduced under the Act contain clear linkage, both in letter and substance, to what is necessary for avoiding the double taxation. Thus the scrutiny for the invocation of exceptions must be conducted not only for the titles or categories of income used in the law in question, but also for the substance of those elements and the law – which is in this case a number of conditions attached to so-called "Extraterritorial Income" including the conditions attached to Qualifying Fo19.1(ei3(itt2.3(Fon Tradd t)7.5l9tt2.3(F(e)t)7.5l2wl2.9(Tw4 T4(so41ls)15l9tt2)

produced goods. That the benefit is also available to the foreign-produced goods category does not in any way make the subsidy, as it is available to exporters, consistent with the SCM Agreement.

18.

IV. THE FSC REPLACEMENT SCHEME'S 50 PER CENT RULE IS INCONSISTENT WITH ARTICLE III OF GATT 1994

25. The United States argues the FSC Replacement Scheme does not require the use of domestic product, and therefore must be consistent with Article III of GATT 1994. This argument, however, misses the essential point of Article III. A measure violates Article III whenever an imported product is accorded less favourable treatment than the domestic product. A measure can accord "less favourable" treatment whether or not there is a specific legal requirement to use domestic goods. Article III prohibits government measures that create legal incentives that disrupt the "effective equality of opportunities between imported products and domestic products.[6]

26. The scope of the FSC Replacement Scheme is wider than just domestic products, but the measure nevertheless covers domestic products. As long as such disparity in treatment between imported products and domestic products exists, the violation of Article III occurs. The FSC Replacement Scheme creates such a disparity. Under this tax programme, an eligible corporation may increase its use of domestic product to any level without affecting whether the income can be deemed "qualifying foreign income," and thus may generate tax benefits. In sharp contrast, an eligible corporation does not have such flexibility with regard to foreign content. Once the foreign content exceeds 50 per cent of the fair market value of the income, the income can no longer be deemed "qualifying foreign income," and the tax benefit is lost. This differential treatment, which skews the incentive to use domestic products over foreign products, violates the "effective equality of competitive opportunities" guaranteed by Article III.

27.