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Institute of International Economic Law
Georgetown Law
600 New Jersey Avenue, NW
Washington, DC 20001

lawiiel@georgetown.edu; http://iielaw.org/

WHY THE RYAN-BRADY TAX PROPOSAL WILL BE FOUND TO BE INCONSISTENT WITH WTO LAW

*Jennifer Hillman**

The tax-reform plan released by Speaker of the House Paul Ryan and House Ways and Means Committee Chairman Kevin Brady is intended to improve our corporate tax system by, among other things, taxing companies based on where they sell their goods, not where the business is located or where the goods are made.[1] To do so, the ambitious reforms would set up a system in which corporations pay taxes on their

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* Jennifer Hillman is a visiting professor of law at Georgetown Law. She is a former Chairman of the Appellate Body of the World Trade Organization (WTO) and a former general counsel at the Office of the United States Trade Representative. The author wishes to thank Christopher Brummer, Itai Grinberg, Gary Hufbauer and Chad Bown for their comments, but all errors or omissions are her own.

[1] The tax plan is laid out in "*A Better Way: Our Vision for a Confident America*," June 24, 2016, often referred to as "The Blueprint for America," https://abetterway.speaker.gov/_assets/pdf/ABetterWay-Tax-PolicyPaper.pdf. Because the details of exactly how the Ryan-Brady cash-flow tax would work in practice have not been made available, it is impossible to know for certain exactly how the new tax system would work. The analysis in this article is based on the description of the plan contained in the Blueprint and statements and responses to questions by Ways and Means Committee Chairman Kevin Brady.

U.S. sales revenues, with deductions permitted for the cost of input materials and labor, along with exclusions for the value of export sales.

Although policymakers rarely need to take the World Trade Organization (WTO) or its rules into account when devising tax policy, the proposal outlined in the Republican Blueprint for a cash flow tax does have significant WTO implications. While many proponents have said that plan is fully consistent with our WTO obligations, or at least that the WTO-consistency of the plan is "ambiguous," that contention rests on a blurring of the distinction between taxes imposed on *imports* with rebates or exclusions for *exports*, combining the two under the overall notion of "border adjusted taxes" or BTAs.[2] As this *Issue Brief* explains, as currently described, the Ryan-Brady taxes on imports are a clear violation of WTO rules while the rebates or exclusion from taxes for exports presents a murkier picture.

The speed with which WTO disciplines can be imposed also vary between imports and exports. Claims that the cash-flow tax's application to *imports* violates the WTO would follow the traditional WTO dispute settlement rules, potentially taking two or more years for a decision on whether a violation has occurred, with significant additional time added on for compliance and possible further litigation over whether any changes the US might make in response to an adverse ruling bring about actual compliance.[3] Disputes claiming that the exemption for *exports* from the sales revenue base violates the WTO rules on subsidies would, on the other hand, potentially be subject to the WTO's expedited dispute process for claims involving prohibited export subsidies or relatively fast action by our trading partners to impose countervailing duties on US exports that cause injury to their domestic producers. As a result, any U.S. violations would likely generate several opportunities for relatively expeditious reprisals by other WTO member states.

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[2] Ways and Means Committee Chairman Brady, for example, said in a statement ""We are now in the process of designing all aspects of our 'Built for Growth' tax plan to withstand any WTO challenge. We're confident we can win any case." The Blueprint itself states (at 28): "With this Blueprint's move toward a consumption-based tax approach, in the form of a cash-flow focused approach for taxing business income, the United States now has the opportunity to incorporate border adjustments in the new tax system consistent with the WTO rules regarding indirect taxes."

[3] While the suggested time frames in the WTO's Dispute Settlement Understanding (DSU) call for disputes with appeals to be resolved in 15 months' time, for a maximum of 15 months as a reasonable period of time by which the US would need to have changed its tax system to comply with any adverse ruling and for a quick resolution of any follow-on disputes over whether compliance has in fact been achieved (Article 21.5 proceedings), the reality is that most cases are being extended beyond the deadlines set forth in the DSU. A more likely scenario with respect to imports is two plus years for the litigation, 15 months as a reasonable period of time for compliance, and another eight or ten months for Article 21.5 proceedings, such that retaliation against the US for its tax on imports would not likely be authorized by the WTO for closer to five years from the date of enactment of the cash-flow tax.

A (Brief) Overview of the Ryan-Brady Plan

While the details of the Ryan-Brady Plan have not yet been released, the basic contours of the proposal are spelled out in the Blueprint and include changes to individual income tax rates, the abolishment of both the Alternative Minimum Tax (AMT) and estate taxes, along with changes to corporate taxes that are the subject of this *Issue Brief*. On the corporate side, the Blueprint calls for the reduction in the corporate tax rate from 35% to 20% and the conversion from a corporate tax system that taxes US corporations on their worldwide earnings to a destination-based consumption system that taxes revenues based on where goods or services are consumed. The 20% tax would be imposed on the revenue generated by the sale of goods or services in the US, with immediate write-offs for new investments and deductions for US inputs and labor costs. Deductions would not be permitted for imported inputs. As such, the 20% corporate tax will be fully imposed on imports because they are sold or consumed in the US but not imposed on exports because they are consumed outside the US.[4]

The Blueprint notes that it is designed to eliminate "the existing self-imposed export penalty and import subsidy by moving to a destination-basis tax system" It does this through the use of border adjustments exempting exports and taxing imports. Border adjustments "mean that it does not matter where a company is incorporated; sales to U.S. customers are taxed and sales to foreign customers are exempt, regardless of whether the taxpayer is foreign or domestic."[5]

As an example, if a US clothing manufacturer makes and sells one dress in the United States for $100, a tax base of $100 results. If the manufacturer used domestic fabric that cost $40 in the dress, $10 worth of domestic thread, trim and buttons and $20 in labor, the manufacturer would deduct from the $100 base the cost of all the inputs ($100 – 40 – 10 – 20 = $30) and would owe a tax of $6 ($30 x.20) based on the new 20% corporate rate. If that same manufacturer made a second dress that also sold for $100 using $40 of imported fabric rather than domestic fabric, with the same $10 in domestic thread, trim and buttons and $20 in labor, the manufacturer would not be able to deduct the cost of the imported fabric. The 20% tax would thus be applied to the $100 base minus only the domestic inputs ($100 – 10-20 = $70) for a tax amount of $14 ($70 x .20). As such, on the total tax base of $200 for two dresses, the manufacturer

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[4] The Blueprint (at 27) notes "Under a destination-based approach, tax jurisdiction follows the location of consumption rather than the location of production. This Blueprint achieves this by providing for border adjustments exempting exports and taxing imports . . . The Blueprint also ends the uncompetitive worldwide tax approach of the United States, replacing it with a territorial tax system that is consistent with the approach used by our major trading partners."

[5] Blueprint at 27.

would owe $20 ($6+$14) in taxes.   If, however, the manufacturer sold one of the two dresses overseas for $100, that $100 export sale would not be included in the tax base, so the manufacturer would deduct all of the domestic inputs ($100-40-10-20-10-20 = $0) for both dresses from the $100 base and would owe no tax.

Why the Plan's Treatment of Imports Run Afoul of the WTO

At the core of the WTO rules is the concept of national treatment—which means that no country can treat its domestic production more favorably than it treats foreign imports.[6]   The Congress is free to impose any tax it likes on domestic goods or services, but if it seeks to apply that same tax to imports, the amount of the tax on imports cannot exceed the amount of the tax on US goods or services.[7]

So the question of the WTO-consistency of the Ryan-Brady plan's application to imports rests on the question of whether the plan results in a tax on imports at all and if so, whether the amount of the tax paid on imports is more than the tax paid on comparable domestic products.[8]   It appears from the current design of the plan that the answer to those questions is yes.[9]

The Ryan-Brady approach to corporate taxes begins with the imposition of a 20% tax on the sales revenue from all products or services consumed in the United States. From that base of sales revenues, the plan, at least as it is usually described in public discourse, permits a deduction for the value of input materials and labor used to produce the good or service.   However, the plan as described would not permit a deduction for the cost of imported input materials or services.   Therefore, US companies will be paying 20% in taxes on the revenue from the sales of any goods or

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[6] Article III.2 of the GATT/WTO provides "The products of [any WTO member] imported into the territory of any other [WTO member] shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products."
[7] It is the WTO's General Agreement on Tariffs and Trade (GATT) that contains the national treatment obligation with respect to trade in goods. The WTO's General Agreement on Trade in Services (GATS) and the United States' commitments in its GATS schedules include a comparable, but not identical, national treatment obligation with respect to imports of services.
[8] The question of whether the cash-flow tax is a tax imposed on imports (as opposed to a tax on the profits of domestic corporations that receive the revenue from their ultimate sale) is related to the issue discussed below of whether the tax would be considered a direct tax on producers versus an indirect tax on products. As a general rule, it is only indirect taxes that are considered eligible for border adjustments.
[9] The Blueprint states that it provides for border adjustments "exempting exports and taxing imports" and that "products, services and intangibles that are imported into the United States will be subject to U.S. tax regardless of where they are produced," making it clear that the tax applies to all imports. Blueprint for America at 27-28.

services that they import. The lack of a deduction for imports would be considered either:

> 1) the equivalent of a tax on imports themselves—which in WTO terms will be considered a tariff on the imports, which would violate our obligation under Article II of the GATT to charge no more in tariffs than is set forth in our tariff schedule[10], or would violate the Article II requirement not to impose on imports an "other duty or charge of any kind,"[11] or
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> 2) the application of an internal tax to imports—which is permitted under Article II(2)(a) of the GATT so long as it does not violate our national treatment requirements--meaning the tax on imports is not greater than the tax on comparable domestically-made goods.[12]

Either way, the absence of a deduction for the value of imports would be considered a tax or an "other charge" on imports, subject to the rules of the WTO. If it is considered an "other charge" on imports, it is entirely prohibited. If, as is far more likely, it is considered an internal tax on domestic products that has also been imposed on imports ("a charge equivalent to an internal tax" under Article II(2)(a)), then it is subject to the national treatment test that it not impose a tax that treats imports less favorably than domestic products.[13]

Because the Ryan-Brady plan would permit the cost of domestic wages and domestic input materials to be deducted from the value of domestically-made goods but not from the value of imports, the amount of the cash flow tax would unquestionably be more for imports than for domestically-made goods. This treatment would be a clear

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[10] Because the US has chosen to bind virtually all of its tariffs in a schedule filed with the WTO and to charge imports only the tariff rate that is reflected in that schedule, the imposition of any amount of additional tariff on imports would violate the US' tariff schedule commitments.

[11] Article II of GATT prohibits charging tariffs in excess of those in each country's tariff schedule. It also provides that imports "shall also be exempt from all other duties or charges of any kind imposed on or in connection with [importation]." Article II:1(b).

[12] GATT Article II: 2(a) provides an exception to the ban on additional tariffs or charges on imports for "a charge equivalent to an internal tax imposed consistently with the provisions of paragraph 2 of Article III (national treatment requirement) in respect of the like domestic product or in respect of an article from which the imported product has been manufactured or produced in whole or in part." Article III:2 (second sentence) places a similar requirement to ensure that any taxes imposed on imports that are directly competitive or substitutable (but not necessarily "like") domestic products be similar to the taxes imposed on domestic products.

[13] GATT Article III:1 states the recognition that "internal taxes and other internal charges . . . should not be applied to imported or domestic products so as to afford protection to domestic production."

violation of the basic national treatment rules of the WTO.[14] The reduction in revenue from domestic sales by any amount of domestic labor costs would result in a lesser amount of tax on domestically-made goods than on comparable imported goods. Whether a lesser tax on domestic products would also stem from the use of domestic input materials would depend on whether the cash-flow tax already collected on the sale of the domestic inputs themselves precisely offsets the value of the deduction for using the domestically-made input in the final product. If it did not, then the exclusion of the value of domestic input materials from domestic goods but not from imports could exacerbate the amount of discrimination against imports.

A finding of discrimination would be true whether the tax was considered a direct tax on producers or an indirect tax on products. And the test for discrimination is a strict one—if the tax on imports is higher than the tax on domestic products by even a tiny fraction, a violation can be deemed to have occurred.[15]

Those contending that the Ryan-Brady tax is consistent with the WTO largely base their claims on the contention that this tax would be analogous to a Value-Added Tax (VAT). VAT taxes are widely used throughout the world and are routinely imposed on imported goods with no claims of WTO violations.[16] However, there are critical distinctions between the Ryan-Brady plan and traditional VAT taxes. The most important difference is the exemption for wages that would be permitted under the Ryan-Brady plan but is not a feature of traditional VATs. Moreover, all taxes on imports—including traditional VATs—are subject to the national treatment requirement, so if a traditional VAT were imposed in a manner that discriminated against imports, it would also violate the WTO.

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[14] See, for example, Hufbauer and Lu, "*Border Tax Adjustments: Assessing Risks and Rewards*," Peterson Institute for International Economics, Policy Brief 17-3, January 2017, which notes: "The deduction of wages means that the chain of value subject to taxation never reaches worker compensation. Hence the cash flow tax rate, when applied to the entire cost of imported inputs, reaches a broader tax base (since it includes direct and indirect wages) than when applied jut to cash flow (which excludes these wages). The result is a tax on imported inputs that exceeds the tax on cash flow."

[15] According to the Appellate Body, "[e]ven the smallest amount of 'excess' is too much. The prohibition of discriminatory taxes in Article III:2, first sentence, is not conditional on a 'trade effects test' nor is it qualified by a *de minimis* standard." Appellate Body Report, *Japan — Alcoholic Beverages II*, p. 23.

[16] Most countries utilizing a VAT system use a "credit method" VAT under which businesses can deduct from their VAT liability the amount of VATs already paid by the producers of any inputs the business buys to make the good or service sold. Japan, on the other hand, uses a form of "subtraction-method" VAT under which businesses subtract the cost of inputs from their total sales value and then pay a VAT calculated on the basis of the resulting amount of sales revenue.

Why the Plan's Treatment of Exports May Not Necessarily Violate WTO Obligations (But Probably Does)

The WTO disciplines on exports are different from those on imports, as they are centered on preventing government finances from being used to subsidize exports.[17] Therefore, the threshold question is whether the Ryan-Brady cash flow tax's treatment of exports will constitute a subsidy. Subsidies are defined in the WTO rules as a financial contribution by a government or public body that confers a benefit on the recipient.[18] A financial contribution is further defined to include "government revenue that is otherwise due [that] is foregone or not collected."[19] Therefore, whether the Ryan-Brady plan's approach to exports is permissible turns in part on whether it results in the government foregoing revenue that would otherwise be due. The Blueprint states that the cash-flow tax will be applied on a destination basis such that "products, services and intangibles that are exported outside the United States will not be subject to U.S. tax regardless of where they are produced."[20] The claim would then be that because exports are not consumed in the United States, they are simply not subject to the US cash-flow tax. Therefore, no government revenue that was "otherwise due" has been foregone by not including exports in the base on which taxes are collected and therefore no subsidy has been provided.

The WTO's jurisprudence recognizes the difficulty of determining exactly when tax revenue has been "forgone." For example, the WTO's Appellate Body noted:

> "[T]he word 'foregone' suggests that the government has given up an entitlement to raise revenue that it could otherwise have raised. This cannot, however be an entitlement in the abstract, because governments, in theory, could tax *all* revenues. There must, therefore, be some defined normative benchmark against which a comparison can be made between the revenue actually raised and the revenue that would have been raised 'otherwise' . . .[21]

In general, the jurisprudence suggests that revenue otherwise due is considered "foregone" when there is a general rule of taxation and certain exceptions to that general

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[17] The WTO rules on subsidies, codified in the Agreement on Subsidies and Countervailing Measures (ASCM), expressly prohibit subsidies that promote exports because of the trade-distorting nature of export subsidies.
[18] ASCM Article 1.1.
[19] ASCM Article 1.1(a)(1)(ii).
[20] Blueprint for America, p. 28.
[21] Appellate Body Report, *US-FSC,* paras. 90-91.

rule. If so, the exceptions may result in the government foregoing revenue that was otherwise due, thereby conferring a financial benefit on those that qualify for the exception.[22] Here, it could be argued that if the general rule is that because exports are not consumed in the US, they are not included in the Ryan-Brady destination-based consumption tax, then there is no exception to a general rule and no revenue that the government is giving up by not taxing exports.

However, it is not yet known exactly how the Ryan-Brady tax plan will be designed. If the treatment of exports were structured not as an exclusion from taxes in the first place but rather as an exemption from taxes due or a rebate on taxes paid, then it could come under the WTO disciplines on subsidies, particularly its rules on export subsidies. While this may appear to be putting form over substance, the sequencing of the analysis and the text of the WTO Agreements are important. Both are clear that the issue of whether a prohibited export subsidy has been granted starts with a determination that a subsidy exists in the first place. Indeed, the text for prohibited subsides starts with "the following subsidies, **within the meaning of Article 1** (definition of subsidy, including reference to foregone revenues) shall be prohibited."[23] As such, if a subsidy does not fall within the meaning of Article 1, it is not subject to the prohibition on export subsidies contained in ASCM Article 3.[24] The ambiguity in how the Ryan-Brady tax might be viewed stems in part from the use of the words "exemptions," "remissions," "deferrals" or "deductions" when describing taxes that may constitute a subsidy (as discussed below) when contrasted with the definition in Article 1, which provides that a subsidy shall be deemed to exist if, among other things, the government has foregone revenue that is otherwise due through the use of tax credits. If the Ryan-Brady tax plan should be found to result in the government giving up on

[22] *See*, for example, *US — Large Civil Aircraft (2nd complaint)*, where the Panel summarized the Appellate Body's guidance as "[t]he Appellate Body's analysis suggests that where it is possible to identify a general rule of taxation applied by the Member in question, a 'but for' test can be applied. In other situations, the challenged taxation measure should be compared to the treatment applied to comparable income, for taxpayers in comparable circumstances, in the jurisdiction in issue." Para. 7.120.

[23] ASCM Article 3.1. See also Panel Report, *Canada-Aircraft Credits and Guarantees,* WT/DS222, para. 7.16, "To prove the existence of an export subsidy within the meaning of this provision, a Member must therefore establish (i) the existence of a subsidy within the meaning of Article 1 of the SCM Agreement and (ii) contingency of that subsidy upon export performance."

[24] The WTO jurisprudence is clear that the prohibition on export subsidies contained in Article 3 and the *Illustrative List* do not override the basic definition of a subsidy contained in Article I of the ASCM, which requires a demonstration of foregone revenue. The Appellate Body in *US-FSC* noted "Article 1.1 sets forth the general definition of the term "subsidy" which applies 'for the purpose of this Agreement'. This definition, therefore, applies wherever the word "subsidy" occurs throughout the SCM Agreement and conditions the application of the provisions of that Agreement regarding prohibited subsidies in Part II, actionable subsidies in Part III, non-actionable subsidies in Part IV and countervailing measures in Part V." para. 93.

revenue that would otherwise be due, then the disciplines on export subsidies would apply.

As a general matter, subsidies for exports are prohibited, while non-export subsidies are subject to disciplines as "actionable" subsidies only if they cause adverse effects to other countries.[25] The ASCM includes some guidance on which subsidies constitute prohibited export subsidies in its *Illustrative List of Export Subsides* (Annex I to ASCM). That *Illustrative List* includes a number of tax measures that would constitute prohibited export subsidies and draws a distinction between direct taxes (on producers) and indirect taxes (on products), defining direct taxes as "taxes on wages, profits . . . and all other forms of incomes" while defining indirect taxes as "sales, excise, turnover, value added . . . and all taxes other than direct taxes and import charges."[26] As such, the *Illustrative List* suggests that rebates or deductions or refunds for taxes related to exports are permitted under the WTO rules if two conditions are met:

1) The tax must be considered an indirect tax on products, rather than a direct tax on producers; and

2) The rebate on exports must not exceed the amount levied on the same goods or services when they are sold for domestic consumption in the U.S.[27]

While there has been considerable debate about where to draw the line between (direct) taxes on producers versus (indirect) taxes on products, the WTO-consistency of the Ryan-Brady plan could depend on which side of the line the tax falls on.[28]

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[25] ASCM Article 3. "[T]he following subsidies . . . **shall be prohibited**: a) subsidies contingent, in law or in fact . . . upon export performance, including those illustrated in Annex I (the *Illustrative List)*." (emphasis added).
[26] ASCM, Annex I, footnote 58.
[27] The two direct taxes expressly noted as prohibited exports subsides are: 1) the full or partial exemption remission, or deferral specifically related to exports, of **direct taxes** or social welfare charges paid or payable by . . . commercial enterprises, and 2) the allowance of special deductions directly related to exports or export performance, over and above those granted in respect to production for domestic consumption, in the calculation of the base on which **direct taxes** are charged. (items e) and f) in the *Illustrative List*). The discipline on indirect taxes, on the other hand, bars only tax breaks for exports that exceed those provided for domestically-produced goods ("The exemption or remission, in respect of the production and distribution of exported products, of **indirect taxes** in excess of those levied in respect of the production and distribution of like products when sold for domestic consumption." (item g) in *Illustrative List)* (emphasis added).
[28] The 1970 GATT Working Party on Border Adjustments concluded that there was a consensus that taxes on products, such as excise taxes, sales taxes, and VATs, were eligible for border adjustment, while taxes not directly levied on products, such as social security or payroll taxes, were not eligible for border adjustment. Paragraph 14, 1970 Working Party Report on Border Tax Adjustments, L/3464. November 20, 1970. For an excellent discussion of the distinction between "direct" and "indirect" taxes, *see*

Therefore, the structure and design of the Ryan-Brady plan will be important in determining whether its treatment of exports fits within either the carve out from the definition of a subsidy for exports exempted from domestic taxes[29] or the allowance for exemptions or rebates from indirect taxes that do not exceed the rebate available for domestic goods.[30]

The more that the plan is structured as a direct tax on producers by imposing taxes based on the producers' accounts of their total revenues with deductions for inputs and wages, the more likely the overall tax plan is likely to be seen as a direct tax, not eligible for border adjustment. The more the tax is structured as a tax on sales, the more likely it is to be considered an indirect tax, for which border adjustments are permitted. In defending the border adjustability of the tax plan, the US can also claim that the tax falls within the catch-all phrase included within the definition of an indirect tax ("all taxes other than direct taxes") with the burden on those challenging the tax to prove that the tax is a direct tax, but whether that argument would carry the day is not certain. However, as described above, the definition of the base will also be important to this analysis, because in principle, if the base does not include foreign consumption, then the direct / indirect tax distinction does not matter.

Finally, the Ryan-Brady cash-flow tax, should it be structured in way that constitutes a subsidy, will need to be carefully designed not to violate the second requirement for permissible rebates or exemptions from taxes on exports—that the amount of the rebate granted to exports does not exceed the amount of tax on like products sold for domestic consumption. [31] If the amount of the export rebate is equal to the total sales value of the good while the same good sold for domestic consumption pays tax on the total sales value minus the cost of domestic inputs and labor, then the export rebate could also run afoul of the second requirement.

The consequences of being found to be a prohibited export subsidy are severe. Prohibited export subsidies are considered *per se* violations of the ASCM because they promote exports over domestic consumption, thereby creating trade distortions. Because they are expressly prohibited, challenges to export subsidies do not require any

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Implementing a Progressive Consumption Tax: Advantages of Adopting the VAT Credit-Method System, Itai Grinberg, National Tax Journal, Vol. LIX, No.4, December 2006.

[29] "[T]he exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption, or the remission of such duties or taxes in amounts not in excess of those which have accrued, **shall not be deemed to be a subsidy**." (ASCM Article 1.1(a)(1)(ii), footnote 1) (emphasis added).

[30] The *Illustrative List* (item (g)) prohibits exemptions from indirect taxes only when "the exemption or remission, in respect of the production and distribution of exported products . . . [is] in excess of those levied in respect of the production and distribution of like products when sold for domestic consumption."

[31] Item (g), *Illustrative List of Export Subsidies*, Annex I, ASCM.

proof that the subsidy is specific to a given enterprise or industry nor do they require proof that the subsidy causes adverse effect to others.[32] Moreover, disputes over prohibited export subsidies are subject to expedited dispute settlement procedures, as seen in the time frames set forth in Table 1 below. Note that the actual time frame in many traditional disputes has been longer than suggested by the rules.

Table 1: Time Frames for WTO Disputes Under the DSU Rules	**Traditional Disputes[33]**	**Prohibited Subsidy Disputes[34]**
Consultations	60 days	30 days
Panel proceedings	180 to 270 days	90 days
Time to request appeal of panel ruling	60 days	30 days
Appellate Body (AB) proceedings	90 days max	60 days max
Adoption of panel/AB reports	30 days	20 days
Reasonable Period of Time for compliance	460 days	Without delay
Compliance proceedings (panel + AB)	180 days	90 days
Total	1,060 to 1,150 days (2.9 to 3.1 years)	320-360 days (less than 1 year)

Because the WTO-consistency of the Ryan-Brady tax plan's approach to exports depends on a number of determinations—whether a subsidy has been provided and if so, whether the tax is a direct tax on producers—the picture for exports is much murkier than for imports. The plan's treatment of imports is a clear violation of the WTO rules, while the treatment of exports is less clear.

How the WTO (and Others) Could Punish the United States for Treaty Violations

Some commentators examining the tax plan take comfort from the fact that WTO disputes tend to be lengthy and that the disciplines, at least with respect to export subsidies, may be uncertain. According to this view, the US therefore has lots of time

[32] ASCM Article 2.3. "Any subsidy falling under the provisions of Article 3 (prohibited subsidies) shall be deemed to be specific."

[33] Time frames for most disputes are provided in the WTO's Dispute Settlement Understanding (DSU). The expedited rules for disputes over prohibited subsidies are set forth in Article 4 of the ASCM and take precedence over the traditional time frames pursuant to Appendix 2 to the DSU.

[34] In addition to the specific time frames noted in Table 2, Article 4.12 of the ASCM provides that all other time periods applicable shall be half the time prescribed in the DSU rules for traditional disputes.

before our trading partners will be authorized to retaliate against the United States should the tax plan be found to violate WTO rules. Others contend that few countries would be willing to challenge the US in such a big dispute, fearing retaliation or other measures restricting their access to the US market. Yet others take the view that the US will be given significant leeway as it seeks to reframe its tax code to better align the US system with other countries around the world and to reduce the incentives to locate production facilities abroad. Some claim that the case is so unusual and so large that the WTO would be reluctant to take it on for fear that it could destroy the trading system.

All of these arguments deserve to be heard and understood. While it is true that a WTO challenge to the Ryan-Brady tax plan and an ultimate determination permitting retaliation would be highly unusual, there is no mechanism in the dispute settlement system for the WTO to refuse to hear a case just because it is very large or politically difficult. The authorization of retaliation is in itself fairly rare, with only 13 out of more than 500 disputes resulting in authorized retaliation. And the amount of retaliation that could be permitted is far beyond anything seen in the WTO. Chad Bown from the Peterson Institute of International Economics suggests that retaliation for the discrimination against imports would be at least $220 billion, while the exclusion for export sales could bring an additional $165 billion in further permitted retaliation.[35] The highest previous amount of authorized retaliation was $4.043 billion in the case against the US tax exemptions for foreign sales corporations which were found to be prohibited export subsidies.[36] But because the WTO cannot refuse to resolve any dispute submitted to it, the size of the case will not prevent an adjudication of the issue, or an authorization for retaliation should the US not comply with an adverse ruling.

Nor is fear of retaliation likely to deter a challenge to the Ryan-Brady tax, as the tax affects all US trading partners and those trading partners are likely to join together in a single complaint, as multiple countries did when challenging China's export restrictions on rare earths and raw materials or in disputing the US safeguards on steel and many others.[37] As such, countries can easily seek the "safety in numbers" of a joint challenge, as it would be impossible for the US to retaliate against all challengers without starting a disastrous trade war.

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[35] PIIE forum, Border Tax Adjustments and Corporate Tax Reform, February 1, 2017, https://piie.com/events/border-tax-adjustment-and-corporate-tax-reforms.

[36] *US-Foreign Sales Corporation (FSC) (EC)* WT/DS108

[37] The challenge to the US safeguards on steel was brought by the Brazil, China, the EU, Japan, Korea, New Zealand, Norway, Switzerland, and Taiwan. The US joined with Ecuador, Guatemala, Honduras, Mexico, and Panama in challenging the EU's quota system on bananas. The challenge to China's export restrictions on raw and rare earth materials included the US, the EU, Japan, and Mexico.

Nor should the length of time it takes to resolve a dispute at the WTO give much comfort. A WTO challenge can be brought the minute a definitive tax plan is enacted, even if it has not yet come into effect.[38] Moreover, counting on having years of time before facing the consequences of enacting a WTO-illegal scheme is risky. It presumes that the rest of the world will abide by the WTO rules that prohibit countries from taking unilateral action and will patiently go through the WTO dispute settlement system. But if the US adopts a tax scheme that is a clear violation of the WTO rules and that is perceived by the world as a willful violation on our part, it may invite other countries to respond in kind.

Finally, the WTO rules provide for two types of actions against subsidized exports—1) a WTO case because export subsidies are prohibited, for which the remedy is a ruling that the subsidy be removed, and 2) a case for the imposition of countervailing duties (CVD), for which the remedy is the imposition of additional duties in an amount calculated to offset the value of the subsidy. A number of the United States' trading partners could seek such additional duties on US exports because CVDs can be imposed relatively quickly through a domestic process that does not require waiting for a WTO ruling. If our trading partners can show that the tax plan results in subsidies to our exports and that the subsidized exports caused injury to their domestic producers manufacturing products like our exports, then they can unilaterally impose additional duties on US exports, without the approval of either the United States or the WTO. Such CVD claims could result in the imposition of additional duties on US exports within 12 to 15 months.

In sum, the enactment of a tax plan that includes provisions that are clear violations of our WTO obligations risks significant litigation, retaliation from our trading partners, possible additional duties on US exports, and carries the potential to start a trade war. The Congress should be very careful in enacting reforms to our corporate tax system to avoid obvious WTO violations.

[38] There are already reports that the EU is preparing a challenge to the Ryan-Brady plan, should it be enacted as it appears to be currently envisioned. "EU and others gear up for WTO challenge to US border tax," Financial Times, February 13, 2017, https://www.ft.com/content/cdaa0b76-f20d-11e6-8758-6876151821a6