

Internal Tax Regime of WTO: A Clog in the Wheel of Economic Progress of the Developing Countries

S.M. OLOKOOBA, J.O. OLATOKE
University of Ilorin, Nigeria

B.B. ORUBEBE
Novena University, Ogume, Delta State, Nigeria

Abstract: The basic principles of the WTO are built on the foundation of GATT. However, even though those principles are far reaching in importance, their effects on the developed and developing nation's economy are not equitable. While the principles look novel and economically viable, some of them are damaging to the economic progress of the developing countries. One of such principle is the internal tax regime of the WTO. This paper therefore examines what this principle is all about, how some constitute a clog in the wheel of economic progress of the developing nations as well as solution thereto in form of recommendation.

Key Words: Internal Tax Regime, WTO, Clog, Wheel of Economic Progress, Developing Countries.

1. Introduction

The World Trade Organisation (WTO) was established in 1994 at the end of the General Agreement on Tariffs and Trade (GATT) of Multinational trade negotiations (MTNs), which started in September, 1986 and ended in Marakesh in December, 1994(Paul, 2013:36).The earlier General Agreement on

Tariffs and Trade (GATT) was formed as a means of achieving peaceful trade dispute settlement system amongst the Nations of the world. The formation after some years metamorphosis to the World Trade Organisation (WTO) through Uruguay Round.

About two third of the WTO's members are developing countries. These countries are playing an increasingly important and active role in the WTO because of their numbers, and God-given natural resources which unfortunately, the developed countries now turned to their own advantages at the detriment of the developing nations. This is because while developing countries produce and supply the raw materials needed for the technological know how of the developed countries cheaply, the finished products are exported back into the developing countries expensively.

Developing countries are a highly diverse group often with very different views and concerns and today, many African and other developing countries believed that Africa had virtually lost out in the global economic politics, and that, the public interest and objectives of trade liberalisation of WTO have actually been turned to a paraphernalia of neo-colonisation of the

developing countries economy (Animashaun, Olokooba, Olatoke, 2016:256).

One of the so-call liberalisation tendency in the WTO activities is the internal tax regime which though on the face of it looks economical reasonable for the encouragement of trade competitiveness and liberalisation, but which on the contrary is more beneficial to the developed nations than the developing ones because the so-called trade, commerce and services are not even available in the developing countries because their economy depend largely on the dictate of the developed economy.

Structured into five sections, an appraisal of the internal tax regime of the World Trade Organisation (WTO) is in the second section of the paper. In the third section, the paper examines the usefulness of taxation while section four examines how the internal tax regime of World Trade Organisation (WTO) constitute a clog in the wheel of developing countries economic progress. The paper ends in section five with conclusion and recommendations.

2. Usefulness of Taxation

Globally, tax is one of the means by which government generate revenue to execute some socio, economic and political activities that may be beneficial to the citizenry. Contemporarily, tax is always the last saving grace whenever any countries adjunct revenue resource is dwindling. Most of the developed economy also depends majorly on revenue generation from tax. Refusal to pay tax is a crime against the state; this is known as tax evasion. In fact, Nonpayment of tax may lead to a catastrophic and unpalatable socio- political and economic upheaval in a given society, not surprising, when Jesus was asked in the Bible about the appropriateness of the payment of tax to the authority his respond was 'give unto Caesar the things that are Caesar's and unto God, the things that are God's (Mark 2:17).'

Nigeria is today overhauling her tax system because the reality of non-sustainability and continuity of oil revenue is now in the fore.

Similarly most states now rely on internally generated tax revenue for their survival. Lagos state in the past survived on internal revenue when the federal governments failed to release their share of 'national cake'-oil revenue to them in 2007. Among the usefulness of tax according to Olokooba and Sulait, 2015:230, are that taxes provide the money that makes it possible for government to function, it also has some other economic significances to wit, the provision of employment, satisfactory rates of economic growth, and stability of money supply in any economy. The economic goals of taxation are achieved by raising or lowering tax rates.

Furthermore, tax can serve as a regulatory mechanism to control and regulate various forms of business activities. For instance, alcoholic beverages and tobacco may be taxed heavily on the grounds that their use is hazardous to the health of individuals. Such revenue, often called a "sin tax", is in fact a penalty paid by the users of the substance. Similarly, Government can control private consumption, especially of imported goods, by increasing customs tariffs but where there is an increase in taxation on personal income, it may result in a decrease in private savings without affecting the level of consumption (Olokooba, Suliat, *supra*). Tax can also be used for redistribution of wealth. Tax is also an effective tool of checking inflation and inequality trade balance between Nations. The less taxes countries pay on exportation, the higher their exportation and the less revenue for the import countries. On the other hand, the higher taxes the import counties levied on importation, the higher revenue they made on such importation. Higher taxes on importation will also protect the local industries and ensure their viability because they will be able to produce at the maximum level to meet the local market demand.

Based on all the aforementioned usefulness, it is trite to posit that stopping any developing nation from effective use of internal revenue taxation cannot be economically viable to the development of such nation? Instead, such act is simply going to be a clog in the wheel of developing countries economic progress. More so since a good tax system is said to be helping

the attainment of the benefits of the law. (Per Lord Dunedin in *Whitney v. Inland Revenue Commissioners* (1926) A.C. 37)

3. Internal Tax Regime of the World Trade Organisation (WTO) Appraised

One representative at the Geneva drafting session suggested that although a “complete legal definition” of internal tax could not be stated, but it may probably meant a tax collected after the goods leave customs (U.N. Doc. EPCT/A/PV. 43, at 24 (1947)). This was immediately refuted by the French representatives who noted that “we have a tax on turnover and a luxury tax, and these are collected by the customs authorities, but they are however, internal taxes”(GATT, Annex 1, Ad. Art.III). The draftsman agreed that exemptions from income taxes did not come within the terms of Article III in GATT, since the language refers specifically to internal taxes on “products.” (UN.Docs.E/Conf.2/C.32,at 1 (1947-1948))

The deliberations at the Havana Conference provided more interpretative material on the meaning of “internal tax or charges.” Relevant committee report note that charges imposed on the transfer of payments for imports or exports, “particularly the charges imposed by countries employing multiple currency practices...(consistent) with the Articles of...the International Monetary fund, would not be covered” (Havana Reports, UN/Doc.ICITO/1/8,at 62,(1948)) by this national treatment obligation. The Committee Report likewise established the fact that “charges are described as internal taxes in the laws of the importing countries would not of itself have the effect of giving them the status of internal taxes under” Article III (Havana Reports, UN/Doc.ICITO/1/8,at 62,(1948)). Certain charges of several countries ‘were examined and it was decided that the original language of Article III in GATT (before the Havana amendments) included the following clause:

In cases in which there is no substantial domestic production of like products of national

origin, no contracting parties shall apply new or internal taxes on the products of the territories of other contracting parties for the purpose of affording protection to the production of directly competitive or substitutable products which are not similarly taxed; and existing internal taxes of this kind shall be subject to negotiation for their reduction or elimination. (GATT, Final Act, Geneva, Art.II Para1,55U.N.T.S,204, (1947)

This language was eliminated from the text of the Article when the 1948 amendments took effect, but an interpretative note was added to GATT that preserved an obligation with respect to “directly competitive or substitutable products.” (Protocol Modifying Part II and Article XXVI of the GATT, 1948 (Agreement No. 10 in APP.C)). The purpose of the language regarding competitive products was illustrated in the preparatory work as follows:

Let us suppose that some country in its negotiations had secured the binding of the duty on oranges. Country A gets a binding on the duty of oranges from country B. now, country B after that can proceed to put on an internal duty of any height at all on oranges, seeing that it grows no oranges itself But by putting on that very high duty on oranges, it protects the apples which it grow itself The consequence is that the binding duty which country A has secured from Country B on its oranges is made of no effect, because of the fact that price of oranges is pushed up so high by this internal duty that no one can buy them. The consequence is that the object of that binding is defeated (U.N. Doc. EPCT/A/PV.9 at 7 (1947)).

A broader relationship than that of “like products” is contemplated by competitive products, since it was recognized that different products could compete so that internal discrimination in favour of one product (“coincidentally” produced at home) could operate to prevent another products’ sales. The difficult problem, of course, is determining what competitive products are. The draftsman avoided setting forth a precise definition, (U.N. Doc. E/Conf.2 /C.3/SR.40, at 1 (1947)) but a number of examples were given. For instance, delegates seemed to agree that among things that could be

competitive products were: tung oil and linseed oil, tramways and buses, coal and fuel oil although one delegate said it would depend on the specific factual competitive situation in each case (U.N. Doc. E/Conf.2 /C.3/SR.40, at 1 (1947)).

4. Internal Tax Regime of WTO as A Clog

Contemporarily and as outlined above, the role tax plays in government's economic, political as well as social policy cannot be underestimated, therefore, any rule or law enacted to debar or debase the objective of tax no matter for whatever motive, save revenue generation; to that extend is inconsistent with tax principle. (Agbonika, 2015:17-19, Olokooba 2010: 12-10). For this, Article III paragraph I of GATT which forbids any state to levy internal taxation is not of taxation and not in line of general tax principles.

Even though, Article III, Paragraph 1, states the general obligation to avoid using internal government measures for the protection of domestic production, but the second paragraph gives the obligation as to internal taxation in more precise language and it shows more of restriction in revenue generation through tax instead of protection of domestic market. According to the paragraph, *The products of the territory of any contracting party imported into the territory of any other contracting party 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. Moreover, no contracting party shall otherwise apply internal taxes or other internal charges to imported or domestic products in a manner contrary to the principles set fourth in paragraph 1*

The evil that the draftsman sought to proscribe by the first sentence was an internal tax applied discriminatorily to imported products, thus operating as effectively as a tariff to protect local products against foreign competition. The obligation to avoid discriminatory internal taxes

is not confined to Schedule items but applies to all goods.

The germane question here however is that, is there an equitable distribution of resources between developing and developed countries that can necessitate the stoppage of developing nations from using internal tax to check the flooding of their local market with foreign goods? Who directly or indirectly are the forces controlling even the domestic market itself? The answer is obvious; the controlling forces through International Institutions like International Monetary Fund, World Bank and other multinational companies are the developed nations of the world. Why then should the developing government not use internal tax measures for the protection of her domestic production?

Agriculture which serves as the major economic source of developing nations unfortunately is also being controlled indirectly by the developed nations. Both import and export is being dictated by the Dollar status and value in the International market. In fact, African farmers often had poor yields and were themselves extremely poor (Animashaun *et al*, 267-268). Despite this bad situation,

The big nations still establish the price of agricultural products and subject these prices to frequent reductions.

At the same time the price of manufactured goods is also set by them, along with the freight rates necessary for trade in the ships of those nation. The minerals of Africa also fall into the same category as agricultural produce as pricing is concerned (Rodney, 2005:18-19).

The expansion in the volume of imported goods and services has been dramatic, exceeding that of exports. Agriculture's contribution to output fell almost continuously and the negative growth rate experienced by the agricultural sector is all the more disturbing when account is taken of the facts that its decline would be greater if we consider per capital terms, it also has adverse effects on the balance of trade, industrial costs.... (Okongwu, 1986:20) Today, *...Africa became increasingly underdeveloped in comparison with the industrialised area of the world.*

The pattern of trade between Africa and the industrialising world in the nineteenth century is a pattern that still exists today....Europe robbed Africa of her surplus products to feed its own economy, obtaining Africa exports at low prices and using them to boost its own industrialisation, thus steadily widening the gap between itself and Africa.... (Michael, Donald, 1980:6)

The dichotomy between a developed, underdeveloped or developing economy which most African countries belongs is of glaring magnitude. According to Rodney (*supra*)

...The developed countries are all industrialised that is to say, the greater part of their working population is engaged in industry rather than agriculture, and most of their wealth comes out of mines, factories, e.t.c. They have high output of labour per man in industry because of their advanced technology and skill.... It is also striking that the developed countries have a much more advanced agriculture than the rest of the world. Their agricultural has already become industry.....

Trapped in a global system fostered by imperialism, poor countries are left with little to sell but the labour of their people and the wellbeing of their environment. While Developed Nations “select location of their factory, plantation or mine, communities around the impoverished world vie for suspect opportunities to be the next expansion site for the global system of exploitation of natural resources for trade”(Adamu, 2010:4) The situation of poor countries has been dubbed ‘the global race to the bottom’(Hossay, 2006:4)

Even other natural resources that the developing nations are using to survive are now facing problem because most of those resources are either going into extinction or gradually disappearance due to climate change. Nigerian as a nation is facing her own problem through constant reduction and fall in her revenue generation from oil. In fact, going by World Bank prediction, Nigerian Crude oil may dry off in couple of years to come (Olokooba, 999). To cushion all these negatives, internal tax on importation would have been the best option.

On the international scene, internal taxes on certain types of goods such as coffee, tea, or tobacco, have posed a particular problem to GATT. Often these goods are almost wholly imported and, when combined with their “luxury” nature, they pose a very attractive revenue target for government treasuries. Thus very high internal taxes often exist on these items. For generally GATT Docs.L/1732, at 5; L/ 1768, at 7 (1962). For a specific example of high internal charges on tropical products see GATT Doc. Com.Td/G/W/10, at 5 (1965). The less developed countries’ products often face even higher internal taxes when they have been processed, e.g., roasted coffee. Id. The contracting parties are now required to “(i) refrain from imposing new fiscal measures, and (ii) in any adjustments of fiscal policy accord high priority to the reduction and elimination of fiscal measures, which would hamper, or which hamper, significantly” the export of primary goods, new or processed, from less- developed countries, GATT Art. XXXVII, Para. 1 (c). see also the EEC’s problems in renegotiating concessions once a common tariff was reached on manufactured tobacco and petroleum products in GATT Docs. L/2039 (1963); L/2234 (1964); L/2762 (1967; L/2997 (1968.)

When imposed by industrialized nations, such taxes may operate to reduce export earning of producing countries and, when the latter are less- developed countries (which is often the case when the products are “tropical”), the effect may be inconsistent with policies aimed at promoting development in the countries. If the price elasticity of demand is high, the internal tax will have the effect of decreasing imports. If, on the other hand, the price elasticity of demand is low (as seems to be the case with goods like coffee and tobacco) there may be simply some diversion of the potential price charged from the producing nation to the taxing nation. The non-discrimination obligation of GATT, even when extended beyond like products to competing or substitutable products,” will not suffice to reach this problem. It may be that only a broad balance of payments or balanced of trade approach to trade obligations in GATT would reach this type of problem, Thus an obligation might have to be

frame which would prohibits an industrialized nation from doing anything which would detrimentally affect the foreign exchange earnings by trade of the less developed country. An attempt to handle this on a product-by-product basis, using the concept on nondiscrimination, does not seem sufficient. But cf. GATT Art XXXVII. Para. 1 (c), at note 18 *supra*

Complaints brought in GATT indicate that sales taxes, luxury taxes, and turnover cannot be applied in such a way as to discriminate against imported goods. In fact, Brazil acknowledged that a number of her internal taxes discriminated against imports. Some she justified as existing legislation; others she acknowledged were contrary to GATT and these she promised to ask the Brazilian Congress to eliminate. GATT, 2 BISD 181 (1952). The Brazilian Congress resisted and did not comply until 1957. GATT Doc. L/729 (1957)

Granting exemption from such taxes for domestic goods but not for imported goods is also a violation of Article III, as it is a discriminatory application of such a tax even though the tax law reveals no discrimination on its face. Great Britain complained of a 2% differential (4% - 6%) in the rate of the Italian turnover applied to domestic versus imported pharmaceutical products. A violation of GATT Article III was alleged. (GATT Doc.L/421 (1955). Similarly, 'The Netherlands complained to the contracting parties of the Utility sentiment" used by Great Britain to impose its purchase tax, whereby certain domestically produced consumer goods were exempted from the tax while the like imports were not. Great Britain agreed that the tax was improper under GATT. (GATT Doc. CP 5.! SR.20 (1950). Britain later reported that an expert committee had been appointed to study the problem. (GATT Doc. CP.6/SR.7 (1951). One year later, upon the recommendation of her study committee, Britain abolished the utility system; thus removing the discriminatory aspect of the purchased tax. (GATT Doc. SR.7/5 (1952). Invariably, the root effect of this will be an opening of more avenues for the developed nations to be able to flood African market an

action that would have effectively been checked with the imposition of higher tax.

5. Conclusion and Recommendations

From the foregoing, it could be gleaned that the actual reasons for the internal tax regime of the WTO is far from ordinary free flow of and/or liberalisation of trade among nations, but one of neo colonialism in disguise. The internal tax regime of WTO looks more like an instrument of blockage of the developing nation's revenue generation through tax. In nut shell, the devastating effect of such regime is better imagining than witnessing. The power to tax internally which would have resulted in increased revenue generation, protections of developing nations industries as well as paraphernalia of development has been curtailed through the provision of Article III, Paragraph 1 in GATT. Conclusively therefore, the combined effect of Article III, Paragraph 1 in GATT, low industrial level with it attendant result of dependency on imported goods and services by most developing countries simply means that the developing economy will be facing an outward flow of investment and absence of direct control of trade and investment in their country which will constitute a great clog in the wheel of economic progress of the developing countries. To effectively check this situation, this paper recommends for the amendment of Article III paragraph 1 in GATT to allow for complete internal taxation of goods, trades and services imported into the developing countries. Doing this will actually accelerate the rate of development of the developing nations economy.

References

- Adamu K.U 'The Law and Policy of Trade Libralization and the Rise in Environmental Degradation and Global Terrorism', *Ahmadu Bello University Journal of Commercial Law*, vol.5., No. 1, 2010-2012
- Agbonika J.A.A. *Problems of Personal Income Tax in Nigeria* (Ababa Press Ltd, Ibadan, 2015)

- Hossay P. ‘*Unsustainable: A Primer for Global Environmental and Social Justice*’, (Pub. Zed Books, London & New-York, 2006), p.132., see also *ibid*, p.4
- Michael, T, Donald, L, *A History of Africa 1840-1914* (London: Edward Arnold Publishers, 1980)
- Okongwu C.S.P *The Nigerian Economy: Anatomy of a Traumatized Economy with some Proposals for Stabilization*, (Enugu: Fourth New Dimension Publishing Co. Ltd, 1986)
- Olokooba S.M and Suliati R.A ‘Managing Conflicts and other Challenges of Nationhood in Nigeria: Experimenting with Good Taxing System as a Paraphernalia’ (*Al-Hikmah University Law Journal* Vol.1(1), 2015)
- Olokooba S.M, *Law of Taxation II* (National Open University, Lagos, 2010)
- Olokooba S.M ‘Taxation: A Noah’s Ark in the event Nigerian Oil Dries Off’, in Uchefula C *et al Law, Social Justice and Development: A Festschrift for Professor UBA Nnabue*, (Imo State University,)
- Paul. I.O “Implementation of the WTO/TRIPS Agreement by Nigeria: Strengthening Protection and Enforcement Mechanisms” in *Nigerian Journal of Food, Drug and Health Law*, vol.6, No. 1, 2013
- Rodney W, *How Europe Underdeveloped Africa*, (Abuja, Panaf Publishing Inc, 2005)
- Shola Animashaun, Olokooba S.M and Olatoke J.O ‘The Proposed New Issues and the Relevance of Africa Membership of the World Trade Organisation (WTO) Examined’ in JAM Agbonika *et, el* (eds.) *Topical Issues in the Nigerian Law: A Book of Readings* (Faculty of Law, Kogi State University, Anyigba, 2016)
- Per Lord Dunedin in *Whitney v. Inland Revenue Commissioners* (1926) A.C. 37
- Statutes**
 U.N. Doc. EPCT/A/PV. 43, at 24 (1947)
 U.N. Docs. E/Conf.2/C.3/SR.13.at 1; E/Conf.2./C.3. A/w/32, at 1 (1947-1948)
 U.N. Doc. EPCT/A/PV.9 at 7 (1947)
 U.N. Doc. E/Conf.2 /C.3/SR.40, at 1 (1947)
- International Documents**
 GATT Docs.L/1732, at 5; L/ 1768, at 7 (1962).
 GATT Doc. Com.Td/G/W/10, at 5 (1965).
 GATT Docs. L/2039 (1963); L/2234 (1964); L/2762 (1967; L/2997 (1968.)
 GATT, 2 BISD 181 (1952).
 GATT Doc. L/729 (1957)
 GATT Article III, paragraph 2 GATT Doc. L/234, at 1 (1954)
 GATT Doc. CP 5.! SR.20 (1950).
 GATT Doc. CP.6/SR.7 (1951).
 GATT Doc. SR.7/5 (1952)
 GATT, final Act, Geneva, Art, II, Para 1, 55 U.N.T.S. 204 (1947)
 Havana Reports, U.N/ Doc. ICITO/1/8, at 62 (1948)
 Protocol Modifying Part II and Article XXVI of the GATT, 1948 (Agreement No. 10 in APP.C)
- On-Line Materials**
 <
http://www.wto.org/english/thewto_e/whatis_e/tif_e/dev1_e.htm> accessed on the 9th /11/2014