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# WTO Appellate Body Report: Argentina – Financial Services

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## Summary

**Decision:** The WTO Appellate Body has dismissed claims by Panama against Argentina's "tax transparency" regulations. The Appellate Body reversed an earlier ruling by a WTO Panel that these measures violated Argentina's obligations under the General Agreement on Trade in Services (GATS).

## Significance of decision

This much-anticipated decision was expected to provide guidance on whether, and to what extent, WTO Members may take measures to address tax transparency issues. International attention to this appeal was heightened by the events of recent weeks, including the "Panama Papers". However, the Appellate Body rendered an extremely narrow decision that sheds relatively little light on the substantive issues in dispute.

Argentina argued, among other things, that its regulations were "defensive tax measures" that were designed to "protect Argentina's tax base by preventing tax evasion, tax avoidance, and fraud". Argentina's asserted that its measures "serve to prevent concealment and laundering of money of criminal origin" and were meant to "protect investors and the soundness of the Argentine financial system". Argentina's law distinguished between "countries cooperating for tax transparency purposes" and "countries not cooperating for tax transparency purposes". It adopted four separate tax measures, as well as measures relating to access to the reinsurance sector, the capital market, and the foreign exchange market. It also imposed requirements with respect to the registration of branches of foreign companies.

The September 2015 Panel decision found, among other things, that the Argentine measures violated the MFN obligation of GATS Article II because they did "not accord, immediately and unconditionally, to services and service suppliers of non cooperative countries treatment no less favourable than that which they accord to like services and

service suppliers of cooperative countries". The Appellate Body overturned that ruling on the grounds that the Panel had used an erroneous "likeness" test. But it did not go on to determine for itself whether the services at issue were "like". Indeed, having reversed the Panel on this threshold issue (and the consequent substantive findings that flowed from it), the Appellate Body took pains to emphasize that "we have taken no view on whether the services and service suppliers of cooperative countries are 'like' the services and service suppliers of non-cooperative countries, or 'like' Argentine services and service suppliers".

Following the Appellate Body's ruling it thus remains unclear whether WTO Members may take measures against countries that are considered to be "not cooperating for tax transparency purposes". This presumably will have to be resolved in a future dispute, perhaps with other litigating parties.

Another notable feature of this decision is that this is the first case since the advent of the WTO to interpret the so-called "prudential carve-out". This exception – set out in the GATS Annex on Financial Services – provides in part that "[n]otwithstanding any other provisions of the Agreement, a Member shall not be prevented from taking measures for prudential reasons, including for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system".

The scope of the prudential carve-out is important, and has generally been interpreted broadly by national regulators, particularly during and after the 2008 financial crisis. In the current dispute, the United States as a third party argued that "the prudential exception preserves the broad discretion of national authorities to protect the financial system, and includes measures directed at individual financial institutions or cross-border financial services suppliers and measures to promote systemic stability". The United States also argued that "the term 'prudential measures' includes 'precautionary measures'".

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The Appellate Body found that the prudential carve-out could in principle be invoked “to justify inconsistencies with all of a Member’s obligations under the GATS”. However, a more critical issue – the meaning of the term “prudential reasons” – was not appealed. This, too, will need to await a future dispute.

## Report

### Background

To be designated as “cooperative”, a country had either (i) to sign with Argentina an agreement on the exchange of tax information, or a double taxation treaty “with a broad information exchange clause, provided that there is an effective exchange of information”; or (ii) initiate with Argentina the negotiations necessary for concluding such an agreement or convention. (Panama was “for many years” classified as a “non-cooperative country”. After the Panel was established in this dispute, Argentina added Panama to the list of “cooperative” countries, even though, as the Appellate Body noted, “it did not have in place a double taxation convention or an information exchange agreement with Argentina, and was not negotiating such a convention or agreement with Argentina”.

### Threshold issue: Panel’s “likeness analysis” considered flawed

Argentina appealed the Panel’s findings that the services and service suppliers at issue are “like” under GATS Article II and Article XVII. This was an important threshold issue in the dispute.

GATS Article II set out the MFN obligation. It provides in part that “each Member shall accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favourable than that it accords to like services and service suppliers of any other country”. GATS Article XVII, which provides for national treatment, states that in sectors for which services commitments have been scheduled, “each Member shall accord to services and service suppliers of any other Member, in respect of all measures affecting the supply of services, treatment no less favourable than that it accords to its own like services and service suppliers”.

The Appellate Body found that the Panel in this dispute erred in its “likeness” analysis. The Appellate Body began by noting that “the concept of ‘likeness’ of services and service suppliers under Articles II:1 and XVII:1 of the GATS is concerned with the competitive relationship of services

and service suppliers”. It added that this approach was “consonant with the Appellate Body’s understanding of ‘likeness’ in the ambit of trade in goods”. The Appellate Body stressed that “the fundamental purpose of the comparison” was “to assess whether and to what extent the services and service suppliers at issue are in a competitive relationship”. It noted that “[t]he existence of a competitive relationship is a precondition for the subsequent analysis under the requirement of ‘treatment no less favourable’ of whether the conditions of competition have been modified”.

The Appellate Body then examined the so-called “presumption of likeness”. It found that “where a measure provides for a distinction based exclusively on origin, there will or can be services and service suppliers that are the same in all respects except for origin and, accordingly, ‘likeness’ can be presumed[.]” Thus, “if a complainant succeeds in making a prima facie case that a measure draws a distinction between services and service suppliers based exclusively on origin, and this is not rebutted by the respondent, the services and service suppliers at issue may be presumed to be ‘like’, and a panel may proceed with the analysis of less favourable treatment without the need to assess the competitive relationship of the services and service suppliers at issue based on the relevant criteria as adapted to trade in services”.

Turning to the facts of the present dispute, the Appellate Body found that the Panel did not make a finding that the difference in treatment was based “exclusively” on origin. The Appellate Body pointed to statements by the Panel that “the classification of a country as cooperative or non-cooperative is not based on ‘origin per se’, but on ‘the regulatory framework inextricably linked to such origin’”. This, according to the Appellate Body, was an error of law.

The Appellate Body therefore reversed the Panel’s finding that the services and service suppliers of cooperative countries were “like” the services and service suppliers of non-cooperative countries. It similarly overturned the Panel’s findings that Argentina’s eight measures violated the MFN obligation of GATS Article II, and that certain of the measures were not inconsistent with GATS Article XVII.

Although the Appellate Body found that the Panel had erred in its analysis, it declined to rule on whether the services at issue in this dispute were indeed “like” or not. Although Argentina had asked the Appellate Body to “complete the analysis” on this issue, the Appellate Body found that the condition for that request had not been met.

The Appellate Body's reversal of the Panel's "likeness" finding meant that "there remains no finding of inconsistency with the GATS", and this "render[ed] moot" the issues of less favourable treatment, or whether Argentina's measures could be justified under the exception provided for in GATS Article XIV(c) or the Prudential carve-out. However, given their "implications for the interpretation of provisions of the GATS", the Appellate Body provided views on these issues, as discussed below.

### **Treatment no less favorable: no "additional step analysis" on regulatory aspects**

The Appellate Body found that "[t]he concept of 'treatment no less favourable' under both the most-favoured-nation and national treatment provisions of the GATS is focused on a measure's modification of the conditions of competition". The Appellate Body faulted the Panel for stating that in assessing less favourable treatment, it needed to "take into account regulatory aspects relating to services and service suppliers that may affect the conditions of competition". The Appellate Body concluded that "under the Panel's legal standard for 'treatment no less favourable', consideration of the regulatory aspects forms part of the examination of whether the measure modifies the conditions of competition". It added that "the Panel effectively employed an erroneous standard whereby certain regulatory aspects can 'convert' 'less favourable treatment' into 'treatment no less favourable'. However, neither the text and context of Articles II:1 and XVII of the GATS, nor the object and purpose of the GATS, provide a basis for such a legal standard".

The Appellate Body overturned the Panel's ruling on less favourable treatment for conducting what it called an "additional step analysis":

[T]he Panel came to the 'preliminary' conclusions that all of the relevant measures modify the conditions of competition to the detriment of like service suppliers of non cooperative countries and that, consequently, they fail to accord 'treatment no less favourable' to such service suppliers. Nonetheless, the Panel did not stop its analysis here. Rather, under both Article II:1 and Article XVII, the Panel went on to conduct an additional step of analysis regarding the 'regulatory aspects' in this dispute, that is, 'the possibility for Argentina to have access to tax information on foreign suppliers providing services in Argentina'. As our review... indicates, in this additional step of analysis, the Panel did not actually examine the regulatory aspects for purposes

of assessing how the measures modify the conditions of competition, but effectively employed an erroneous legal standard under which the regulatory aspects could justify the detrimental impact....

The Appellate Body found that "[t]he Panel's interpretive errors are manifested in both its articulation of the legal standard and its application of Articles II:1 and XVII to the facts of the case". It concluded that the Panel's findings on 'treatment no less favourable' "lack a proper basis and cannot stand" and it reversed the Panel's conclusion that the eight measures were inconsistent with Article II:1 of the GATS, as well as the conclusion that three measures were not inconsistent with GATS Article XVII.

### **Prudential carve-out: wide scope of application**

The Appellate Body began by noting that this was the first dispute in which a WTO Member had invoked the prudential carve-out.

The prudential carve-out is provided for in paragraph 2(a) of the Annex on Financial Services (entitled "Domestic Regulation"). The Appellate Body agreed with the Panel that:

[P]aragraph 2(a) contains three requirements that must be fulfilled for a measure to be justified under this provision. First, there is the threshold, or preliminary, question of what types of measures may potentially fall within the scope of paragraph 2(a). Second, a measure must have been taken "for prudential reasons". Finally, under the second sentence of paragraph 2(a), the measure "shall not be used as a means of avoiding the Member's commitments or obligations under the Agreement". Only when a measure falls within the scope of paragraph 2(a) will there be a need to evaluate whether it was taken "for prudential reasons" and whether it fulfils the requirement in the second sentence of paragraph 2(a).

Panama's appeal was "limited to the threshold question" and so the Appellate Body did not opine on the second or third factors. Panama pointed to the title of this provision ("Domestic Regulation"), and argued that this "delimits the scope of the provision", or defined the type of measures that could be covered by it. Under Panama's interpretation, market access restrictions could not fall under the prudential carve-out.

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The Appellate Body disagreed. It reasoned that “[t]he fact that paragraph 2(a) covers violations of obligations under “any other provisions of the Agreement” means that it could be invoked to justify inconsistencies with all of a Member’s obligations under the GATS. These include, for example, a Member’s most-favoured-nation treatment obligation under Article II, market access commitments under Article XVI, or national treatment obligation under Article XVII [original emphasis]”.

The Appellate Body therefore concluded that “an interpretation of paragraph 2(a) of the Annex on Financial Services on the basis of its text, read in the light of its context and the object and purpose of the GATS, supports the view that paragraph 2(a) does not impose specific restrictions on the types of ‘measures affecting the supply of financial services’ that fall within its scope, provided that such measures fulfil all of the requirements of paragraph 2(a)”.

### **Exception under GATS Article XIV(c): compliance measures**

GATS Article XIV(c) provides an exception – similar to GATT Article XX(d) – for measures “necessary to secure compliance” with GATS-consistent laws or regulations.

The Appellate Body noted that a measure “can be said ‘to secure compliance’ with laws or regulations when its design reveals that it secures compliance with specific rules, obligations, or requirements under such laws or regulations, even if the measure cannot be guaranteed to achieve such result with absolute certainty”. It cautioned that “there is no justification under Article XIV(c) for a measure that is not designed to ‘secure compliance’ with a Member’s laws or regulations”. The second element requires an analysis of whether “this relationship is sufficiently proximate, such that the measure can be deemed to be ‘necessary’ to secure compliance with such laws or regulations”.

The Panel had found that Argentina’s measures were “provisionally” justified under GATS Article XIV(c), but that their application constituted “arbitrary and unjustifiable discrimination” within the meaning of the chapeau of GATS Article XIV. Panama appealed the Panel’s findings on provisional justification. The Appellate Body found, among other things, that Panama failed to demonstrate that the Panel erred in finding that the measures were designed to secure compliance with Argentine laws, and were relevant. Neither party appealed the Panel’s findings on the chapeau.

### ***Note from Brendan McGivern, head of the World Trade Organization (WTO) practice of the White & Case LLP and Executive Partner of the Firm’s Geneva office.***

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